IV. Bilateral Negotiations

A. The Americas

1. Canada

Canada is the largest trading partner of the United States with over $1 billion of two-way trade crossing our border daily. At the same time, the United States and Canada share one of the world's largest bilateral direct investment relationships. In 2000, the stock of U.S. foreign direct investment in Canada was $126.4 billion, an increase of 13.8 percent from 1999. In 2000, the stock of Canadian direct foreign investment in the United States was $100.8 billion, an increase of 31.7 percent.

a. Softwood Lumber

On April 2, 2001, one day after the expiration of the 1996 U.S.-Canada Softwood Lumber Agreement, the Coalition for Fair Lumber Imports filed both antidumping and countervailing duty petitions. Affirmative preliminary determinations by the Department of Commerce ("Commerce") in both its countervailing duty and antidumping investigations resulted in provisional import duties being imposed on Canadian softwood lumber imports based on a net countervailable subsidy rate of 19.31 percent and an antidumping rate of 5.94 to 19.24 percent. Commerce's final determinations in the investigations are scheduled for late March 2002.

In August 2001, the United States received a request for WTO consultations from Canada regarding Commerce's preliminary countervailing duty determination. A WTO panel was established on December 5, 2001.

In July, 2001, Canada agreed to a constructive dialogue on softwood lumber issues. Federal and provincial officials have participated in this discussion to determine whether the United States and Canada can find a durable solution as an alternative to the litigation. The United States continues to seek a solution to the underlying concerns of this long-standing trade issue. Discussions with Canadian federal and provincial officials include reforms in provincial pricing practices, tenure systems, and mandated requirements.

b. Agriculture

Canada is the United States' second largest market for food and agricultural exports. For fiscal year 2001 (October 2000 - September 2001), U.S. agricultural exports to Canada grew by 6.5 percent to $8 billion.

As a result of the 1998 U.S.-Canada Record of Understanding on Agricultural Matters (ROU), the U.S.-Canada Consultative Committee (CCA) and the Province/State Advisory Group (PSAG) were formed to provide fora to strengthen bilateral agricultural trade relations and to facilitate discussion and cooperation on matters related to agriculture. In 2001, the CCA and PSAG met twice on issues covering livestock, grain, seed, and horticulture trade, as well as pesticide and animal drug regulations.

As a result of the ROU, U.S. feeder cattle exports from eight states to Canada continued to increase at a record pace in 2001 and are expected to set another record in 2002. Grain transshipped through Canada under an ROU program also continued to accelerate reaching 1 million tons in 2001.

Despite these accomplishments, the U.S. Government continues to have concerns about the marketing practices of the Canadian Wheat Board. On October 23, 2000, USTR initiated a Section

301 investigation of certain trade practices of the Canadian Wheat Board, in response to a petition filed by the North Dakota Wheat Commission. At the request of USTR, the ITC conducted an investigation on Canadian wheat marketing practices, and released its report in December 2001. USTR is scheduled to make a final determination on the 301 petition in February 2002.

On a related but separate track, the United States is seeking reforms to state trading enterprises as part of the WTO agricultural negotiations. The U.S. proposal calls for the end of exclusive export rights to ensure private sector competition in markets 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.

In April 1999, the United States successfully challenged Canada's subsidized dairy industry. A WTO panel found that the Canadian government, through its government-managed provincial marketing boards, was subsidizing the price of exported milk through a two-tiered pricing system. In light of this finding, the Panel also concluded that Canada had violated its export subsidy reduction commitments by exporting a higher volume of subsidized dairy products than permitted by Canada's obligations under the WTO Agreement on Agriculture. The Panel also found that Canada had improperly imposed a limit on the value of milk that could be imported in any single entry under the relevant tariff-quota. This finding was sustained by an appeal panel in October 1999.

Under a negotiated implementation agreement, Canada committed to bring its export regime into compliance with its WTO export subsidy commitments on butter, skimmed milk powder and an array of other dairy products, by January 31, 2001. Although Canada eliminated one export subsidy program in this process, new programs were substituted in nine provinces. Because the United States is concerned that the new measures appear to duplicate most of the elements of the export subsidies which they replace, the United States requested a panel be reconvened to review Canada's compliance. In July 2001, the compliance review panel agreed with the United States that Canada was not in compliance. However, Canada appealed the July report. On December 3, 2001, the Appellate Body determined that there was insufficient information to make a ruling. As a result, on December 18, the United States requested another compliance review panel in order to consider additional information. The compliance review panel is expected to issue a decision in spring 2002.

c. Intellectual Property Rights

The United States initiated a dispute on May 6, 1999 arguing that the Canadian Patent Act was inconsistent with the TRIPS Agreement as it did not provide for a patent term of at least 20 years from the date of application for all patents in existence on the date that Canada was obligated to comply with TRIPS. On September 18, 2000, the Appellate Body affirmed that Canada's law failed to provide the patent term guaranteed by TRIPS. The DSB adopted the reports of the panel and Appellate Body on October 12, 2000. The United States asked an arbitrator to determine the reasonable period of time for Canada to comply, and on February 28, 2001, the arbitrator determined that the deadline for compliance would be August 12, 2001. Effective July 12, 2001, Canada announced that it had enacted an amendment to its Patent Act to bring it into conformity with its obligations under the TRIPS Agreement.

2. Mexico

Mexico is our second largest single-country trading partner and has been among the fastest growing major export markets for goods since 1993, with U.S. exports up more than 144 percent through 2001. The potential of trade with Mexico is just beginning to be tapped, while the benefits to workers, consumers, farmers and firms are increasingly apparent. The NAFTA, now in its ninth year, has fostered this enormous relationship with its unprecedented comprehensive market opening rules. It is also creating a more equitable set of trade rules as Mexico's higher trade barriers are being reduced or eliminated. On January 1, 2002, the results of the Fourth NAFTA Accelerated Tariff Elimination Agreement were implemented, which eliminated duties on U.S. exports valued at $25 billion ahead of schedule. The United States has continued to seek improved access to the Mexican market in several other areas.

a. Intellectual Property Rights

Piracy and counterfeiting of U.S. intellectual property in Mexico continue to raise serious concerns. Over the past year, enforcement against piracy has declined dramatically, resulting in even greater losses for the U.S. copyright industries and the closure of legitimate copyright industry-related businesses in Mexico. Despite significant raiding efforts, only a small percentage of arrests have resulted in court decisions and deterrent penalties. Both the U.S. pharmaceutical and agrochemical industries also have expressed concern regarding the confidentiality of data submitted in conjunction with applications for marketing approval.

b. Agriculture

North American agricultural trade has grown significantly since the NAFTA. Mexico is currently the United States' third largest agricultural export market. For fiscal year 2001 (October 2000-September 2001), U.S. agricultural exports to Mexico grew by 15.4 percent to $7.3 billion, the highest value ever, with value-added consumer agricultural products surging 30 percent to an all-time high.

Current trade irritants include Mexico's limits on the importation and domestic consumption of high fructose corn syrup (HFCS). In 1997, Mexico initiated an antidumping investigation and in 1998 imposed antidumping duties. The United States challenged Mexico's determination in the WTO. The panel ruled in favor of the United States in January 2000. Mexico did not appeal. In September 2000, Mexico issued a new determination that purported to comply with the original panel decision. The United States challenged the new determination and in June 2001 the panel ruled in our favor. Mexico appealed the panel's decision. The Appellate Body rejected Mexico's appeal on October 22 and on November 21, 2001, the WTO adopted the Appellate Body's report.

In other agricultural sectors, the United States and Mexico continue to seek to resolve a dispute over the NAFTA's sugar provisions. In May 2001, the United States and Mexico reached agreement to improve Mexico's administration of its tariff rate quota on U.S. dry bean exports ensuring the United States' full access under the NAFTA to the Mexican dry bean market. Following WTO consultations with the United States regarding Mexico's antidumping investigation of U.S. slaughter hog imports from the United States, Mexico self-initiated a review of the dumping order. A preliminary resolution was issued in June 2001, and a final resolution is expected soon. On April 28, 2000, Mexico announced final antidumping duties on imports of U.S. beef (boneless, bone-in and carcasses). The final antidumping margins are, in many cases, lower than those in the July 27, 1999 preliminary determination, but remain a concern to the United States. In June 2000, the Mexican Congress passed a law that imported beef was to be inspected in Mexico. Because Mexico does not have sufficient facilities to handle the volume of imports and trade would have been severely disrupted, Mexico granted a delay on implementation of the law until June 2002.

In 2001, the Administration continued to address a number of Mexican sanitary and phytosanitary measures. Of particular note, in summer 2001, the Administration negotiated a resolution to phytosanitary measures impeding shipments of California tree fruit. Working with affected industries to address these and other problems as they arise will continue to be a high priority, particularly given the importance of continued growth in export opportunities for U.S. agricultural producers.

c. Telecommunications

Market barriers in Mexico's telecommunications sector remain a serious source of concern. In particular, through a series of rules and other measures, Mexico does not permit effective competition and otherwise discriminates against U.S. suppliers of basic telecommunications services. As a result, wholesale telecommunications rates for U.S.-Mexico calls are still roughly four times their cost. These high rates cost U.S. companies and consumers about $600 million in excess payments a year.

The United States initially requested WTO consultations with Mexico on telecommunications issues in August 2000 and first requested the establishment of a WTO panel in November 2000. At that time, Mexico took steps to address several important barriers to telecommunications trade. However, relevant Mexican agencies have not yet addressed trade barriers affecting international telecommunications services. The United States expects to file a new request for establishment of a WTO panel in early 2002 that specifically addresses this issue.

3. Brazil and Southern Cone

a. Mercosur (Argentina, Brazil, Paraguay and Uruguay)

The Common Market of the South, referred to as "Mercosur," from its Spanish abbreviation, is the largest preferential trade agreement in Latin America. It consists of Brazil, Argentina, Uruguay and Paraguay and represents over half of Latin America's gross domestic product. Chile and Bolivia are Associate Members of the group. Mercosur was established in 1991, with the goal of creating a common market. Implementation of the Mercosur customs union commenced January 1, 1995, with the establishment of a common external tariff (CET), covering some 85 percent of intra-Mercosur trade. Convergence on excepted items is slated for completion by January 1, 2006.

Four Plus One: In September 2001, the United States and the four Mercosur countries resumed meeting under the auspices of the 1991 Rose Garden Agreement. This agreement created a framework, known as the Four Plus One, for the United States and the Mercosur countries to discuss means to deepen their trade relationship. At the September ministerial meeting, the Four Plus One agreed on a work plan and a series of meetings to discuss coordination in multilateral fora, such as the FTAA and the WTO and bilateral trade and investment issues of mutual interest.

b. Argentina

U.S. exports to Argentina were 4.0 billion in 2001, and Argentina remained in the top 30 export markets of the United States. Overall bilateral trade was $7.0 billion, and the U.S. surplus narrowed by $0.6 billion to $1.0 billion in 2001. A key factor in the Argentine economy is its trade with Brazil, Argentina's number one trading partner.

During 2001, the United States pursued resolution of existing trade disputes, such as the dispute involving Argentina's inadequate patent and data protection regimes.

Agriculture: After several years of technical discussions, in January 2001, Argentina signed the protocol allowing entry of U.S. exports of both in-bone and boneless pork.

Intellectual Property Rights (IPR): Argentina's intellectual property rights regime does not yet appear to meet TRIPS standards and fails to fulfill long-standing commitments to the United States. Grave concerns regarding Argentina's IPR regime, particularly with respect to patent protection, have led USTR to maintain Argentina on the Special 301 "Priority Watch List" since April 1998. In 1997, the United States withdrew 50 percent of Argentina's benefits under the Generalized

System of Preferences (GSP) over this same issue, and benefits will not be restored unless the concerns of the United States are addressed adequately.

Despite U.S Government efforts, intellectual property protection continued to deteriorate. In May of 1999, the United States initiated a WTO case against Argentina because of its failure to protect patents and test data. The United States added additional claims to this case in May of 2000, due to the fact that the TRIPS Agreement became fully applicable for Argentina in the year 2000. The United States has engaged in a series of consultations with Argentina in Geneva throughout 2001. To date, the two countries have been unable to find a fully satisfactory solution. Argentina's copyright laws are currently under review by the Executive Branch.

c. Brazil

The United States exported goods valued at $16.3 billion to Brazil in 2001. Brazil's market accounts for 27 percent of U.S. annual exports to Latin America and the Caribbean excluding Mexico, and 66 percent of U.S. goods exports to Mercosur.

Intellectual Property Rights (IPR): In 1997, Brazil enacted laws providing protection for computer software, copyrights, patents and trademarks. The United States has identified certain problems with some of this legislation, including a local working requirement and extensive exceptions to a prohibition on parallel imports in the patent law. U.S. industry has also voiced concerns about the high levels of piracy and counterfeiting in Brazil and the lack of effective enforcement of copyright (especially for sound recordings and video cassettes) and trademark legislation. In 2001, the International Intellectual Property Association (IIPA) filed a petition to remove Brazil's GSP benefits due to its failure to offer adequate protection to copyrighted materials, in particular sound recordings. The petition remains under review.

On April 30, 2000, the United States requested that the WTO establish a dispute resolution panel to review a narrow part of Brazil's patent law referred to as a local manufacturing requirement. Article 68(1)(I) of the law provides that if a patented product is not being manufactured in Brazil within three years of the issuance of the patent, the government may compel the patent owner to license a competitor. However, Article 27.1 of the TRIPS Agreement provides that patents may be used without discrimination as to " . . . whether the products are imported or locally produced." The United States continues to question the consistency of this provision under the obligations of the TRIPS Agreement, which prohibits such conditions.

In June 2001 the United States and Brazil agreed to transfer their WTO disagreement over Brazil's patent law from formal WTO litigation to a newly created bilateral consultative mechanism. Under the terms of the agreement, Brazil will provide advance notice to the U.S. Government before utilizing Article 68 (1)(I). If Brazil seeks to activate this provision there will be an adequate opportunity for consultations in the bilateral Consultative Mechanism. This will provide an early warning system to protect U.S. interests. The United States reserved all its rights in the WTO with respect to this matter.

Autos: In March 1998, USTR signed an agreement with the Government of Brazil to terminate its TRIMS-inconsistent (Trade-Related Investment Measures) auto regime, enacted in December 1995. The regime had offered auto manufacturers reduced duties on imports of assembled cars and auto parts and other benefits if they exported sufficient quantities of parts and vehicles and promised to meet local content targets in their Brazilian plants. The Brazilian Government committed to eliminate the trade and investment distorting measures in its auto regime and not to extend the measures to its Mercosur partners when their auto regimes were unified in 2000. Argentina and Brazil recently reached agreement on a new regime, which remains TRIMS-inconsistent. Argentina requested a WTO TRIMS extension, which was granted.

Wheat: In March 2001, the United States and Brazil reached agreement on a phytosanitary protocol to allow entry of certain U.S. wheat shipments.

d. Paraguay

With a population of just over five million, Paraguay is one of the smaller U.S. markets in Latin America. In 2001, the United States exported only $401 million worth of goods to Paraguay. However, Paraguay is a major exporter of and a transshipment point for pirated and counterfeit products in the region, particularly to Brazil.

Intellectual Property Rights (IPR): In January 1998, the USTR identified Paraguay as a "Priority Foreign Country" (PFC) under the "Special 301" provisions of the Trade Act of 1974. In identifying Paraguay as a PFC, the USTR noted deficiencies in Paraguay's intellectual property regime, especially a lack of effective action to enforce IPR. As required under the Trade Act of 1974 as amended, the USTR initiated an investigation of Paraguay in February 1998.

During negotiations under Special 301, the Government of Paraguay indicated that it had undertaken a number of actions to improve IPR protection, such as passing new copyright and trademark laws and undertaking efforts to improve enforcement. In November 1998, in light of commitments made by the Government of Paraguay in a bilateral Memorandum of Understanding (MOU), USTR concluded its Special 301 investigation. The Government of Paraguay committed to take a number of near-term and longer-term actions to address the practices that were the targets of the investigation, including implementing institutional reforms to strengthen enforcement and taking immediate action against known centers of piracy and counterfeiting. The U.S. Government is currently monitoring Paraguay's implementation of the MOU.

e. Uruguay

With the smallest population of Mercosur (just over three million), Uruguay nonetheless imported over $417 million of goods from the United States in 2001. Areas of recent consultation have included coordinating U.S efforts in multilateral fora such as the FTAA and WTO and the importance of Uruguay's apparent failure to bring its intellectual property regime into line with TRIPS standards by January 1, 2000.

f. Chile

Chile is our 32nd largest export market, purchasing nearly $3.2 billion in U.S. exports in 2001. Chile has been a recognized leader of economic reform and trade liberalization in Latin America, with real GDP growth averaging eight percent for the decade prior to Chile's economic slowdown in 1998-99. Chile's real GDP grew by more than 3 percent in 2001. As a resource-based, export-dependent economy, Chile was seriously affected by the global drop in commodity prices. In addition, continued sluggishness in the economies of Mercosur, particularly Argentina, a major destination for Chilean exports, contributed to slower Chilean growth in 2001.

Chile FTA

In December 1994, the United States, Canada and Mexico announced their intention to negotiate Chile's accession to NAFTA. Several negotiating rounds were held in 1995. However, Chile withdrew from the negotiations due to concerns at that time about the absence of fast track negotiating authority. Chile subsequently negotiated a bilateral FTA with Canada (Chile already had a bilateral agreement with Mexico). In 1998, United States initiated the U.S.- Chile Joint Commission on Trade and Investment, which led to increasingly ambitious work programs in areas including services, government procurement, investment, environment, business visas, norms and standards, labor, and civil society. On November 29, 2000, the United States and Chile announced their agreement to initiate immediately negotiations for a U.S.-Chile Free Trade Agreement.

In 2001, there were eight negotiating rounds towards a comprehensive bilateral free trade treaty. Following the December round of talks, both parties agreed to another round of talks in January 2002 and committed to concluding the agreement in early 2002.

4. The Andean Community

The U.S. trade deficit with the Andean region decreased from $17.8 billion in 2000 to $12.9 billion in 2001. U.S. goods exports to the region were up 4.6 percent in 2001, totaling $12.7 billion.

The Andean Community originated as the Andean Pact in 1969, with Bolivia, Colombia, Ecuador, Peru and Venezuela as its members. However, it was only in the 1990s that the Andean Pact's commitment to form a customs union took on momentum, with the reduction and elimination of most duties among the members and an increasingly common external tariff. In 1997 the Andean Community became operational. Among its features are strengthened institutions, such as a Council of Presidents and a Council of Foreign Ministers in addition to meetings of Trade Ministers, and creation of a General Secretariat of the Andean Community mandated to act as the group's executive body.

a. Andean Trade Preference Act

The Andean Trade Preference Act (ATPA) of 1991 authorized the President to provide reduced-duty or duty-free treatment to most imports from Bolivia, Colombia, Ecuador and Peru. It was intended to help the four beneficiary countries expand economic alternatives in their fight against drug production and trafficking. The Administration strongly supports renewal of the ATPA and expansion of the program to additional products. During November 2001, the U.S. House of Representatives approved a bill for ATPA expansion and renewal, and the Senate Finance Committee approved its version of the bill.

Unfortunately, the original ATPA program expired on December 4, 2001, before a new program was in place. The Administration remains firmly committed to working with Congress to achieve ATPA renewal and expansion as soon as possible.

b. Intellectual Property Rights

In the area of intellectual property, the Andean Community countries have developed common disciplines with legal effect throughout the Community. The U.S. Government is in the process of analyzing the revised legislation with regard to WTO TRIPS compatibility. Of particular concern is an Andean Tribunal decision calling on Peru to invalidate a pharmaceutical patent on the basis that it represented a "second use" innovation. Both the U.S. pharmaceutical and agrochemical industries are also concerned that Andean laws are not sufficiently explicit regarding the confidentiality of data submitted in conjunction with applications for marketing approval.

During 2001 Ecuador was removed from the Special 301 Watch List, while the other four Andean countries are on the Watch List. In general, piracy levels in the region are high and while enforcement efforts have improved somewhat, they remain inadequate.

5. Central America and the Caribbean

a. Caribbean Basin Initiative (CBI)

The trade programs known collectively as the Caribbean Basin Initiative (CBI) remain a vital element in the United States' economic relations with its neighbors in Central America and the Caribbean. Initially launched in 1983 through the Caribbean Basin Economic Recovery Act, and substantially expanded in 2000 through the U.S.-Caribbean Basin Trade Partnership Act (CBTPA), the CBI currently provides 24 beneficiary countries with duty-free access to the U.S. market for most goods. In 2001, U.S. imports from the CBI region totaled $21.2 billion, with U.S. exports amounting to $21.2 billion.

Ongoing implementation of the CBTPA was an important Administration objective for the Caribbean Basin region during 2001. The CBTPA provided expanded preferential treatment for a range of products, including certain apparel, which had previously been excluded from CBI coverage. As of late 2001, it was clear that these new provisions were being used extensively by CBI countries and U.S. importers, with nearly 25 percent of total U.S. imports from the CBI region entering under the enhanced preference provisions. At the same time, it has been apparent that implementation of the CBTPA has been characterized by certain challenges, particularly with respect to the application of statutory provisions in the technical rules governing imports under the new preferences. The Administration will continue to work with Congress, the private sector, CBI beneficiary countries, and other interested parties to ensure a faithful and effective implementation of this important expansion of trade benefits.

The Administration also continued during 2001 to engage with CBI beneficiary countries in connection with the policy objectives established as eligibility criteria under the CBI statutes. In the March-May period, the U.S. conducted a focused review of labor practices in Guatemala, linked to that country's eligibility under both the CBI and Generalized System of Preferences programs. During the course of the review, Guatemala enacted important reforms to its labor laws, engaged directly with a special mission of the International Labor Organization, and committed to stronger efforts to enforce labor law provisions. The U.S. review was suspended in May 2001 with positive note of these actions; the U.S. also indicated that it would continue to monitor closely labor practices in Guatemala. In July 2001, the U.S. also participated in bilateral consultations with the governments of El Salvador, Honduras, and Nicaragua regarding labor practices.

In December 2001, USTR released its 4th Report to Congress on the Operation of the Caribbean Basin Economic Recovery Act. This biennial report summarizes the main provisions of the Caribbean Basin Initiative, reviews regional and bilateral trade trends under the CBI programs, and reflects an overview of the performance of beneficiary countries with respect to the CBI eligibility factors. The report is available on-line at www.ustr.gov.

b. Central America

The United States remains Central America's principal trading partner. The Central American Common Market (CACM) consists of Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua, and provides duty-free trade for most products traded among these countries. Panama, which has observer status, and Belize participate in CACM summits but not in regional trade integration efforts. As a group, the countries of the CACM exported a total of $9.1 billion of goods to the United States in 2001, importing $11.1 billion of U.S. goods. The CACM is an internal market of 33 million people with a combined GDP of over $50 billion. GDP per capita varies widely within the Central American region, with the relatively developed service-oriented economy of Panama registering an estimated $2,316 per capita. At the other extreme, Nicaraguan GDP per capita was only $517. Furthermore, these figures do not capture the broad disparities of income evident within most Central American countries.

During 2001, the CACM countries publicly expressed an interest in pursuing free trade negotiations with the United States. In September, USTR convened a meeting with representatives of these countries to explore ways of deepening trade policy engagement between the United States and Central America. That meeting produced an agreement to pursue a series of technical workshops on trade policy issues, which will continue into mid-2002.

In December, the Administration convened a meeting of the U.S.-Panama Trade and Investment Council, with the aim of exploring Panama's interest in expanding its bilateral trade relationship with the United States.

Central American countries continued during 2001 to pursue a range of bilateral and regional trade agreements. Costa Rica signed a free trade agreement with Canada in April, and negotiations between Canada and the other CACM members countries (El Salvador, Guatemala, Honduras, and Nicaragua) began late in the year. Negotiations for a Panama-CACM free trade agreement led to conclusion of work on common disciplines, with work continuing on negotiation of related market access provisions. In several Central American countries, work continued towards ratification of previously-negotiated agreements with Chile, Mexico, and the Dominican Republic.

All of the countries of the region are participating in the Free Trade Area of the Americas (FTAA) negotiations. Central American countries take an active role in the negotiating process. In the May 2001 to October 2002 phase of negotiations, Guatemala chairs the Negotiating Group on Agriculture, Costa Rica chairs the Negotiating Group on Government Procurement, and Nicaragua serves as Vice Chair of the Consultative Group on Smaller Economies.

During the course of 2001, the United States consulted regularly with Central American trade officials, including in the context of the FTAA and Summit of the Americas processes. The United States Trade Representative met with his counterparts from the region at the April 2001 FTAA Ministerial in Buenos Aires, and held additional, individual meetings with the region's trade ministers throughout the year.

Agriculture

Tariff and non-tariff barriers to U.S. agricultural exports are among the biggest U.S. trade policy concerns in Central America. Several countries in the region, including Costa Rica, Nicaragua and Panama, have recently raised tariffs on agricultural products, although they are still within WTO-bound rates. Panama's practices with respect to issuance of sanitary and phytosanitary licensing, often linked to local buying requirements, have been a matter of concern; the United States has pursued these concerns with the Government of Panama, and some improvement was seen by the end of 2001.

Intellectual Property Rights (IPR)

In general, the legal framework for protection of intellectual property has improved in Central America in recent years, although concerns remain, particularly in the area of enforcement. Enforcement-related issues were the principal factor leading to USTR's placement of Costa Rica on the Special 301 Priority Watch List in 2001. Both El Salvador and Honduras, however, are considering a number of TRIPS-conforming amendments to their respective IPR legal frameworks, while in 2001 Guatemala appointed a specialized prosecutor for intellectual property matters.

c. The Caribbean

CARICOM: Countries in the Caribbean region include members of the Caribbean Community and Common Market (CARICOM) and the Dominican Republic. Current members of CARICOM are: Antigua and Barbuda, the Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname and Trinidad and Tobago. In theory, CARICOM is a customs union rather than a common market. However, progress towards a customs union has been limited.

CARICOM countries have played an active role in the FTAA process, which has provided an opportunity for frequent bilateral interaction between U.S. and Caribbean trade officials. During the May 2001 to October 2002 phase of the FTAA negotiations, Bahamas is chairing the Negotiating Group on Services, and Dominican Republic chairs the FTAA Committee of Government Representatives on the Participation of Civil Society.

Agriculture

The Caribbean countries, Barbados and the Dominican Republic in particular, have made significant advances in lowering tariffs in advance of their WTO reduction schedule. However, many countries, including Trinidad and Tobago, the Bahamas, Jamaica, and Barbados have increased the use of non-tariff barriers such as arbitrary customs valuation, domestic absorption requirements and discretionary import licensing practices to stem the flow of imports and make up for lost government revenues due to lower tariffs.

Other Caribbean Countries

The Dominican Republic, the largest beneficiary of the Caribbean Basin Initiative program, does not belong to any regional trade association, but has increased cooperation with both Central America and CARICOM. In July 2001, the Dominican government implemented its commitments under the WTO Customs Valuation Agreement. The United States has expressed concerns about the Dominican Republic's Industrial Property law which appears to fall short of certain basic requirements of the WTO TRIPS Agreement, and the U.S. and Dominican governments have engaged in consultations on these issues. The U.S. has also raised concerns regarding possibly discriminatory effects of certain excise tax increases implemented by the Dominican Republic in late 2000.

B. Western Europe

Overview

The U.S. economic relationship (measured as trade plus investment) with Western Europe is the largest and most complex on earth. Due to the size and nature of the transatlantic economic relationship, serious trade issues inevitably arise on occasion. Sometimes small in dollar terms, especially compared with the overall value of transatlantic commerce, these issues can take on significant importance as potential precedents for broader U.S. trade policies.

From its origins in the 1950s, the EU has grown from six to fifteen Member States, with Austria, Finland, and Sweden becoming the newest EU members states on January 1, 1995. These fifteen countries together comprise a market of some 370 million consumers with a total gross domestic product of more than $8 trillion. U.S. goods exports to the EU totaled $165.1 billion in 2000, second only to Canada. Since 1994, U.S. goods exports to the EU have increased 53 percent.

The other major trade group within Western Europe is the European Free Trade Association (EFTA), which, through 1994, included Austria, Finland, Iceland, Liechtenstein, Norway, Sweden, and Switzerland (Austria, Finland, and Sweden ceased EFTA membership upon their accession to the EU). Formed in 1960, EFTA provides for the elimination of tariffs on manufactured goods and select agricultural products that originate in, and are traded among, its Member States.

In late 1991, the EFTA countries and the EU formed the European Economic Area (EEA), designed to strengthen significantly the free trade agreement already in place between the two groups. Switzerland rejected the EEA in a referendum at the end of 1992. A revised EEA (excluding Switzerland) took effect on January 1, 1994. In practice, the EEA involves adoption by the EFTA signatories of approximately 70 percent of EU legislation.

2001 Activities

In 2001, the EU intensified its efforts to deepen the economic and political integration of its Member States. The pace of additional Western European integrative efforts over the next few years is being set first by the experience of implementing the Economic and Monetary Union (EMU) established by the EU's Maastricht Treaty, which went into force on November 1, 1993, and amendments to Maastricht contained in the 1997 Amsterdam and 2000 Nice Treaties. Under the Maastricht Treaty schedule, eleven Member States on January 1, 1999 launched in earnest the EMU program, the most prominent feature being the introduction of the new European single currency (the "euro"), which replaced national currencies in participating Member States on January 1, 2002.

The second major factor affecting the pace of European integration will be the process of enlarging the EU to include new members to the East and South. The EU has signed association agreements and other types of free trade arrangements with the Czech Republic, Slovakia, Hungary, Poland, Bulgaria, Romania, Latvia, Lithuania, Estonia, Albania, Slovenia, Israel, Algeria, Morocco, and Tunisia. The EU has also negotiated a customs union with Turkey. In November 1998, the EU formally launched substantive accession negotiations with six "first-tier" candidate countries: Poland, the Czech Republic, Hungary, Slovenia, Estonia and Cyprus. In late 1999, the EU declared it also would begin formal negotiations for accession with Slovakia, Romania, Bulgaria, Lithuania, Latvia, and Malta (Turkey remains an accession candidate, with no EU commitment to commence formal negotiations). Important institutional questions associated with EU enlargement still need to be resolved before enlargement can take place. No firm target has been set for completing any of the accession negotiations and some candidate states have expressed concern that the process could last for a number of years.

In 2001, USTR devoted considerable resources to addressing pressing or potential trade problems with the EU and its individual Member States, as well as to efforts to enhance the transatlantic economic relationship. As part of our ongoing dialogue with the European Union under the Transatlantic Economic Partnership (TEP) during 2001, we negotiated a Mutual Recognition Agreement (MRA) on marine equipment and are nearing completion on guidelines for more effective transatlantic regulatory cooperation and transparency. We have resolved the long-standing bananas dispute and continued efforts to reach an understanding with the EU that would lead to EU compliance with the WTO dispute settlement ruling on beef, as well as other bilateral trade problems. In addition, with respect to the WTO ruling in the Foreign Sales Corporation (FSC) case, we will work to resolve the situation and to ensure that this issue does not seriously damage our overall bilateral relationship.

USTR activity on a bilateral basis with respect to the EFTA states in 2001 was modest, though the EFTA EEA states have continued to make inquiries concerning possibilities for further regulatory cooperation.

1. Transatlantic Economic Partnership

At the May 1998 U.S.-EU Summit in London, the President and EU Leaders announced the Transatlantic Economic Partnership (TEP) initiative, which seeks to deepen and systematize the cooperation in the trade field launched under the New Transatlantic Agenda process begun in 1995. In the TEP, the two sides identified a number of broad areas in which they committed to work together in order to increase trade, avoid disputes, address disagreements, remove barriers, and achieve mutual interests. These areas include: technical barriers to trade, agriculture, intellectual property, government procurement, services, electronic commerce, environment and labor. In addition, the United States and EU agreed to put an emphasis throughout the initiative on shared values, i.e., they agreed to more fully involve citizens and civil society on both sides of the Atlantic in trade policy so as to strengthen the consensus for open trade. Cooperation under the TEP occurs with respect to bilateral matters, as well as in the context of multilateral activities such as in the WTO. The TEP Action Plan, endorsed by Leaders at the December 1998 U.S.-EU Summit in Washington, lays out specific goals under each of the above categories. At the June 1999 U.S.-EU Summit, U.S. and EU leaders agreed to use TEP mechanisms to carry out part of a joint effort to identify – and hopefully defuse – potential trade problems at an early stage, before they become irritants to the bilateral economic relationship.

Public Dialogues: Important companions to the Transatlantic Economic Partnership initiative are the various private dialogues among European and American businesses, labor organizations, and environmental and consumer groups. The first of these to be established, the Transatlantic Business Dialogue (TABD), is a forum in which American and European business leaders can meet to discuss ways to reduce barriers to U.S.-European trade and investment. Other dialogues – the Transatlantic Labor Dialogue (TALD), the Transatlantic Consumer Dialogue (TACD), and the Transatlantic Environment Dialogue (TAED) – start from a similar premise, i.e., that corresponding organizations on both sides of the Atlantic should share views and, where possible, present joint recommendations to governments in both the United States and the EU on how to improve transatlantic relations and to elevate the debate among countries in multilateral fora. The dialogues have forwarded recommendations related to trade policy issues to governments on both sides of the Atlantic.

2. Standards, Testing, Labeling, and Certification

A process of harmonization of technical regulations and product standards is underway within the EU. Given assessments that EU legislation covering regulated products eventually may affect half of all U.S. exports to Europe, EU legislation and standardization work in the regulated areas is of considerable importance. Although there have been improvements in some respects, a number of problems related to this evolving EU-wide regulatory process continue to cause concerns for U.S. exporters. Among these concerns are: inadequate transparency in the EU rulemaking process; lags in the development of EU standards and harmonized legislation for regulated areas; inconsistent application and interpretation by Member States of the legislation that is in place; overlap among directives dealing with specific product areas; gray areas among the scope of various directives; and unclear or unnecessary marking and labeling requirements for these regulated products before they can be placed on the market.

In December 1998, the United States and the EU began implementation of the U.S.-EU Mutual Recognition Agreement (MRA) in sectors representing more than $50 billion of annual two-way trade. The MRA is designed to reduce duplicative conformity assessment procedures, while maintaining our current high levels of health, safety, and environmental protection. Once fully implemented, the MRA will permit U.S. exporters to conduct required conformity assessment procedures (such as product testing and inspection) in the United States according to EU requirements, and vice versa. The sectors covered by the current MRA include: telecommunications and information technology equipment; network and electromagnetic compatibility (EMC) for electrical products; electrical safety for electrical and electronic products; good manufacturing practices (GMP) for pharmaceutical products; product evaluation for certain medical devices; and safety of recreational craft. The recreational craft annex entered the operational phase in June 2000, and the telecommunications equipment and EMC annexes entered the operational phase in January 2001.

Over the past year, the United States continued work to enhance regulatory cooperation and reduce unnecessary technical barriers to transatlantic trade. Under the Transatlantic Economic Partnership (TEP), the United States and EU advanced our bilateral regulatory cooperation workplan in 2001 by negotiating a path-breaking MRA on marine equipment, which should take effect in mid-2002. We also made substantial progress on U.S.-EU guidelines for effective regulatory cooperation and more transparent regulatory procedures. These guidelines will serve as a framework for pursuing possible bilateral regulatory cooperation projects.

3. Telecommunications

Europe is in the process of implementing wide-ranging liberalization and harmonization in its telecommunications services market and is undergoing a process to update its telecommunications legislation. The EU and the Member States, with limited exceptions, committed to provide market access, national treatment, and fair regulatory practices as part of the WTO Basic Telecommunications Agreement. Greece, Ireland, Portugal, and Spain made subsector-specific reservations in the WTO agreement, mirroring derogations granted under EU law that permit an extra one to five years before the introduction of competition. Ireland and Spain abandoned these derogations and, as of January 1, 1999 and December 1, 1998 respectively, opened their markets to full competition. Portugal and Greece abandoned their derogations at the end of 2000.

The record of implementation under the agreement so far is mixed. Many Member States have licensed new entrants, and have taken steps necessary to compel former monopolies to meet pro-competitive obligations set forth in the WTO Agreement. The European Commission proposed, and the Council and Parliament approved, a Regulation to make local loop unbundling mandatory by January 1, 2001. However, some governments have been slow to adopt or put in place the legislative and regulatory mechanisms necessary to implement EU directives. The European Commission's competition directorate has taken an active stance in bringing actions for noncompliance with EU directives in order to compel implementation. In December 2001, the European Commission decided to open legal proceedings against Germany, Greece, and Portugal for failing to open their local telephone services fully to competition.

The EU is also in the process of privatizing state-owned telecommunications firms, but in some countries, this process has proceeded slowly. About half the incumbent operators in EU Member States continue to have government ownership, including France, Germany, Austria, Belgium, Luxembourg, Sweden, Finland, and Greece.

The United States continues to work closely with the EU to monitor how EU Member States are addressing these issues.

4. Aircraft

In January 2001, the United States and the European Union held consultations concerning the potential provision of EU government financial assistance for the Airbus A380 jetliner project and other issues regarding trade in large civil aircraft. In April 2001, the European Commission provided notification that seven Member States had made commitments to provide government loans for part of the development costs for the Airbus A380 aircraft. The United States reviewed the transparency data provided by the EU and requested supplemental information regarding the terms and conditions of such financing to ensure that it would be consistent with the EU's obligations under the *1992 U.S.-EU Agreement Concerning the Application of the WTO Agreement on Trade in Civil Aircraft* and the *WTO Agreement on Subsidies and Countervailing Measures.* In January 2002, the EU and the United States held another round of aircraft consultations during which the U.S. sought additional details on support for the A380.

5. Foreign Sales Corporation Tax Rules

Potentially the most damaging of the trade disputes currently involving the U.S. and the EU is the EU's complaint to the WTO that the U.S. Foreign Sales Corporation (FSC) tax rules are an illegal export subsidy. The United States lost this case on appeal in Spring 2000, but repealed the FSC law and enacted new legislation in November to correct the shortcomings identified in the dispute. Though the United States and the EU agreed in September 2000 on procedures that would permit WTO legal review of the new legislation, the EU nonetheless requested permission ultimately to retaliate against up to $4 billion in U.S. exports should the new measure be found inconsistent with WTO rules, as the EU charged. On January 14, 2002, the WTO review was completed, resulting in a finding that the new legislation is WTO-inconsistent. In the U.S. view, the EU's WTO challenge does not arise out of substantive commercial problems identified by EU businesses. To the extent that European industry has spoken out on this issue, it has been to counsel against escalation and confrontation and to urge a reasonable settlement of the dispute.

6. Ban on Growth Promoting Hormones in Meat Production

The EU continues to ban the import of U.S. beef obtained from cattle treated with growth-promoting hormones. In 1996 the United States challenged the EU ban on U.S. beef in the WTO. In June 1997, a WTO panel found in favor of the United States on the basis that the EU's ban was inconsistent with the EU's obligations under the WTO Agreement on the Application of Sanitary and Phytosanitary Measures (SPS Agreement) because the ban was not based on a scientific risk assessment. In January 1998, the WTO Appellate Body upheld the panel's finding that the EU's ban on imported meat from animals treated with certain growth-promoting hormones is inconsistent with obligations under the WTO SPS Agreement. In 1999, the WTO authorized U.S. trade retaliation because the EU failed to comply with the WTO rulings by the May 13, 1999 deadline. In July 1999, the United States applied 100 percent duties on $116.8 million of U.S. imports from the EU after receiving WTO authorization. The United States is currently engaged in discussions with the EU on the possibility of reducing the level of retaliation in exchange for improved market access for U.S. non-hormone treated beef.

7. Agricultural Biotechnology

a. Approvals Process for Agricultural Biotechnology Products

In the past the EU approved several U.S. agricultural biotech products. However, no U.S. products have been approved since Member States imposed a moratorium on the approval of agricultural biotechnology products in June 1998, resulting in the loss of $200 million in U.S. exports of corn to the EU annually. Restarting the approvals process is a high priority for the United States in order to restore these exports. Although European Commission officials made statements suggesting the EU might restart the process in 2001, the moratorium remains in place, and the Commission does not appear to have a strategy for resolving this issue. Both sides agreed in 1998 to establish a Biotechnology Group under the Transatlantic Economic Partnership to identify and address regulatory issues regarding the approvals process. Initially, the activities of this group served to increase understanding between the Commission and the United States officials. However, there was little progress in 2001. The U.S. Government continues to raise its concerns regarding the failure of the EU to have a functioning approval process.

b. European Commission Proposals on Traceability and Labeling

In July 2001, the Commission issued proposals on traceability and labeling of agricultural biotechnology products. These proposals are subject to a co-decision process involving the European Parliament and the European Council, which is expected to take at least 18 months. The proposals cover a range of products, including animal feed, with the potential of disrupting nearly $4 billion in U.S. exports to the EU. The United States has carefully reviewed the proposals and considers them unworkable, overly expensive, and subject to fraud. In addition, the U.S. does not believe the proposals will enhance food safety. In December 2001, the United States submitted detailed comments to the Commission outlining specific concerns about the proposals and seeking clarification. The U.S. has offered to work with the Commission, the Parliament, the Council, and the Member States in developing a better understanding of these proposals and avoiding potential trade disruptions.

8. Veterinary Equivalence

As a part of the Single Market initiative in 1992, the EU harmonized its animal and public health standards among Member States. In harmonizing these standards, the EU introduced new import controls for animal and animal products that threatened to disrupt U.S. exports to the EU. On April 30, 1997, USDA announced that the United States and the European Union had reached an agreement on an overall framework for recognizing each other's veterinary inspection systems as equivalent. The agreement is expected to open new opportunities for red meat exports and preserve most pre-existing trade in products such as pet food, dairy and egg products. Without this agreement, U.S. exports of some products, including egg products and dairy products, would have been blocked from the EU market unless U.S. industries invested in costly adjustments to their facilities to comply with each EU internal market requirement. The agreement, which covers $1 billion in U.S. animal and animal product exports to the EU and a slightly larger value of EU exports to the United States, was signed on July 20, 1999 and became effective on August 1. In June 2001, the Joint Management Committee created by the agreement met for the second time. Agreement was reached on establishing a Technical Working Group on Foot and Mouth Disease (FMD) which met for the first time in October to discuss the FMD outbreak in the EU. The two parties received a status report from the Technical Working Group on Audits and also discussed plant listings, antimicrobial treatments for poultry, regionalization and other issues of concern.

While conditions for trading poultry and poultry products will be less restrictive under the agreement, U.S. poultry plants using certain antimicrobial treatment are not able to ship to the EU. The EU will not accept use of certain antimicrobial treatments despite the fact that such treatments are an important element in modern poultry processing. The United States continues to explore with the EU ways of resolving this issue.

9. Wine

The U.S. and EU successfully launched wine negotiations in 1999 following several years of discussions concerning various market access problems. The negotiations became possible when, in response to U.S. insistence, the Council in December 1998 approved an extension of the existing derogations for U.S. wine making practices for five years or until an agreement is reached, whichever comes first. Commission and U.S. negotiators met several times during 1999-2001, most recently in June 2001, gaining valuable information about each other's regulatory systems for wine that will help them achieve a bilateral agreement. The United States continues to be concerned about the EU's requirements for the review and approval of wine making practices, and has questioned the EU's export subsidies on wine and domestic support programs benefitting its grape growers and wine producers. A major EU concern is the use of semi-generic names on some U.S. wines. Other issues include tariffs, the use of geographic indicators and certain other terms on labels, and import certification. The United States will continue to press the EU to give U.S. wine makers equitable access to the EU wine market. In late 2000 the EU Council agreed on new guidelines for EC negotiators. Negotiations are expected to accelerate in 2002.

C. Central Europe and the Newly Independent States

Overview

In order to ensure a permanent end to the Cold War, the United States has been actively supporting political and economic reforms in Central Europe (Poland, Hungary, Slovenia, the Czech Republic, Slovakia, Romania, Bulgaria, Estonia, Latvia, Lithuania, Croatia, Albania, Bosnia-Herzegovina, the Former Yugoslav Republic of Macedonia, and Serbia-Montenegro) and the Newly Independent States (NIS) (Russia, Ukraine, Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, Tajikistan, Turkmenistan, and Uzbekistan). The U.S. Government has been striving to construct a framework for the development of strong trade and investment links between the United States and Central Europe and the NIS. This approach has been pressed on both bilateral and multilateral fronts. Bilaterally, the United States has negotiated trade agreements to extend Normal Trade Relations (formerly referred to as "most-favored nation" or "MFN") tariff treatment to these countries and to enhance intellectual property rights protection. The United States also has extended Generalized System of Preferences (GSP) benefits to eligible countries and negotiated bilateral investment treaties (BITs) to guarantee compensation for expropriation, transfers in convertible currency, and the use of appropriate dispute settlement procedures. Multilaterally, the United States has encouraged accession to the WTO as an important method of supporting economic reform. Now that much of this framework is in place, USTR strives to ensure that Central Europe and the NIS satisfy their bilateral and multilateral trade obligations, as well as comply with U.S. trade laws and regulations, such as those governing eligibility for participation in the GSP program.

2001 Activities

1. Normal Trade Relations Status

Russia, Ukraine, and seven of the other NIS republics within the region receive conditional NTR tariff treatment pursuant to the provisions of title IV of the Trade Act of 1974, the so-called Jackson-Vanik amendment. As part of U.S. sanctions policy related to the conflict in the region, the President revoked NTR from Serbia-Montenegro (now the Federal Republic of Yugoslavia) in 1992. While certain sanctions against Serbia-Montenegro were lifted in 1996 pursuant to the peace accords negotiated in Dayton, Ohio, NTR tariff treatment was not restored.

Under the Jackson-Vanik amendment, the President is required to deny NTR tariff treatment to any non-market economy that was not eligible for such treatment in 1974 and that the President determines denies or seriously restricts or burdens its citizens' right to emigrate. This provision is subject to waiver, if the President determines that such a waiver will substantially promote the legislation's objectives. Alternatively, the President can determine that an affected country complies fully with the legislation's emigration requirements and report on this status semi-annually. Affected countries must also have a trade agreement with the United States, including certain specified elements to obtain conditional NTR status.

The President has determined that Russia, Ukraine and all of the other NIS republics, with the exception of Belarus; are in full compliance. Belarus continues to receive NTR tariff treatment under annual waivers. Congress must enact a law to terminate application of Title IV to a country. In 2000, pursuant to specific legislation, the President terminated application of Title IV to the Kyrgyz Republic, Albania and Georgia. The Administration is currently consulting with the Congress and interested stakeholders with a view to removing the remaining NIS republics (except Belarus) from the coverage of Title IV provisions.

If a country is still subject to Jackson-Vanik at the time of its accession to the WTO, the United States has invoked the "non-application" provisions of the WTO. In such cases, the United States and the other country do not have "WTO relations" which, among other things, prevents the United States from bringing a WTO dispute based on a violation of the WTO or the country's commitments in its accession package. (See Chapter II for further information.)

2. Intellectual Property Rights

Since the United States has concluded bilateral agreements covering intellectual property rights (IPR) protection throughout Central Europe and the NIS, today USTR concentrates principally on ensuring compliance by these countries with their international IPR obligations. In 2000, the transitional period granted developing countries and formerly centrally planned economies for compliance with the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Agreement) expired. Accordingly, USTR has conducted a close examination of compliance of WTO Members in the region with the TRIPS Agreement. The U.S. Government has cooperated with and provided technical assistance to the countries in the region to help improve the level of IPR protection. Much of USTR's focus in the region is on improving enforcement of existing IPR legislation. Copyright and trademark piracy has been a widespread and serious problem throughout much of Central Europe and the NIS. Customs and law enforcement authorities in the region are making slow progress in upgrading these countries' enforcement efforts, but continued close monitoring and technical assistance are still warranted.

Three IPR issues in the region merit special mention:

a. Ukraine - Optical Media Piracy

Ukraine has become the leading producer and exporter of pirated compact discs (CDs) in Europe. U.S. industry estimated that in 1999 pirates exported over 35 million pirated CDs to Europe and elsewhere, which represented over $200 million in lost revenues. In June 2000, Ukrainian President Kuchma committed to a plan of action to stop the unauthorized production of CDs and to enact legislation to outlaw such piracy by November 1, 2000. However, due to the failure of Ukraine to pass an adequate optical disc media licensing law , USTR designated Ukraine a Priority Foreign Country in March and initiated a Special 301 investigation. In August 2001, USTR withdrew GSP beneficiary status from Ukraine and published a preliminary sanctions list of Ukrainian products. On December 11, 2001, USTR announced that the U.S. Government would impose 100 percent duties on a list of 23 Ukrainian products with an annual trade value of approximately $75 million contingent upon the outcome of a vote on an optical media licensing law in the Ukrainian parliament scheduled for December 13. As Ukraine failed to adopt the optical media licensing law, USTR announced on December 20, 2001 that the sanctions would take effect January 23, 2002.

b. Hungary, Slovenia, and Poland - Protection of Confidential Test Data

USTR places a high priority on protecting the confidential test data submitted by pharmaceutical firms to health authorities in order to obtain marketing approval. This test data typically require millions of dollars and years of research to develop, so innovators have a strong interest in preventing potential copiers from being able to rely on the data to obtain their marketing approvals. USTR seeks to ensure that WTO Members provide the protection of confidential test data (so-called "data exclusivity") specified in Article 39.3 of the TRIPS Agreement. The United States usually provides five years of exclusivity for confidential test data, and the EU requires its members to provide 6-10 years of exclusivity. Data exclusivity is an important issue in U.S. relations with the countries of Central Europe, because at present many pharmaceutical products of U.S. firms do not yet enjoy product patent protection there. Many foreign pharmaceuticals, at best, receive process patents, a relatively weak form of protection. Over the next five years, this vestige of the transition from socialist economic regulation will diminish in importance as new products gain product patent protection. For those drugs without product patent protection, however, data exclusivity can take on special importance. Accordingly, USTR has pressed the Central European countries - especially Hungary and Slovenia with their large generic drug industries - to provide data exclusivity. In September 2001, Poland passed a law eliminating existing protections for confidential test data until it becomes an EU member, despite USTR representations to the contrary. The United States has raised objections to the law, and at the end of 2001, the Polish government was considering legislation to modify the law.

c. The Russian Federation - Widespread Piracy

Russia has enacted comprehensive laws to protect IPR, but certain major deficiencies remain. Most notably, enforcement of IPR remains a pervasive problem. The prosecution and adjudication of intellectual property cases remains weak and sporadic; there is a lack of transparency, and a failure to impose deterrent penalties. Russia's Customs administration also needs significant strengthening. Piracy of U.S. films, videos, sound recordings, and computer software remains pervasive. Russia has yet to provide protection, as required by our 1990 bilateral trade agreement, to pre-existing U.S. copyrighted works and sound recordings still under protection in the United States. Some U.S. companies have also had difficulty registering well-known marks, and trademark infringement is reportedly on the rise. In April 2001, Russia was again placed on the Special 301 "Priority Watch List" because of these and other problems. In 1998, the U.S. Government began a U.S. Government-wide IP law enforcement technical cooperation program with Russia. Since 1998, this group has intensified technical assistance on both enforcement and WTO requirements.

3. Generalized System of Preferences

Under the Generalized System of Preferences (GSP) program, developing countries are eligible to receive duty-free access to the U.S. market for many items, if it is determined that these countries meet certain statutory criteria. All of the Central European countries (other than the Federal Republic of Yugoslavia) and most of the NIS participate in the GSP program. Azerbaijan, Tajikistan and Turkmenistan have never requested designation as a beneficiary under the U.S. GSP program and, therefore, are not eligible to receive benefits under the program. In 2001, Georgia was added as a beneficiary developing country under the GSP program.

In 1997, the Government of Russia petitioned the U.S. for duty-free treatment under the GSP program for exports of both unwrought titanium and wrought titanium. On July 1, 1998, the President granted the request on wrought titanium. The petition on unwrought titanium was "pended" based on the situation in the U.S. titanium industry. Since 1997, Russia has expressed a continuing interest in a GSP designation for unwrought titanium; however, the domestic industry faces a situation of weakened demand and depressed prices. Three petitions on titanium were submitted during the 2001-2002 GSP Annual Product Review. The GSP Sub-Committee will decide to either accept or deny review of these petitions once the GSP program is re-authorized in 2002.

In 1997 the AFL/CIO petitioned USTR to remove Belarus from eligibility for the GSP program due to violation of worker rights. After conducting an extensive review process, including public hearings, and after affording the Government of Belarus ample time to improve its worker rights situation with no progress on this front, Belarus's GSP benefits were suspended in 2000.

In 2000, USTR commenced reviews on the continued eligibility of Ukraine, Armenia, Moldova, Kazakhstan and Uzbekistan under the U.S. GSP program, due to concerns that these countries were not providing adequate and effective protection of intellectual property rights as required by the GSP statute and as agreed to in the bilateral trade agreements that all of these countries entered into with the United States in the early 1990s. (See section on Intellectual Property Rights above.) In late 2000, based on significant improvement in Moldova's intellectual property rights regime since the initiation of the GSP review process, the U.S. copyright industry, which had petitioned USTR to conduct these reviews, withdrew its petition with respect to Moldova. In 2000, the USG initiated bilateral consultations with both Armenia and Uzbekistan designed to improve the protection and enforcement of intellectual property rights in these countries. In August 2001, USTR withdrew GSP beneficiary status from Ukraine. (See subsection on Ukraine - Optical Media Piracy above.)

The U.S. GSP legislation contains a provision that makes a country ineligible for GSP benefits if it affords preferential treatment to the products of a developed country, other than the United States, which has a significant adverse effect on U.S.

commerce. The U.S. Government has been consulting with the Central European countries about addressing the problem of preferential tariffs given EU exporters vis-a-vis U.S. exporters pursuant to their Association Agreements with the EU. In June 2001, USTR negotiated an agreement with Poland under which Poland agreed to reduce tariffs on key U.S. exports and the U.S. agreed to support, consistent with U.S. laws, Poland's continued participation in the GSP program. (See section on Country Specific Issues below.)

4. The Southeast Europe Trade Preference Act

On November 12, 1999, the Administration transmitted a draft bill, the "Southeast Europe Trade Preference Act" (SETPA), to Congress for its consideration. The SETPA would implement, in part, the United States' commitments to the countries of Southeast Europe pursuant to the Southeast Europe Trade Expansion Initiative announced at the Sarajevo Summit in July 1999. The SETPA would promote economic development and stability in Southeast Europe by increasing access to the U.S. market and facilitating regional investment. The SETPA, which is patterned after the Andean Trade Preference Act, would provide the authority to establish duty-free treatment of certain imports from Albania, Bosnia and Herzegovina, Bulgaria, Croatia, the Former Yugoslav Republic of Macedonia, Romania, Slovenia, and the territories of Kosovo and Montenegro on the basis of specified criteria. Duty-free treatment under the SETPA would extend for a period of five years in order to provide investors adequate time to take advantage of the unilateral preferences that the program offers.

5. WTO Accession

Prior to the end of 2001, virtually all of the Central European countries (Poland, Hungary, the Czech Republic, Slovakia, Romania, Albania, Slovenia, Croatia, Latvia, Lithuania and Estonia) and three NIS countries (the Kyrgyz Republic, Georgia and Moldova) had become members of the WTO. Armenia is expected to complete its accession process in 2002.

WTO accession working parties have been established for an additional eight NIS countries (the Russian Federation (see section on Country Specific Issues below), Ukraine, Armenia, Azerbaijan, Belarus, Kazakhstan, Tajikistan and Uzbekistan) and three Central European states (Bosnia-Herzegovina, the Federal Republic of Yugoslavia, and the Former Yugoslav Republic of Macedonia). Of the NIS, Turkmenistan has not yet applied for observer status or membership in the WTO.

The United States supports accession to the WTO on commercial terms and on the basis of implementation of WTO provisions. WTO accession and the adoption of WTO provisions can be an important method of supporting economic reform. The United States has provided technical assistance, in the form of short- and long-term advisors, to many of the countries in support of the WTO accession process. (See Chapter II for further information on accessions.)

6. Bilateral Trade Agreements and Bilateral Investment Treaties

The United States has some form of bilateral trade agreement with all of the Central European and NIS countries. In addition to these general trade agreements, the United States has concluded a variety of trade agreements concerning specific product areas with various Central European countries and the NIS, such as regarding firearms with Russia, textiles with Romania and Macedonia, customs valuation with Romania, and poultry with Poland and Russia.

In Central Europe, the United States has Bilateral Investment Treaties (BITs) in force with Albania, Bulgaria, the Czech Republic, Estonia, Latvia, Poland, Romania, Slovakia, and Croatia and has signed a BIT with Lithuania, for which the formal ratification process has not yet been completed. Of the NIS, the United States currently has BITs in force with seven countries (Armenia, Azerbaijan, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, and Ukraine) and has signed BITs with three others (Russia, Belarus, and Uzbekistan) for which the formal process of ratification has not been completed. The United States has held consultations with Slovenia on a BIT, but significant differences remain outstanding. After bilateral discussions, Hungary opted not to conclude a BIT with the United States.

7. EU Association Agreements and EU Membership

The United States has been strongly supportive of the integration of the Central European countries into Western Europe. Ten Central European countries (Poland, Hungary, Slovenia, the Czech Republic, Slovakia, Romania, Bulgaria, Estonia, Latvia, and Lithuania) have concluded Association Agreements (often called "Europe Agreements") with the EU. These Europe Agreements are meant to set the stage for eventual EU membership. The EU is not expected to accept new members before 2004, and many predict that enlargement may take significantly longer, especially for the less developed of the candidate countries. The Europe Agreements provide for the reduction to zero of virtually all tariff rates on industrial products and preferential rates and quotas for many agricultural products. In 2000, the EU and all the candidate countries agreed to reduce their tariff rates to zero for the vast majority of each other's agricultural products. The candidate countries' Most Favored Nation (MFN) tariff rates on industrial goods are generally higher, and the rates on agricultural goods are usually lower, than comparable EU rates. Consequently, U.S. exporters often face relatively high MFN tariff rates in contrast with the zero or preferential rates borne by EU exporters. Much of this tariff differential problem with respect to industrial goods will dissipate when the candidate countries join the EU and adopt its generally low industrial tariff rates.

In the interim period prior to these countries' accession to the EU, the United States has been consulting with the Central European countries to address this tariff differential problem. In 2001, the United States held discussions with Poland, the Czech Republic, and Hungary on this issue. Slovenia is implementing a plan to lower its high MFN tariff rates on industrial products to the level of the EU's common external tariff rates over a three-year period. The Czech Republic and Slovakia renewed tariff waivers for 2002 for civil aircraft and key parts. (See section on Country Specific Issues below.)

As part of the accession process, the candidate countries are harmonizing their laws and regulations to those specified in the EU's common legislative regime, the "acquis communautaire." Frequently, harmonization represents an improvement over the existing regimes in the candidate countries. In the case of audio-visual policy, however, candidate countries must harmonize their laws with the EU's Broadcast Directive, which establishes television broadcast quotas for European and domestic production. This directive provides a country with flexibility in implementing the quotas. In 2001, USTR continued to work with the candidate countries to encourage them to include the flexibility option in their legislation.

To facilitate trade with Hungary and the Czech Republic, the EU concluded Protocols to the Europe Agreements on Conformity Assessment and Acceptance of Industrial Products (called "PECAs") with these countries in 2000. These first PECAs entered into force in 2001, and the EU is negotiating PECAs with a number of other EU candidate countries. The agreements eliminate the need for further product testing and certification of EU-origin products covered by the PECAs. Products originating in countries not party to the PECAs, including products tested and certified to EU requirements, may not benefit from these agreements. During 2001, the United States raised concerns, both bilaterally and in the WTO, that the rule of origin provision in these agreements unjustifiably discriminates against non-EU origin products and is inconsistent with WTO obligations. The European Commission proposed in late 2001 that the problematic origin provision be dropped from these agreements. We will continue to monitor this issue.

8. Country Specific Issues

The United States continued to encounter a number of country specific trade issues in the region, which were not described above. The major items are discussed below:

a. Russia: Product Standards, Testing, Labeling and Certification

U.S. companies still cite product certification requirements as a principal obstacle to U.S. trade and investment in Russia. In the context of Russia's WTO accession negotiations, we continue to urge Russia to bring its standards and certification regime into compliance with international practice. The Russian Government is now attempting to put in place the necessary legal and administrative framework to establish standards procedures and processes for certification and licensing of products in Russia in order to better align with WTO rules.

There has been some movement to eliminate duplication among regulatory agencies and to clarify categories of products subject to certification. However, businesses are still experiencing difficulties in getting product approvals in key sectors. Manufacturer declaration of conformity is now feasible under Russian law, but is not yet widely used. In 1998, the Russian State Committee on Standards adopted a new nomenclature of goods subject to mandatory certification, effective January 1, 1999, and the Russian Government has been moving to revise problematic legislation, as provided under its Technical Barriers to Trade action plan.

Certification is a particularly costly and prolonged procedure in the case of telecommunications equipment. In many sectors, type certification or self-certification by manufacturers is currently not possible. Veterinary certification is often arbitrary and needs to be more transparent and based on science. Russian phytosanitary import requirements for certain planting seeds (notably corn, soybeans and sunflowers) appear to lack scientific basis and have blocked imports from the United States. Discussions to ease or eliminate burdensome Russian requirements are ongoing.

b. Russia: WTO Accession

Russia has been an observer in the GATT and WTO since 1990 (initially as the Soviet Union), and formally applied for accession to the GATT 1947 in 1993. Its request for WTO accession has been under discussion since 1995. The United States has strongly supported Russia's efforts to join the GATT and WTO, through active participation in the WTO Working Party established to conduct the negotiations and through technical assistance on how to move Russia's trade regime into conformity with WTO rules. In a series of Working Party meetings through December 2000, Russia described its trade regime and WTO delegations noted specific aspects of the trade regime that require legislative action to become compatible with the WTO. The United States and Russia also continued bilateral discussions on Russia's offers on goods and services market access throughout 2001. WTO-based reforms to Russia's trade regime will strengthen its ongoing efforts for broader-based market-oriented economic reform and can help Russia integrate more smoothly into the global economy. Adopting WTO provisions will give Russia a world-class framework for intellectual property protection, customs duties and procedures, and application of other requirements to imports that will encourage increased investment and economic growth. Russia has indicated an interest in accelerating the negotiations and has taken steps to begin development of new and amended laws and regulations to bring it into conformity with WTO provisions. Completion of the accession negotiations will depend on how rapidly Russia implements WTO rules and moves to conclude negotiations on goods and services with current WTO members.

c. Russia: Aircraft Market Access

The United States and Russia concluded a joint Memorandum of Understanding (MOU) in 1996, which addresses U.S. concerns about access to the Russian civil aircraft market and the application of international trade rules to the Russian aircraft sector. Under the MOU, the Russian Federation confirmed that it will become a signatory to the WTO Agreement on Trade in Civil Aircraft. In the interim before Russia accepts its full international trade obligations, the MOU commits the Russian Federation to provide fair and reasonable access for foreign aircraft to its market. Russia agreed to take specific steps, such as the granting of tariff waivers and the reduction of tariffs, to enable its airlines to meet their needs for U.S. and other non-Russian aircraft on a non-discriminatory basis.

Through 2001, Russian airlines have been able to import over 20 non-Russian aircraft under the MOU, the majority of which were of U.S.-origin. In accordance with the MOU, the Russian Federation also lowered tariffs on aircraft from 30 to 20 percent. In October 2001, the Russian Government announced that it planned to lower the tariffs on certain aircraft parts to 5 percent.

In 1998, the Russian Ministry of Economy issued Resolution #716 which sets conditions for tariff waivers on imported aircraft. The resolution, among other things, required Russian airlines to commit to the purchase or lease of Russian-made aircraft in order to receive tariff reductions and duty waivers for foreign-made aircraft acquisitions. The United States urged the Russian Federation to continue to grant duty waivers to U.S. aircraft imports on a nondiscriminatory basis as provided for in the MOU and to repeal Resolution #716 in the process of moving its trade regime toward conformity with WTO trade rules. In August 2001, the Russian Government repealed Resolution #716 through successive legislation. The United States intends to monitor developments in this area to achieve desired market access.

d. The Czech Republic and Slovakia: Waiver of Tariffs on Civil Aircraft and Parts

The Czech Republic and Slovakia, which have a customs union, impose a 4.8 percent tariff rate on large civil aircraft and parts from U.S. exporters, but allow duty-free access to their markets for EU exporters. This tariff barrier posed a major impediment to the ability of U.S. firms to compete against EU firms for the over $2 billion worth of aircraft tenders to be conducted in 2001. In late 2000, the Czech Republic and Slovakia, in response to U.S. Government reports, agreed to waive 2001 tariffs on large civil aircraft and key parts. In 2001, this waiver was renewed for 2002.

e. Romania: Minimum Reference Prices

Romania had established minimum and maximum prices for various imports, including poultry and distilled spirits and had instituted burdensome procedures for investigating import prices when the invoice value falls below the minimum import price. USTR concluded that this customs valuation regime violated Romania's WTO obligations, especially those under the WTO Agreement on Customs Valuation. The United States initiated a WTO Dispute Settlement case in 2000 and a settlement of the matter occurred through an exchange of letters in June 2001.

f. Poland: Tariff reductions

In 2001, the U.S. and Poland concluded a comprehensive trade package designed to lower tariffs on key U.S. exports to Poland by January 2002 and to establish a process for addressing further the tariff differential that exists between the duties applied by Poland on EU- and U.S.-origin agricultural and industrial products and other bilateral trade issues. The agreement creates a bilateral working group where these issues can be addressed. The industrial products for which tariff reductions have been negotiated include: certain chemicals and chemical products, beauty products, personal deodorants and antiperspirants, gas turbines, centrifuge filters, machines for the preparation of food or drink, fiber optic cables, tractors, large engine autos and auto parts, certain medical supplies, and measuring instruments. With respect to agricultural products, Poland agreed to begin the process of lowering tariffs by January 2002 on grapefruit, non-sparkling wine, and almonds. Poland also agreed to an independent peer review of its phytosanitary measure on ragweed. In exchange for Poland's commitments, the United States expressed its intention to continue support for Poland's participation in the U.S. Generalized System of Preferences (GSP) Program.

D. Asia and the Pacific

Overview

The dramatic expansion of trade and economic growth in the Asia Pacific region over the past decade was due in large measure to the progressive and steady opening of markets in the region. While numerous barriers to trade in the region still exist, significant progress was made in the past decade in dismantling impediments to trade. The commitment of regional leaders in the Asia Pacific Economic Cooperation (APEC) forum to move forward toward free and open regional trade and investment has been an important factor in spurring this regional trend (see Chapter III for information on APEC). In addition, the Administration has delivered results in bilateral negotiations and consultations with countries in the region, opening markets of interest to American farmers, manufacturers, and services providers, and protecting intellectual property, which is critical to U.S. exporters in the high-tech, entertainment and other key sectors.

Highlights of the achievements in this region include:

- *Effective Enforcement of Trade Commitments through WTO Dispute Settlement.* The United States effectively used the WTO Dispute Settlement mechanism to ensure that countries in the region implemented their multilateral commitments. The United States prevailed in a number of cases, which led to the resolution of U.S. complaints regarding Korea's discriminatory import regime for beef, the elimination of India's Balance of Payments (BOP) trade regime, and confirmation that India's local content requirements in the automotive sector are WTO inconsistent.

- *A Series of Significant Market Opening Agreements with Korea.* Through a combination of bilateral consultations, the use of U.S. trade remedy law, and action in the WTO, the United States has concluded agreements with Korea, and obtained commitments from its government: (1) in 1990, 1993, and 2000, to open its market for beef; (2) in 1995, to reform its government mandated shelf-life system, which had impeded the import of meat products; (3) in 1995, to address market access problems for trade in passenger cars; (4) in 1998, to further reduce trade barriers affecting passenger vehicles and to render trade in minivans and sport utility vehicles fairer; (5) between 1995 and 1998, to revise Korean import clearance procedures, thereby expediting the import of several key U.S. agricultural exports; (6) in 1998 and 1999, to take steps to privatize the second largest steel company in the world and to get the Korean Government "out of the steel business;" (7) in 1999, to reform its pharmaceutical pricing and regulatory policies, thereby making the drug approval process in Korea faster and less onerous; and (8) in 1996, an agreement, and in 1997, a policy statement, to ensure equal treatment for foreign goods, services and intellectual property rights protection in telecommunications.

- *Normalization of Trade Relations with the Countries of Indochina.* As a result of the Vietnam era conflict, Cambodia, Laos and Vietnam were three of only seven countries in the world not to receive normal trade relations (NTR) status from the United States. In 1996, the United States completed a bilateral trade agreement with Cambodia granting it NTR status; in 1997, a bilateral trade agreement and a bilateral investment treaty were concluded with Laos (Congressional approval is still required to grant NTR under the terms of this agreement); and in July 2000, the United States and Vietnam signed a bilateral agreement granting NTR status to Vietnam, with provisions covering market access for goods and services, intellectual property and investment issues. After ratification by the U.S. Congress and the National Assembly of Vietnam, the U.S. - Vietnam agreement went into effect on December 10, 2001.

- *Significant Progress in Protecting Intellectual Property Rights.* Bilateral consultations and negotiations with a number of countries in the region resulted in new commitments to protect intellectual property. USTR's efforts highlight the difficulties in securing both the appropriate legislation and enforcement capabilities necessary to protect substantially all forms of intellectual property in Asia Pacific markets. In 2000, Thailand enacted two TRIPS-related laws (trademark amendments and integrated circuits) following extensive consultations with USTR. The Malaysian Government passed in 2001 landmark legislation to reduce pirated optical media production and export, and has begun implementation of these measures. Korea amended its Copyright Act to address some U.S. concerns and implemented a Special Enforcement Period at the direction of President Kim to reduce software piracy.

- *Enhanced Access for U.S. Agriculture and Processed Food Exports.* The United States has vigilantly utilized WTO procedures and bilateral consultations to reduce Asian and Oceanic restrictions which impede market opportunities for U.S. agriculture and food exporters. In addition to the agriculture-related WTO disputes mentioned elsewhere, resolution of India's balance of payments restrictions resulted in the elimination of quantitative restrictions affecting a broad range of agricultural and processed food products. In Southeast Asia, particularly during the recent economic turmoil and currency volatility, U.S. efforts concentrated on a host of measures which threatened U.S. agriculture exports, including: Philippine arbitrary customs valuation practices; Thai tariff adjustments and import licensing restrictions; Malaysian food standards and certification; and Indonesian tariff adjustments and monopolistic distribution channels.

- *Ensuring that Responses to the Financial Crisis are Market Opening.* USTR worked with Treasury and other agencies to ensure that International Financial Institutions (IFIs) stabilization programs adopted by countries affected by the 1997-1998 financial crisis (including Korea, Indonesia and Thailand) worked to open markets and expand competition. Many aspects of these programs have a direct bearing on trade, in areas such as improved market access, transparency, economic deregulation, attracting investment, and allocating public and private resources based on market disciplines. The United States continues to monitor the trade-related aspects of these programs closely to ensure their effective implementation.

- *Restoring Market Opening Reforms.* Following the 1997-98 financial crisis, many Asian countries adopted much needed reform programs, which were then abandoned during the export boom of

1999-2000. In 2001, the Administration pursued initiatives with many countries in the regon, including Indonesia, Thailand and the Philippines, to highlight the continued need for market-opening reforms.

2001 Activities

The countries in the Asia Pacific region suffered in 2001 from slumping demand worldwide, particularly for key exports such as electronics and information technology (IT) products. As a result of the global downturn, no country in ASEAN expects growth to exceed 3.3 percent for 2001-2.

The United States had a full agenda of specific bilateral impediments that it sought to tackle in the Asia Pacific region in 2001, as described below. It also continues to work regionally, primarily through APEC, to foster concrete movement toward more open markets, as described elsewhere in this report. In addition, it is using the WTO process – both in enforcing existing commitments and in its future work program – to further drive open markets and expand trade in a region that accounts for over half of total U.S. exports. The negotiation of a comprehensive U.S.-Singapore Free Trade Agreement is intended to complement both our regional and multilateral work by serving as a significant step toward realization of APEC's "Bogor Vision," under which APEC's 21 members are working toward "free and open trade in the Pacific" and by underscoring the benefits of further trade liberalization.

1. Australia and New Zealand

Australia's market for agricultural commodities continues to be closed for some products due to sanitary and phytosanitary measures. The U.S. Government has made some progress toward resolution of these issues in recent years. For example, Australia's longstanding import prohibition of U.S. table grapes is advancing toward resolution.

On November 14, 2001, President Bush signed a proclamation to terminate the U.S. safeguard action on lamb meat. The Australia/New Zealand WTO dispute brought against the U.S. safeguard measure was thereby closed.

On October 30, 2001, the New Zealand Government announced that it will legislate a two-year moratorium on the release of genetically modified organisms, except those that provide direct benefits to human or animal health. The U.S. Government has expressed its concerns about the imposition of this moratorium which appears to be inconsistent with New Zealand's avowed policy of regulating these products on a scientific basis. The government did announce that it will lift the 17-month moratorium on new genetically modified field trials. It also intends to clarify its expectation that all research must meet strict safety standards by amending the Hazardous Substances and New Organisms Act to require specific mandatory conditions to be applied to any research approval, which the New Zealand Government claims is necessary to ensure that appropriate environmental and health safeguards are imposed.

2. The Association of Southeast Asian Nations (ASEAN)

The trade and investment relationship between the United States and the members of the Association of Southeast Asian Nations is strong, mature, and mutually beneficial despite the effects of the global economic downturn. U.S. exports to ASEAN in 2001 decreased by an estimated 6 percent (annualized based on the first 11 months of 2001). The now ten-member ASEAN group – comprising Brunei, Burma, Cambodia, Indonesia, Laos, Malaysia, Philippines, Singapore, Thailand, and Vietnam – collectively continues to be the United States' fifth largest trading partner. As such, the United States has an important stake in ASEAN's economic recovery and is committed to working closely with ASEAN as an institution, and with ASEAN member countries individually, to pursue and promote our mutual trade and investment interests.

In 2001, the Administration reinvigorated the U.S.-ASEAN Trade Dialogue, a formal mechanism to advance the trading relationship between the U.S. and ASEAN group a whole. In August, 2001, senior officials of ASEAN member states and the U.S. Government met in Brunei to reinitiate this mechanism.

While ASEAN's gradual expansion over time has added to the association's diversity, it has also posed new challenges, which manifest themselves as more complicated decision-making and the lack of ASEAN solidarity in other fora, such as APEC and the WTO (in which some ASEAN members do not participate). Tensions have also surfaced in terms of individual member's economic difficulties and selective implementation of trade-related initiatives undertaken within ASEAN. In order to ensure that these intra-ASEAN undertakings do not adversely affect U.S. interests, we have stressed the importance that such undertakings be consistent with WTO rules, be taken in the spirit of APEC's goals and principles, and be faithfully implemented if ASEAN hopes to attain its own developmental goals and in order to promote a business and investor-friendly environment.

In 1993, the then-seven members of ASEAN created the ASEAN Free Trade Area (AFTA) as a means to promote regional economic competitiveness and prosperity. The objective of AFTA is to promote trade among ASEAN member countries by gradually eliminating customs duties on intra-ASEAN trade of qualifying products by 2005, with special allowance for sensitive sectors. By agreement, AFTA members decided to accelerate the reduction of tariff cuts under AFTA from 2003 to 2005. Laos and Burma were admitted to ASEAN as full members in July 1997, although these countries have until 2008 to phase in obligations under the AFTA.

ASEAN continues efforts to implement and expand the AFTA by including unprocessed agricultural commodities in the tariff phase-out scheme, and placing greater emphasis on the elimination of non-tariff measures such as customs surcharges and technical barriers to trade. Members also continue to follow the 1999 "ASEAN Vision 2020" declaration in which members resolved, among other things, to continue with full implementation of AFTA, to implement fully the ASEAN Investment Area by 2010, and to achieve the free flow of investment by 2020.

a. Indonesia

i. General

The Indonesian economy remains fragile and in need of significant reforms including corporate governance and the privatization of assets seized by the state during the 1997-98 regional financial crisis. Indonesia's IMF program, initiated in October 1997, was modified in each of the three subsequent years as the economic situation deteriorated. Concerns about the Indonesian Government's ability to follow through with these reforms along with continuing political uncertainty is weakening investor confidence and adding to the serious problems faced by Indonesia's financial and corporate sectors.

Despite the country's tenuous economic situation, the Administration sought to bolster the U.S.-Indonesian trade relationship by convening a Bilateral Trade and Investment Council in September 2001. At that meeting, senior officials met to address several long-standing trade issues such as IPR and market access for U.S. poultry products.

ii. Intellectual Property Rights

In April 2000, USTR removed Indonesia from the Special 301 Priority Watch List, where it had been since 1996, and placed it on the Watch List in recognition of efforts made toward a more effective IPR regime. The Indonesian Government resubmitted draft legislation on trade secrets, industrial designs, patents, trademarks and copyrights in 2000, although this legislation has yet to gain parliamentary approval.

U.S. industry reports continuing problems with IPR issues, including: software, book, video, and VCD piracy; drug and apparel trademark counterfeiting; audiovisual market access barriers; inconsistent enforcement; and an ineffective legal system. Indonesia's amendments to the copyright, patent and trademark laws would not appear to be fully consistent with Indonesia's WTO obligations.

The U.S. Government has raised these issues with Indonesia since 1998, when it presented Indonesia with an IPR work plan (market access, enhanced enforcement, WTO consistency of laws, special juridical arrangements, legal use of software, and increased protection of well-known marks in several company-specific cases). Although the Indonesian Government has yet to take sufficient action on the proposed work plan, it has acknowledged the need for improved enforcement and a broad education program, in addition to the need to bring its statutes into WTO conformity. The U.S. and Indonesian Governments have agreed to work together under the auspices of the bilateral Trade and Investment Council to achieve progress on intellectual property issues in 2002.

b. Malaysia

i. Investment and Services

Malaysia maintains investment limits which predate the mid-1990s financial crisis and which adversely affect the local business and investment climate. In general, Malaysian law requires that business entities include a domestic partner with a minimum 30 percent stake. Banking and other financial services providers face foreign-held equity restrictions, as do suppliers in the wholesale/retail, distribution and multi-level marketing, construction and legal services sectors. U.S. officials will continue to raise concerns over investment restrictions in the distribution services sector and will continue to monitor developments on this issue.

ii. Tariffs

In 1997 and 1998, Malaysia raised tariffs on certain goods from 0 percent in 1996 to current levels of between 5 and 20 percent ad valorem – still within its WTO-bound commitments. The products affected include some types of heavy machinery and construction equipment, automobiles, motorcycles, and home appliances. Malaysia reduced tariffs for information technology products covered by the Information Technology Agreement (ITA), under which most of its tariffs were bound at zero by 2000.

iii. Local Content-Related Investment Incentives

Malaysia has taken a number of steps which confer tax benefits, based on the amount of locally produced parts or inputs utilized, in order to promote the development of domestic automobile manufacturers under its "national automobile" program. As required by the WTO Agreement on Trade-Related Investment Measures, Malaysia's various incentives for local production were to have been eliminated by January 1, 2000. However, in late 1999, Malaysia notified WTO members of its desire to obtain a two-year extension of its auto-related measures. In October 2001, WTO members, including the United States, reached an agreement with Malaysia to allow an extension of these measures through December 2003.

iv. Intellectual Property Rights

USTR conducted a Special 301 out-of-cycle review of Malaysia's intellectual property practices in September 2001 and decided to remove Malaysia from the Priority Watch List following the passage and initial implementation of new optical disc (OD) legislation designed to reduce pirated optical media production and export. The United States will continue to encourage the Malaysian Government to fully implement the enforcement provisions of this legislation.

c. Philippines

i. Market Access Issues

In 2000, the Philippines passed a new safeguard law. Although no action has been taken under this law, the U.S. Government and U.S. industry have serious concerns with its provisions. The legislation does not give foreign producers a meaningful opportunity to defend their interests. In addition, the prerequisites for imposition of provisional relief appear to be lower than the requirements contained in the WTO Safeguards Agreement. The U.S. Government has raised its concerns with the Philippine Government over this law and will take appropriate steps, as necessary, if the Philippine Government takes safeguard actions against U.S. firms.

ii. Intellectual Property Rights

The protection of IPR continues to be hampered by the lack of a political commitment from the Philippine Government to implement existing laws, to dedicate the necessary resources to law enforcement, and to stress publicly the need for consistent protection of intellectual property rights. While a comprehensive 1997 law on IPR represented a significant step toward implementation of the Philippines' commitments under the WTO TRIPS Agreement, several provisions of the law remain of concern, including provisions governing the circumstances under which decompilation of software programs is permissible, *ex parte* search and seizure, and restrictions on technology licensing arrangements. The United States also continues to monitor Philippine enforcement efforts and judicial efficiency. As a result of these concerns, the U.S. Government elevated the Philippines to the Special 301 Priority Watch List in 2001.

iii. Customs

On March 31, 2000, the Philippine Government ended a problematic pre-shipment inspection services contract with Swiss Societe Generale De Surveillance, but during 2001 an influential minority in the Philippine business community pressed the Philippine Government for a return to this practice. The U.S. Government has expressed its opposition to a return to a pre-shipment inspection regime that does not strictly adhere to the WTO Customs Valuation Agreement, and will closely monitor further developments on this issue.

iv. Local Content-Related Investment Incentives

As required by the WTO Agreement on Trade-Related Investment Measures, the Philippines' local content-related measures in the automobile sector were slated for elimination by January 1, 2000. In October 1999, the Philippines requested a five-year extension of these measures. After extensive consultations with the Philippines, the United States filed a dispute settlement case with the WTO in 2000, and in October 2001, USTR secured the Philippines' agreement to submit to a phase-out program that will eliminate local-content requirements in its automobile sector by June 30, 2003.

d. Singapore

In November 2000, the United States and Singapore announced the launch of negotiations for a U.S.-Singapore Free Trade Agreement (FTA). This agreement is expected to have significant commercial benefits, as Singapore is our largest trading partner in Southeast Asia, with two-way trade in goods and services totaling more than $40 billion. In negotiating this agreement, the United States is seeking to eliminate tariffs on substantially all goods over time, obtain substantial sectoral coverage in services, help develop electronic commerce, protect intellectual property rights (IPR), and achieve other bilateral trade objectives. The agreement also will include provisions on labor and the environment.

While the United States and Singapore are discussing IPR in the context of the FTA negotiations, this area has been a longstanding concern for the United States. Singapore readily acknowledges that enhanced IPR regulation and enforcement is necessary to achieve its goal of becoming a "knowledge-based economy." The creation of mobile IPR units in 2000 has increased the Singaporean Government's ability to conduct raids on major centers of distribution for pirated products. In addition, the Government of Singapore's efforts to promote a "code of conduct" for local manufacturers of optical disks in order to improve the performance of its domestic industry has helped to focus attention on the growing problem of piracy of CDs, VCDs, and CD-ROMs. The U.S. Government recognized this progress in 2001 by removing Singapore from the Special 301 Watch List.

e. Thailand

i. Intellectual Property Rights

In recent years, Thailand's commitment to effective IPR protection has been uneven, as evidenced by growing piracy rates and inconsistent coordination between enforcement authorities. Despite some progress on the legislative front in 2000, by the end of 2001, many key statutes remained pending before the Thai legislature, including promising legislation on optical media piracy and the protection of business trade data. Recognizing the increasing problem of pirate optical media production in Thailand, U.S. copyright industries petitioned USTR in 2001 to suspend or remove Thailand's benefits under the Generalized System of Preferences until such time as the Thai Government moved to significantly improve IPR protection. With the expiration of GSP at the end of 2001, the industry request was suspended. At such time as GSP is reauthorized, USTR will further consider the request. The Thai Government has begun to make progress, but more remains to be done to ensure sustained enforcement efforts.

ii. Market Access Issues

Thailand's applied tariffs are generally higher than many of its neighbors. As a signatory to the Information Technology Agreement (ITA), effective January 2000, Thailand eliminated tariffs on 153 information technology-related products pursuant to its obligations. The Thai Government, however, continues to require that certificates of origin accompany ITA products through Thai Customs. Thailand is the only ITA member to require such certification, a practice that appears to violate the ITA Agreement. The U.S. Government has repeatedly raised its serious concerns about this practice with the Thai Government.

f. Cambodia

On December 31, 2001, the United States and Cambodia reached agreement extending the Bilateral Textile Agreement for an additional three years, through December 31, 2004. In the renewed agreement, the quota for most textile exports from Cambodia in 2002 was fifteen percent higher than in 2001, a nine percent increase in recognition of Cambodia's progress in reforming labor conditions in textile factories over the last three years, in addition to the normal increase in quotas of six percent.

The nine percent increase for 2002 reflects Cambodia's progress towards ensuring that working conditions in its garment sector are in "substantial compliance" with internationally recognized labor standards and provisions of Cambodia's labor law, and follows recent formal U.S.- Cambodian labor consultations. The International Labor Organization (ILO) also has two projects underway assisting Cambodia with the implementation of its labor law.

As in the original agreement, Cambodia will be eligible for future additional quota increases if working conditions in the garment industry substantially comply with internationally recognized core labor standards. The U.S. and Cambodian governments agreed to increase this potential quota reward for full compliance from 14 to 18 percent. The United States and Cambodia will keep working conditions in the Cambodian garment sector under ongoing review, and will conduct two rounds of labor consultations in 2002, as provided for in the Agreement.

g. Normalization of Trade Relations with Vietnam and Laos

i. Vietnam

On July 13, 2000, the United States and Vietnam signed an historic bilateral trade agreement, concluding a four-year negotiation to normalize trade relations. Upon implementation, the agreement grants Vietnam "Normal Trade Relations" (NTR) status, that is, the same low tariffs that the United States applies to imports from nearly every other country. The agreement also commits Vietnam to sweeping economic reforms, which will create trade and investment opportunities for both U.S. and Vietnamese companies, and will lay the foundation for a new American relationship with Vietnam.

Under U.S. law, for Vietnam to receive NTR status, a bilateral trade agreement must be completed and approved by Congress, and the President must "waive" the "Jackson-Vanik" provision, indicating that Vietnam is making sufficient progress on the issue of free emigration. Since 1998, the President has granted a Jackson-Vanik waiver for Vietnam. Thus, completion of this agreement, and its subsequent approval by Congress has cleared the way for Vietnam to receive annually renewed (as opposed to permanent) NTR treatment from the United States.

On June 8, 2001, President Bush signed Proclamation 7449 and transmitted the Agreement to Congress on that date for its approval. In the proclamation, the President directed the USTR to publish notice of the effective date of the Agreement. Congress approved the Agreement on October 3, 2001 and the President signed the legislation approving the Agreement on October 16, 2001. The National Assembly of Vietnam approved the resolution ratifying the Agreement on November 28, 2001 and the President of Vietnam signed the legislation on December 4, 2001.

On December 10, 2001, U.S. Trade Representative Robert B. Zoellick and Vu Khoan, Minister of Trade of the Socialist Republic of Vietnam, exchanged written notices of acceptance, implementing the Agreement. Thus, in accordance with the terms of the Agreement, NTR tariff treatment for products of Vietnam became effective on December 10, 2001.

The trade agreement commits Vietnam to opening its market and moving toward adoption of WTO and international norms. The agreement has five major sections:

1. *Market Access for Agricultural and Industrial Goods.* Vietnam has made significant commitments across a wide range of industries. It will grant trading rights (the right to import and export) to all Vietnamese and U.S. persons and firms; lower tariffs on hundreds of categories of industrial goods and farm products of interest to U.S. exporters; phase-out all non-tariff measures; and adhere to WTO standards in applying customs, import licensing, state trading, technical standards and sanitary and phytosanitary measures.

2. *Intellectual Property Rights.* Vietnam will adopt the WTO "TRIPS" standard for intellectual property protection (e.g., in the area of copyrights, patents, and trademarks) in 18 months or less, and will take further measures in several other areas not covered by the TRIPS Agreement (e.g., protection of satellite signals).

3. *Market Access for Services.* Vietnam will allow U.S. persons and firms to enter its services market in a broad array of areas, including financial services (insurance and banking), telecommunications services, distribution services, audiovisual services, as well as other sectors. These commitments are phased in, typically within three to five years.

4. *Investment.* Vietnam will protect U.S.

investments from expropriation, eliminate its "Trade Related Investment Measures," and phase out its investment licensing regime for many sectors, as well as modernize its investment regime in other areas.

5. *Transparency*: Vietnam has agreed to adopt a fully transparent regime in each of the four areas above, by publishing all laws, regulations and rules; submitting them for public comment in advance; and giving U.S. citizens the right to appeal rulings made with respect to all such laws and regulations.

ii. Laos

In 1997, the United States completed a comprehensive bilateral trade agreement with Laos aimed at normalizing trade relations. Laos, unlike Vietnam, is not covered by the "Jackson-Vanik" provisions of U.S. trade law. As with the Vietnam agreement, the Laos agreement requires separate legislation enabling the President to grant normal trade relations status to Laos once formal acceptance of the agreement is completed.

3. Republic of Korea

a. Macroeconomics and Trade

At the end of 1997, the IMF negotiated a macroeconomic stabilization package with the Korean Government when the value of the won depreciated dramatically due to a large outflow of foreign investment. The stabilization package for Korea included credit from the IMF, the World Bank, and the Asian Development Bank.

The stabilization plan focused on: (1) restructuring the financial and corporate sectors to make them more market-driven, efficient, transparent, and open to foreign investment; and (2) eliminating trade- and competition-distorting policies. Korea's trade-related reforms included early elimination of WTO-prohibited export and domestic content subsidies and the import diversification program (which prohibited many Japanese imports) and a reduction in the number of products subject to tariff adjustments, or snapbacks. Korea also agreed to liberalize its import licensing and certification procedures and to bind its OECD financial services market access commitments in the WTO.

The Korean Government made progress on implementing some of its reform commitments during the past four years, particularly in the financial sector, by rationalizing and recapitalizing its banks, and by consolidating regulatory authority over the financial sector in a new, independent Financial Supervisory Commission. However, the Korean Government still maintains a majority ownership in several of the largest commercial banks in Korea and a significant stake in a number of others. Korean authorities are seeking to further strengthen commercial bank balance sheets and restructure merchant banks, investment trust companies and the insurance industry.

With respect to changes in corporate practices, Korea is in the process of implementing international standards on accounting practices, including corporate activities on a consolidated basis, and has provided for the appointment of outside directors on corporate boards. The rights of small shareholders have been strengthened, while restrictions on foreign participation have been eased and bankruptcy laws have been strengthened. In 2001, the Korean Government announced that it would relax restrictions on corporate ownership and implemented the Corporate Restructuring Promotion Act, both of which have raised some concerns on the part of foreign firms.

Many of the systemic reforms that President Kim Dae Jung laid out for Korea have yet to be implemented. The U.S. Government has noted in representations to the Korean Government that for restructuring to be considered meaningful: (1) it must yield efficient, market-driven companies; and (2) the process through which it is carried out must be open, transparent, and treat foreign creditors equitably, and comport with Korea's international obligations.

The fiscal, monetary, and restructuring policies laid out by the Kim Administration have contributed to a resumption of foreign and domestic consumer confidence in Korea's economy. In 2000, Korea's economy grew by more than 9 percent and growth in 2001 was about 2.6 percent, despite the global downturn. The United States ran a bilateral trade deficit with Korea of $12.5 billion in 2000, and the deficit in 2001 is expected to be higher.

Despite their differences over a wide range of bilateral trade issues, the United States and Korea cooperated effectively in regional and multilateral fora. Their cooperative efforts helped lead to the successful launch of new multilateral trade negotiations at the Doha Ministerial in November.

b. OECD

In late 1996, the Korean National Assembly ratified Korea's accession to the OECD. Given Korea's membership in the OECD, the United States expects Korea to implement its WTO commitments and to negotiate in the new round of multilateral trade negotiations as a *developed* country, including in the area of agriculture.

In addition, the United States underscored the need for Korean regulations and other rules, and the officials who administer them, to reflect the free and open trade and investment policy that Korean President Kim Dae Jung has embraced. Among the specific areas of concern flagged by the United States in this review were Korean policies on motor vehicles, pharmaceuticals, telecommunications, *chaebol* reform, import clearance procedures, foreign equity restrictions, and customs classification and border treatment.

In September 2000, the OECD Trade Policy Review Body reviewed Korea's trade policies. The report noted the progress the Korean Government had made over the past few years in instituting market-based reforms, which helped pave the way for the recovery of the Korean economy following the financial crisis. However, the United States and Korea's other trading partners highlighted areas where additional progress is required. Among these were Korean Government policies on privatization and *chaebol* reform, motor vehicles, pharmaceuticals, telecommunications, agriculture, intellectual property protection, import clearance procedures, foreign equity restrictions, subsidies, and labor rules.

c. Motor Vehicles

On October 20, 1998, the United States and Korea concluded a Memorandum of Understanding (MOU) to improve market access for foreign motor vehicles. This MOU followed USTR identification of Korean barriers to motor vehicles as a priority foreign country practice. Under this MOU, Korea agreed to: (1) bind in the WTO its 80 percent applied tariff rate at 8 percent; (2) lower some of its motor-vehicle-related taxes and to eliminate others, thereby substantially reducing the tax burden on motor vehicle owners; (3) streamline its standards and certification procedures and adopt a manufacturer driven self-certification system by 2002; (4) establish a new mortgage mechanism to make it easier to purchase motor vehicles in Korea; and (5) continue to actively and expeditiously address instances of anti-import activity and to proactively educate Korean citizens on the benefits of free trade and competition. As a result of the measures the Korean Government committed to in the 1998 MOU, the USTR terminated a Section 301 investigation and began monitoring the Korean Government's implementation of these measures through formal reviews.

At the most recent MOU review, held in September 2001, the United States and Korea held consultations to assess the progress under the agreement and to discuss additional steps Korea will take to implement this agreement. While the Korean Government has implemented many of the specific provisions of the MOU, the U.S. Government remains concerned about the lack of substantial increases in market access for foreign motor vehicles in Korea. The share of foreign vehicles in the Korean market remains at well under one percent as a result of high taxes and tariffs, and continuing anti-import sentiments among many Korean consumers, as well as standards and certification issues.

The United States has made specific proposals for addressing these concerns and achieving further progress under the agreement. Among these were proposals for Korean Government action to improve the generally negative perception of foreign vehicles among Korean citizens, which are largely the result of successive Korean Government policies that discouraged the purchase of foreign autos. The U.S. Government also made specific proposals on outstanding standards and certification, financing, and tax and tariff issues.

In November 2001, the Korean Government reduced one auto-related consumption tax through June 2002, which may have a positive effect on foreign auto sales. In addition, while negative consumer perception of foreign products remains the single most significant barrier to foreign vehicle sales, the Korean Government has taken a few steps in this area. President Kim publicly urged Koreans to buy more foreign products, including autos, and the Korean Government will purchase 100 imported cars for its Police Agency fleet over the next two years. Nonetheless, it has refused to lower tariffs, despite its own study that showed that doing so would lead to significant increases in foreign car sales.

d. Steel

A discussion of the overall situation facing the steel industry in the United States and the initiatives of the Administration during 2001 is contained in Chapter V of this report.

e. Pharmaceuticals

U.S. concerns regarding pharmaceuticals trade relate to three baskets of issues: (1) listing and pricing on Korea's national health insurance reimbursement schedule, and associated hospital margins and administrative procedures that limit the commercial distribution of foreign-made pharmaceuticals; (2) protection of intellectual property rights, particularly protection of clinical data and patents; and (3) regulatory requirements, particularly on acceptance of foreign and clinical test data and approval of new drugs.

In 1999, the Korean Government took a number of steps to address U.S. concerns in this sector. Since then, the U.S. Government has been closely monitoring Korea's implementation of these changes. The United States has urged Korea to take steps to ensure full implementation and enforcement of the Actual Transaction Price (ATP) system whereby both imported and domestically-manufactured pharmaceuticals are reimbursed without hospital margins (such margins had previously benefitted only Korean-produced drugs). The Korean Government has recently suggested that it is considering changes to the ATP system and other aspects of its pharmaceutical pricing system. The U.S. Government has strongly urged Korea to ensure that any changes do not undermine the agreements the two governments have reached on this issue or lead to a distortion of the incentives needed to promote innovation and the availability of innovative pharmaceutical products.

To speed the introduction of innovative drugs into Korea, the U.S. Government has underscored the need for Korea to improve market access for foreign pharmaceuticals by eliminating requirements for redundant clinical test data in the drug approval process. USTR also continues to press Korea to implement international guidelines by adopting tests for bio-equivalency that are based on global scientific standards. In addition, the U.S. Government continues to encourage Korea to accept foreign clinical test data, and has urged Korea to apply requirements for bridging studies based on International Conference on Harmonization (ICH) and global scientific studies.

f. Intellectual Property Rights

USTR placed Korea on the Special 301 Priority Watch List in 2000 as a result of serious concerns over legal protection and enforcement of intellectual property rights (IPR). While some progress has been made, the U.S. Government and U.S. industry remain concerned about enforcement by the Korean Government of Korea's IPR laws.

In 2000, the Korean National Assembly passed amendments to laws on protection of copyrighted works, including computer programs, which addressed some U.S. Government concerns, but outstanding issues remain. The U.S. Government raised these issues in detail with Korea on numerous occasions in 2001. It also raised the failure to provide full protection for pre-existing copyrighted works as required under the TRIPS Agreement. The U.S. Government will continue to work with the Korean Government to ensure its full compliance with its WTO obligations, including those on protection of test data against unfair commercial use and disclosure, and on protection of copyrights. Issues related to Korea's WTO consistency must be resolved before concluding a Bilateral Investment Treaty (BIT).

The United States also continues to monitor Korea's implementation of an amendment to the Pharmaceutical Affairs Act in January 2000, which provides for the protection of data submitted to the Korean Government when the submitting company requests such protection. The U.S. Government also remains concerned about the lack of coordination between the Korea Food and Drug Administration (KFDA) and intellectual property (KIPO) officials, which allow products that infringe existing patents to be approved for marketing.

g. Telecommunications

The Korean Government raised foreign investment limits in telecommunications services companies (other than Korea Telecom) from 33 percent to 49 percent in April 1999, 18 months sooner than its WTO commitment. The limit on foreign investment in Korea Telecom was increased from 20 percent to 33 percent in September 1999, and the Korean Government announced in September 2000 that it would ask the Korean National Assembly to revise the Telecommunications Business Act to increase the foreign ownership ceiling to 49 percent. The United States has urged Korea to eliminate all investment restrictions in this sector, which limit Korea's ability to introduce the infrastructure necessary to develop its telecommunications sector.

Continued Korean Government intervention in the private sector's selection of technologies and interference with private sector negotiations involving foreign licensing and tecnology transfers remained a U.S. concern in 2001. This governmental influence on the choice of sources of equipment and technologies is often apparent in the licensing process for operators and in localization policies for procurement. The Korean Government may use its influence directly but often works indirectly through industry associations and quasi-governmental commissions or other entities. As a result, some U.S. firms with leading-edge technologies have encountered resistance to their efforts to introduce new software and technologies to the market, and some U.S. firms that formerly had a dominant market share have lost significant market share to Korean firms over the past few years. By limiting competition in the Korean telecommunications market, the Korean Government also is hampering the ability of Korean firms to develop state-of-the-art, globally competitive products. The U.S. Government will continue to raise these concerns with the Korean Government.

h. Financial Services

As a condition in the IMF stabilization package, Korea agreed to bind its OECD commitments on financial services market access in the WTO. In January 1999, Korea provided WTO members with a revised and somewhat improved schedule of financial services commitments that entered into force as of September 1999. The U.S. Government will continue to work with Korea to bring about more liberal treatment of foreign financial services providers.

i. Government Support for Semiconductor Production and Export

The U.S. Government continued to express strong concerns about instances of possible Korean subsidization of semiconductor production and export that could adversely affect U.S. trade interests. In particular, the U.S. Government raised concerns about the support by the Korean Government of Hyundai Electronics, Ltd. (now, Hynix Semiconductor, Inc.), Korea's second largest semiconductor manufacturer.

In early 2001, the state-run Korea Development Bank (KDB) issued a special one-year bond obligation and most of the seven firms which have received benefits under the program have been Hyundai affiliates, with the KDB purchases of Hynix bonds totaling more than $700 million. In May, Korean state-owned and state-controlled banks and several investment trust companies provided additional assistance to Hynix under a complex refinancing agreement. In the fall, at the instigation of the partially state-owned Korea Exchange Bank (KEB), Hynix's creditors agreed to a new $4 billion bailout. Still later last year, the KEB organized yet another $7 billion debt restructuring package among Hynix creditors and approximately $500 million in new loans. A collection of investment trust companies also apparently rolled over around $900 million in loans for three years.

The U.S. Government raised its concerns on this issue at the two regular meetings of the WTO Subsidies Committee last year. It has drawn Korea's attention to its obligations under the Subsidies Agreement not to provide subsidies that may cause adverse effects to other WTO Members and has pointed out the questionable consistency of these interventions with the spirit of Korea's financial and market reform commitments. At the second meeting, U.S. objections were echoed by the European Union, while Japan and Singapore also expressed interest and concern regarding the situation. In addition, senior U.S. officials have raised this issue in meetings with officials at the highest levels of the Korean Government. By year's end, Micron had entered into talks with Hynix to explore the possibilities of a merger or buy-out arrangement that could result in the rationalizing the two firms' chipmaking operations. The U.S. Government will continue to watch the situation closely and, if no market-based solution is found, will take appropriate action.

j. Screen Quotas

Korean Law requires that domestic films be shown in each cinema for a minimum number of days per year. Current law requires that Korean films be shown 146 days of the year, with a potential discretionary reduction to 106 days. The Korean National Assembly adopted a resolution on December 8, 2000 stating that the screen quota system must not be abolished or reduced until the domestic market share for Korean films maintains a 40-percent level.

k. Bilateral Investment Treaty

In 2001, the U.S. Government sought further progress in negotiations with Korea on a BIT aimed at securing Korean commitments on a balanced and open investment regime and providing protections for U.S. investors in Korea. Negotiations in 1999 made progress on Korean commitments to liberalize investment restrictions in a number of sectors, but several key issues remain unresolved, including greater access for U.S. investors in telecommunication services, liberalization of the screen quota system, and resolution of IPR issues, specifically, with respect to retroactive copyright protection for pre-existing works and sound recordings.

l. Cosmeceuticals

The Korean Cosmetic Products Act, which became effective in July 2000, separates cosmetic products from cosmeceuticals or cosmetics with a function, such as sun screen, wrinkle cream or skin whiteners. The new regulations govern the sale and promotion of cosmeceuticals and require that these products be labeled as cosmeceuticals and not include claims that are beyond proven efficacy. However, the new regulations are extremely vague, and as a result, since their implementation, only 18 U.S. products have been approved for sale in Korea out of more than 600 applications. The U.S. Government has repeatedly raised its concerns with Korea and both the United States and the EU are considering next steps to resolve this issue.

m. Agriculture

Beef: To address longstanding impediments to the entry and distribution of foreign beef, on February 1, 1999, the U.S. Government requested WTO dispute settlement consultations. Australia also requested formation of a panel on Korea's beef measures and the U.S. and Australian panels were eventually joined. Canada and New Zealand participated in the panel process as third parties.

The U.S. complaint focused on Korea's: (1) requirements that imported beef be sold only in specialized imported beef stores and Korean laws and regulations restricting the resale and distribution of imported beef by SBS super-groups, retailers, customers, and end-users; (2) a discretionary import licensing regime; (3) imposition of duties and charges in the form of a markup, which is not provided for in Schedule LX; and (4) failure to fulfill its WTO reduction commitment for domestic support.

The United States prevailed in the case against Korea, with the WTO panel concluding in July 2000 that Korea's import regime for beef discriminates against imports of beef from the United States and other foreign countries. Korea filed an appeal of the case in September; and in December 2000 the Appellate Body report affirmed the key findings of the WTO panel. In September 2001, Korea passed legislation to bring its measures into compliance with WTO rules. The U.S. Government is continuing to monitor implementation of the new laws by central and local government authorities.

In October 2000, the Korean Government passed a rule of origin requiring that cattle must be in the United States for at least six months prior to slaughter in order to be considered U.S beef when exported to Korea. The requirement was to go into effect at the beginning of 2001. The U.S. Government raised strong concerns about the new requirement and its likely impact on U.S. beef exports to Korea, a key market for U.S. beef exporters. Korea agreed to delay implementation of the new requirement for one year to study U.S. concerns. On December 2001, the Korean Government eliminated the residency requirement.

The U.S. Government has also sought changes to Korean regulations prohibiting the freezing of meat sold "fresh" or "chilled" or the thawing of meats sold as "frozen." Freezing of fresh or chilled meat is commonly practiced in the United States and many other markets to ensure product wholesomeness, especially when the meat must be transported lengthy distances, and U.S. regulations allow for freezing of fresh or chilled beef as long as the meat is properly labeled and appropriately handled. The Korean Government is reviewing U.S. regulations regarding this issue and actively considering changes to its regulations.

Rice: The Korean Government purchased U.S. rice for the first time in 2001. In addition, in December, the Ministry of Agriculture announced a plan for the stabilization of the rice industry, emphasizing compensation to farmers for shifting production to alternative crops, an important first step toward reform of Korea's rice market.

However, the Korean Government continues to exercise full control over the purchase, distribution, and end-use of imported rice. The state trading enterprises that administer the WTO-mandated minimum access program continue to purchase only low-quality Asian rice, as Korean law forbids the use of imported rice for purposes other than industrial or processing uses, severely impeding imports of high quality U.S. rice.

Oranges: The Cheju Citrus Cooperative, a Korean producer group, has controlled the allocation of the in-quota quantity of Korea's orange tariff-rate quota (TRQ). In the past, Cheju has filled the quota, with most of the imports coming from the United States. During the past three years, however, the quota was not filled. The United States will continue to actively engage Korea on this issue to ensure its full compliance with its WTO obligations on citrus.

Croaker: Korea's application of prohibitively high adjusted tariffs to croaker significantly limits U.S. exports of the fish species to Korea, which is the largest per capita consumer of croaker in the world. Only joint ventures with Korean importers (with a minimum of 49 percent Korean ownership) are eligible to export croaker to Korea at a zero tariff rate. Korea's market for croaker was closed until 1997, when the Government introduced a 90 percent adjustment tariff. Since 1997, in accordance with the requirements of its IMF stabilization package, the Korean Government has reduced the number of items that qualify for adjusted tariff protection. Of the remaining 27 items, however, 14 are seafood products, including croaker.

The U.S. Government has urged Korea to eliminate or reduce its tariff on croaker. The Korean Government reduced the tariff by 10 percent each year for each of the last three years, to 70 percent in early 2001. However, in late 2001, the Korean Government failed to include further reductions for 2002. The United States will continue to press Korea to phase out these tariffs.

Potato Preparations: The Korea Customs Service's (KCS) repeated misclassification and change in border treatment of potato preparations has hampered U.S. exports of these products to the Korean market. Potato preparations should enter Korea in the unrestricted HS heading 2005 with a current applied tariff rate of 20 percent and a bound rate of 31.5 percent. Instead, Korea has been classifying these products in the more restrictive HS heading 1105 (pure potato), with an in-quota quantity of 60 metric tons and an over-quota tariff rate in excess of 300 percent. The U.S. Government will continue to urge Korea to take steps to resolve this issue.

Agricultural Tariffs: In 1999, the U.S. Government discovered a discrepancy between Korea's applied tariff rates on several agriculture items – peanuts, popcorn, potato flour, potato flakes, and wheat and soybean meal – and its WTO bindings and tariff commitments made to the United States in a 1993 U.S.-Korean Record of Understanding and a February 1994 exchange of letters. In February 1999, U.S. Embassy officials in Seoul brought these discrepancies to the attention of the Korean Government. The Korean Government adjusted the in-quota tariff rates of potato flour, potato flakes, and peanuts effective January 1, 2000. The U.S. Government will continue to press Korea to bring duties on the remaining agricultural products into compliance with Korea's WTO and bilateral commitments.

Biotech Labeling Requirements: In July 2001, the Korean Government began imposing new mandatory biotech labeling and identity preservation requirements for processed foods containing soy or corn products, which are to be extended to products containing potato products in mid-2002. These requirements were probationary until January 13, 2002, when the requirements were to be finalized and penalties imposed for non-compliance.

According to U.S. industry, the requirements are extremely burdensome and have disrupted U.S. exports of processed foods. The U.S. and other foreign governments have repeatedly raised concerns about the new requirements, including the documentation requirements, whether the Korean Government has met its transparency and notification obligations, and national treatment and MFN issues.

The U.S. Government is continuing to urge the Korean Government to consider whether the requirements appear to be more burdensome than necessary to achieve the goal of providing consumers clear information. The U.S. Government is continuing to urge the Korean Government to amend the requirements and will consider further action, as appropriate, to address this issue.

n. Import Clearance Procedures, Food Standards, and Labeling

After WTO dispute settlement consultations with 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) beginning revisions of the Korean Food and Food Additives Codes, for example, by bringing Korean pesticide residue level standards for citrus into conformity with CODEX standards; and (5) requiring ingredient listing by percentage for major, rather than all, ingredients. In 2000, the KFDA issued revisions to the Food Code, the Food Additives Code, and Labeling Standards for Food. However, additional work will be needed to bring Korea's Food and Food Additives Codes into conformity with international standards, specifically those related to chocolate and food additives.

U.S. firms continue to experience problems with import clearance in Korea. The U.S. Government has sought to expand access for a number of cherry varieties to the Korean market, but the Korean Government has provided no response to U.S. proposals for mitigation measures. The United States will continue to urge the Korean Government to address this issue. However, the Korean Government has initiated the domestic legal process necessary to revise its regulations and recognize U.S. industry fumigation for shelled walnuts. Currently, U.S. walnut exporters are required to conduct redundant fumigation on walnuts, causing processing delays and significantly raising costs.

4. India

a. General

The U.S. and India continued to make progress in developing a constructive long-term trade relationship. To this end, in August 2001, U.S. Trade Representative Robert B. Zoellick was the first member of President Bush's Cabinet and the first USTR to visit India in more than ten years. Important events during the year included the elimination of India's remaining balance of payment-related quantitative restrictions and a U.S. victory in its WTO challenge to India's automotive TRIMS regime. However, India continues to limit market access in various areas, including through the application of soda ash import restrictions, minimum reference prices on steel products and onerous labelling requirements.

b. Trade Dialogue

USTR Zoellick and Indian Minister of Trade and Industry Murasoli Maran agreed in August 2001 to operationalize the United States-India Trade Policy Working Group (TPWG) at the Ministerial level (this had been established in the Clinton Administration). The TPWG will facilitate regular consultations on the range of trade issues between the United States and India.

c. WTO Balance of Payments Case

The United States prevailed in its WTO challenge to India's Balance of Payments (BOP) trade regime, leading India to eliminate bans, restrictive licensing, and other quantitative restrictions (QRs) on imports of industrial, textile, and agricultural products for the first time in 50 years. In 1999, BOP restrictions applied to approximately 15 percent of India's tariff lines. Virtually all consumer goods were affected, as were many agricultural, textile, and petroleum-related products.

In 1997, during India's consultation with the WTO Committee on Balance of Payments Restrictions, the International Monetary Fund stated that India no longer had a BOP crisis necessitating recourse to the GATT BOP exception. However, India insisted on at least six years to remove the BOP QRs. Following unsuccessful settlement talks with India, the United States initiated dispute settlement proceedings against India in 1997. The WTO panel issued its final report in April 1999 affirming the U.S. contention that these measures were inconsistent with India's WTO commitments. India appealed the decision but the Appellate Body rejected India's claim that its balance of payments situation justified import restrictions.

On December 28, 1999, the United States and India reached an agreement to lift these restrictions. Under the agreement, India eliminated one-half, or 714, of its 1,429 QRs on March 31, 2000. Restrictions on the remaining 715 items were eliminated by April 1, 2001. Eliminating these restrictions offers new market access opportunities for U.S. producers in key sectors such as textiles, agriculture, consumer goods, and a wide variety of manufactured products. India had previously reached agreements with the EU, Japan, and other trading partners to remove these restrictions by April 2003. The agreement with the United States advanced that time table by two years.

d. Intellectual Property Rights and the WTO TRIPS Mail Box

As a signatory to the Uruguay Round of GATT trade negotiations, India was required to comply with most of the obligations of the TRIPS Agreement by January 1, 2000, and must introduce a comprehensive patent system for pharmaceuticals and agricultural chemicals no later than 2005. The Indian Government has announced its intention to conform fully to the IPR-related requirements of the Uruguay Round. In December 1999, Parliament successfully passed three IPR related bills: the Copyrights Amendment Bill, the Trademark Bill, and the Geographic Indicators Bill. While the copyright law is generally compliant with the TRIPS Agreement, the 1999 amendments undermine TRIPS requirements concerning protection for computer programs. In 1999, the Parliament failed to amend the Patents Act and, thus, apparently failed to meet fully its WTO TRIPS obligations by the January 1, 2000 deadline. The Patents Act was originally expected to pass the Parliament in July 2000, and subsequently in November 2000, but remains mired in Committee nearly one year past its original submission to Parliament. Even should the bill eventually pass, several provisions still appear to be inconsistent with the TRIPS Agreement.

In April 1999, the United States and India resolved the WTO dispute brought by the United States regarding India's implementation of Articles 70.8 and 70.9 of the TRIPS Agreement. Through the enactment of the Patents (Amendment) Act 1999 and its accompanying regulations, India established a mechanism for the filing of so-called "mailbox" patent applications and a system for granting exclusive marketing rights for pharmaceutical and agricultural chemical products.

e. Auto TRIMS

The United States considers India's measures affecting trade and investment in the motor vehicle sector to be inconsistent with India's obligations under Articles III and XI of the GATT and Article 2 of the Agreement on Trade-Related Investment Measures. Indian policies require manufacturing firms in the motor vehicle sector to achieve specified levels of local content; to achieve a neutralization of foreign exchange by balancing the value of certain imports with the value of exports of cars and components over a stated period; and to limit imports to a value based on the previous year's exports.

On June 1999, the United States requested consultations with the Government of India pursuant to the WTO Dispute Settlement Understanding (DSU) and these consultations were held on July 20, 1999. The United States and the EU requested panels, which subsequently were merged. On December 21, 2001, the final panel report was released, confirming that WTO Members cannot impose local content requirements or trade balancing requirements on companies doing business in their countries, thus rejecting India's defense of its regime. India appealed the panel's report on January 31, 2002.

f. GSP

In December 1998, the United States accepted the petition of the American Natural Soda Ash Corporation (ANSAC) to withdraw, suspend or limit the application of GSP treatment to Indian imports. The subcommittee accepted the petition because of the lack of market access in the Indian market stemming from the injunction of the Indian Monopolies and Restrictive Trade Practices Commission barring ANSAC imports. In India's FY1999-2000 budget, it raised the import tariff on soda ash to 38.5 percent, the highest import tariff on soda ash in the world. Coupled with other excise taxes and charges, importers faced levies of nearly 70 percent at the border. A public hearing was held on March 23, 1999.

On February 28, 2001, as part of the FY2001-2002 budget, the Government of India announced a reduction in the duty on soda ash to 20 percent. When coupled with reduced excise taxes and charges, the aggregate border levy was reduced to about 45 percent. Discussions between the U.S. and Indian Government on the injunction barring ANSAC imports (but not imports from individual ANSAC members) continued in 2001 and are ongoing.

g. Reference Pricing

In December 1998, three weeks after imposing antidumping duties on certain steel products, the Government of India established minimum reference prices for certain other imported steel products: hot-rolled steel coils, cold rolled steel coils, hot-rolled sheets, and alloy steel bars and rods. Under this regime, India prohibits the import of these products when the import values are below the established minimum price. India had noted that the regime was adopted to discourage dumping. U.S. industry is concerned that this practice, which violates India's obligations under the Customs Valuation Agreement, could divert imports to the United States.

Minimum prices on steel were withdrawn on January 1, 2000, for primary products but still apply to secondary merchandise. In the spring of 2000, the Indian steel industry challenged the Indian Government's elimination of the regime for primary products. The Supreme Court of India reinstated the regime for these products while it considers the petitioner's claim. To date, the Supreme Court has not issued a final decision and the regime remains in place for both primary and secondary products. The U.S. Government is evaluating the appropriate response to this situation.

h. Other Import Barriers

Throughout the year, USTR and the interagency community worked with the U.S. Congress and U.S. industry to address a variety of measures which impede U.S.-India trade. These measures include longstanding issues, including high tariff and non-tariff barriers to the Indian market for U.S. textile and agricultural products and other, newer measures that have appeared as India has eliminated its regime of BOP-related quantitative restrictions.

5. People's Republic of China

Overview

Our China trade policy goals have been to open China's markets to American exports, support Chinese domestic economic reform, and integrate China into the Pacific and world economies. We have used a variety of means to achieve these goals, including commercially meaningful agreements that create opportunities for Americans. These efforts culminated in the accession of China to the WTO in December 2001, which followed the formal approval of China's accession agreement by WTO Ministers at Doha, Qatar, in November 2001, ending 15 years of often intense and difficult negotiations in which the United States had taken a leading role among WTO members.

To realize the full benefits of China's WTO accession requires extensive monitoring and enforcement. We have put into place a comprehensive interagency monitoring effort and are prepared to use our trade laws to secure compliance, where necessary. China's status as a WTO member will provide new means and focus for U.S. efforts. We will benefit from the multilateral monitoring efforts mandated by China's terms of accession through which we will be able to work with 142 other WTO members instead of acting alone when addressing compliance problems. We can also use WTO dispute settlement where necessary.

2001 Activities

In 2001, the United States played a key role in negotiating the multilateral portion of China's WTO accession, achieving important concessions in areas of interest to U.S. firms. Upon China's accession, an expert group was formed under the TPSC in Washington and a WTO Coordination Committee was established within the Mission in Beijing to monitor China's implementation of its commitments. The Departments of Commerce and State continued to devote considerable resources to building an understanding among the Chinese of China's WTO obligations.

China's accession to the WTO in December 2001 was facilitated by two key events, the historic U.S.-China bilateral market access agreement reached in November 1999 and the subsequent enactment in October 2000 of legislation permitting the grant of permanent normal trade relations (PNTR) to China. Building upon a record of bipartisan Congressional support for a market-opening China trade policy, the PNTR legislation authorized the President to terminate application of Section 402 of the 1974 Trade Act (the Jackson-Vanik Amendment), which had mandated annual reviews of China's receipt of normal trade relations treatment, and to grant China PNTR treatment if the President could certify that the final terms of China's accession were at least equivalent to those agreed bilaterally between the United States and China in November 1999. The President issued his report on certification in November 2001, and his subsequent proclamation granting PNTR status to China became effective January 1, 2002.

a. WTO Accession

i. Background

In July of 1986, China applied for admission to the General Agreement on Tariffs and Trade (GATT 1947). The GATT formed a Working Party in March of 1987, composed of all interested GATT contracting parties, to examine China's application and negotiate terms for China's accession. For the next eight years, negotiations were conducted under the auspices of the GATT Working Party. Following the formation of the WTO on January 1, 1995, a WTO Working Party, composed of all interested WTO members, took over the negotiations.

Like all GATT and WTO accession negotiations, the negotiations with China had three basic aspects. First, China provided information to the Working Party regarding its trade regime. China also updated this information periodically during the 15 years of negotiations to reflect changes in its trade regime. Second, each interested WTO member negotiated bilaterally with China regarding market access concessions and commitments in the goods and services areas, including, for example, the tariffs on industrial and agricultural goods and the commitments that China is making to open up its market to foreign services suppliers. The most trade liberalizing of the concessions and commitments obtained through these bilateral negotiations were consolidated into China's Goods and Services Schedules and now apply to all WTO members. Third, overlapping in time with these bilateral negotiations, China engaged in multilateral negotiations with Working Party members on the rules that govern trade with China. The rules commitments made by China in this area are set forth in its Protocol of Accession and an accompanying Report of the Working Party.

With its accession to the WTO, China is implementing significant changes to its trade regime, at all levels of government. Although it has been gradually transitioning toward a market economy from what had been a strict command economy two decades ago, China has now taken on the far-reaching obligations of the WTO, a rules-based system that requires its members to operate with openness and transparency and stresses the central role of markets and private enterprise.

In order to accede to the WTO, China has committed to undertake important systemic reforms, which should facilitate business dealings. China has also committed to take concrete steps to remove trade barriers and open its markets to foreign companies and their exports from the first day of accession in virtually every product sector and for a wide range of services. Supporting these steps, China has also committed to eliminate or significantly reduce restrictions on the rights of foreign companies to import and export goods and to distribute goods within China, and it has further committed to rectify numerous trade-distortive industrial and agricultural policies.

The openness, accountability and changes required by China's commitments should strengthen and accelerate the achievement of China's economic reform goals. China's ministries and agencies will transition out of their old role of directing and controlling how and with whom Chinese enterprises do business. Increasingly, they will need to focus on the implementation and enforcement of laws, regulations and other measures that will help to promote the smooth functioning of markets. Meanwhile, State-owned enterprises will face greater accountability for their business decisions, and together with other Chinese enterprises they will face the full forces of global competition for the first time.

ii. Systemic Reforms

China committed to implementing broad reforms in the areas of transparency, notice and comment, uniform application of laws and judicial review. Each of these reforms will strengthen the rule of law in China and help to address practices that have made it difficult for U.S. and other foreign companies to do business in China.

iii. Adherence to Existing Multilateral WTO Agreements

As a WTO member, China assumes the obligations of more than 20 existing multilateral WTO agreements covering all areas of trade, with only minimal transition periods, where necessary. Consequently, China will be taking on the obligations of the GATT, the WTO agreement that lays down core principles, such as non-discrimination and national treatment, that constrain and guide national trade policies as well as other WTO agreements, such as those governing agriculture, sanitary and phytosanitary measures, technical barriers to trade, trade-related investment measures (TRIMS), trade-related intellectual property rights (TRIPS), services (GATS), subsidies, import licensing, rules of origin, customs valuation and preshipment inspection.

iv. China-Specific Trade-Liberalizing Commitments

China's accession agreement also includes numerous China-specific trade-liberalizing commitments. One of the most significant of these commitments involves trading rights. Prior to its accession, China restricted the number of companies with trading rights, *i.e*, the right to import and export goods, and the products that a particular company can import or export. China agreed to phase-in trading rights, so that all enterprises in China and all foreign enterprises and individuals will have full trading rights within three years after accession.

Perhaps equally significant is China's commitment regarding distribution services. Prior to its accession, China generally did not permit foreign companies to distribute products through wholesale and retail systems in China or to provide related distribution services, such as repair and maintenance services. China agreed to phase-out these prohibitions over three years, subject to limited exceptions.

China also committed to the phase-out of trade-distortive non-tariff measures (NTMs), such as quotas and licenses, covering hundreds of products. Most of these NTMs must be eliminated upon accession, while the remainder of them must be eliminated within three years after accession.

China further committed to the elimination of import monopolies maintained by State trading enterprises in China on many industrial goods upon accession. It must also provide full information on the pricing mechanisms of state trading enterprises, to limit the mark-up on goods that they import in order to avoid trade distortions and otherwise to ensure that their import purchasing procedures are transparent and fully in compliance with WTO rules.

China's accession agreement includes many provisions directly or indirectly addressing state-owned enterprises. China agreed that laws, regulations and other measures relating to the purchase and commercial sale and production of goods or supply of services for commercial sale by state-owned enterprises or for use in non-governmental purposes are subject to WTO rules. China also agreed that state-owned enterprises must make purchases and sales based solely on commercial considerations, such as price, quality, marketability and availability, and that the government will not influence the commercial decisions of state-owned enterprises.

In an annex to its accession agreement, China provided detailed information on the limited number of products and services subject to price control or government guidance pricing and the procedures for establishing prices. China may not use price controls to restrict the level of imports of goods or services.

Finally, China committed to non-discrimination in the treatment of enterprises within its special economic areas.

v. Tariff Reductions

When China's Goods Schedule went into effect shortly after China acceded to the WTO, greatly increased market access was realized by U.S. and other foreign companies through cuts in China's tariffs on industrial and agricultural goods. Although these reductions generally take place over a period of five years, in almost all instances most of the reductions took place immediately on January 1, 2002.

Tariffs on industrial goods of greatest importance to U.S. businesses were reduced from a base average of 25 percent (in 1997) to 7 percent. More specifically, China agreed to participate in the Information Technology Agreement, which requires the elimination of tariffs on computers, semiconductors and other information technology products. China's elimination of these tariffs will be completed by January 1, 2005. China also agreed to implement tariff reductions on more than two-thirds of the 1,100-plus products covered by the WTO's Chemical Tariff Harmonization Agreement. In addition, tariffs on autos were to be reduced from 80-100 percent to 25 percent (by July 1, 2006), and tariffs on auto parts were to be reduced from a base average of 23 percent to 9.5 percent (by January 1, 2006). Tariffs in the wood and paper sectors were to be reduced from a 1997 average of 18 percent on wood and 15-25 percent on paper to 5 percent and 7.5 percent, respectively.

Tariffs on agricultural goods of greatest importance to U.S. farmers were to be reduced from a 1997 average of 31 percent to 14 percent.

vi. Services Commitments

As set forth in China's Services Schedule, 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. Notably, these commitments represent only the minimum level of market access that China will be expected to make available once it becomes a WTO member. Nothing in China's Services Schedule precludes the Chinese government from applying more liberal measures that would allow foreign companies to provide services with even fewer limitations on market access.

vii. Enforceability

WTO members established a multilateral review mechanism at the WTO of unprecedented scope and authority. This so-called "Transitional Review Mechanism" operates annually for 8 years after China's accession, with a final review in year 10. It requires China to provide detailed information, to report to Washington on its implementation efforts, and to give all WTO members the opportunity to raise questions, in a multilateral setting, about how China is complying with its commitments before 16 subsidiary WTO bodies, which report to the WTO's General Council. The General Council then conducts an overall review each year and may issue recommendations.

Normal WTO dispute settlement procedures remain available to enforce all of the rights of the United States and other WTO members under the WTO agreements, including with regard to the commitments in China's accession agreement.

viii. Safeguard Mechanisms

Even though the terms of China's accession agreement are directed at the opening of China's market to WTO members' industries, China's accession agreement also includes several safeguard mechanisms designed to prevent injury that U.S. or other WTO members' industries and workers might experience based on unfair trade practices or import surges.

For 15 years after China's accession to the WTO, the United States and certain other WTO members will continue to have the ability to utilize a special non-market economy methodology for measuring dumping in anti-dumping cases against Chinese companies

China's accession agreement also includes a unique, China-specific safeguard provision allowing a WTO member to restrain increasing Chinese imports that disrupt its market. This mechanism applies to all industrial and agricultural products and will be available for 12 years after accession.

Additionally, the accession agreement includes a special textiles safeguard, which will be available for 7 years after accession (until December 31, 2008). This safeguard covers all products subject to the WTO Agreement on Textiles and Clothing as of January 1, 1995.

Finally, the United States (and other WTO members) will continue to have the rights under WTO rules to maintain, for example, its export control policies and to prevent the import of Chinese goods made with prison labor.

ix. U.S. Monitoring and Enforcement Efforts

Given China's importance as a major trading power and the breadth and complexity of China's WTO commitments, the U.S. Government initiated a comprehensive and coordinated interagency monitoring effort to ensure that China complies with its commitments. As part of this effort, the U.S. Government will be active on several fronts. In China, State Department economic officers, Foreign Commercial Service officers, Foreign Agricultural Service officers and Customs attaches will gather information and work with U.S. companies and assist them in doing business in China. In Washington, an interagency team of experts, led by USTR, drawing on the assistance of the U.S. Government personnel in China as well as trade associations, chambers of commerce, industry and agriculture groups and individual companies, will closely monitor China's compliance efforts. In Geneva, USTR and other concerned agencies will also be active participants in the WTO's annual

Transitional Review Mechanism.

Where the U.S. Government finds systemic problems and potential WTO violations, it will act quickly to resolve them through all available mechanisms. It will use bilateral means, including U.S. trade laws, the WTO's multilateral Transitional Review Mechanism and WTO dispute settlement proceedings, as necessary. This effort will be greatly enhanced by the placement of overseas trade compliance officers from the Commerce Department and other agencies in our embassies in key trading partners.

b. Agriculture

China's WTO membership is a huge step forward for the U.S. agricultural community in its long sought objective to gain direct access to China's market for U.S. agricultural products and, in particular, its aim to remove China's remaining unjustified sanitary and phytosanitary barriers. Previously, in 1992, China signed a bilateral Memorandum of Understanding on Market Access with the United States, agreeing to remove unjustified technical barriers to imports of U.S. agricultural commodities. Although China agreed to address these issues within one year, access issues for several products remains limited.

On April 10, 1999, just months before finalizing their November 1999 bilateral WTO agreement, the United States and China signed an Agreement on U.S. - China Agricultural Cooperation (ACA), which eliminated technical barriers in China to imports of U.S. citrus, meat and poultry, wheat, and other grains. The signing of this agreement facilitated and greatly enhanced the strong positive support for PNTR by the agricultural community. While trade to China has increased for U.S. citrus, grains, red meat and poultry under the 1999 ACA, China's compliance with this agreement has been inconsistent and U.S. exporters still do not have the access envisioned in the agreement. While China agreed to recognize the U.S. inspection system for meat and poultry, for example, it has erected new barriers to poultry imports with new regulations (issued December 1, 2000), which it eventually revised and republished in February 2001. China's regulatory stance on poultry was primarily intended to deal with a long-standing smuggling problem. But, the result was to impose confusion and raise concerns among traders. Most recently, in late 2001, China insisted that imported U.S. chicken paws carry a "Certificate of Wholesomeness" declaring them to have been inspected and found fit for human consumption by the Food Safety and Inspection Service, requiring the U.S. poultry industry to modify processing plant operations.

In the 1999 ACA, China also agreed to remove phytosanitary barriers to citrus exports from Arizona, California, Florida and Texas over a two-year phase-in period. While it implemented the first tranche on schedule, China delayed implementation for remaining counties in California and Florida three months beyond the October 2000 deadline, finally implementing the agreement for those counties on January 18, 2001. China has not responded to the February 2001 Animal and Plant Health Inspection Service's request to add five more counties (one in California and four in Florida) to the export list for China.

China also agreed to remove phytosanitary barriers to wheat and other grains from the Pacific Northwest beginning April 1999. In marketing year 2000/2001, wheat shipments from the Pacific Northwest totaled 233,000 tons, but China periodically detained U.S. wheat shipments, subjecting them to unwarranted special handling requirements and other actions not consistent with the ACA. As of November 2001, 142,000 tons of sales have been made, 120,000 tons of which have already been exported. No U.S. wheat is currently detained.

Bilateral negotiations on remaining sanitary and phytosanitary issues continue, with barriers still in place on plums, additional varieties of apples, potatoes and pears.

With its accession to the WTO, China took on the obligations of the WTO Agreement on

Agriculture. China also made several additional commitments that will help to rectify numerous agricultural policies upon accession or after limited transition periods. For example, China committed to eliminate export subsidies upon accession, and it has agreed to a cap for trade and production-distorting domestic subsidies that is lower than the cap permitted developing countries and that includes the same elements that developed countries use in determining whether the cap has been reached. In addition, China committed to implement tariff-rate quotas that provide significant market access for bulk goods of special importance to American farmers such as grains, soy oil and cotton upon accession. China also agreed to eliminate import monopolies maintained by State trading enterprises on agricultural goods such as wheat, rice and corn and to permit non-State trading enterprises to import them.

c. Intellectual Property Rights

For more than a decade, the United States and China have engaged in detailed discussions regarding the improvement of China's protection of intellectual property rights and market access for products with intellectual property rights protection. In January 1992, the United States and China reached an agreement on improved protection for U.S. inventions and copyrighted works, including computer software and sound recordings, trademarks, and trade secrets. This Agreement focused principally on revisions to China's laws and membership in international intellectual property rights agreements, including the Berne Convention for the Protection of Literary and Artistic Works, the Universal Copyright Convention, the Geneva Phonogram Convention, the Patent Cooperation Treaty, and the Madrid Protocol on the Protection of Marks.

Although China improved the legal framework for intellectual property rights protection based on the 1992 bilateral agreement, enforcement of those laws was seriously deficient. In 1995, the United States and China reached a second agreement that focused on intellectual property rights enforcement and market access issues.

Based on our 1995 IPR Agreement and the Administration's continuing bilateral efforts, China has developed a basic infrastructure for the protection and enforcement of intellectual property rights. Implementation of our bilateral intellectual property rights agreements provided a basis for China's commitment to implement the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) upon accession to the WTO. Additional improvements to China's laws and training of judges and enforcement personnel are essential. U.S. and Chinese rights-holders can seek administrative and judicial remedies for infringement of their intellectual property rights; however, administrative sanctions need to be increased and the threshold to initiate criminal investigations needs to be lowered. China has formally issued a decree to address the "end-user" computer software piracy issue in connection with government purchase and use of legitimate software.

As a result of intensive bilateral implementation and enforcement negotiations in 1996, China has made further progress on enforcement of intellectual property rights. For example, Chinese authorities have shut down over 100 illegal CD, CD-ROM and VCD production facilities. This effort has changed China from an exporter of pirated material to being the import target for pirated product from other countries in the region.

China also is improving customs enforcement of intellectual property rights. Each year customs authorities seize millions of pirated CDs, CD-ROMs and VCDs. Since the importation of pirated product has been on the increase, we have encouraged enhanced cooperation with regional customs authorities, such as those in Hong Kong and Macau, Vietnam and others, to stop this trade in pirated product.

Under our bilateral agreements, market access for computer software, motion pictures, videos and sound recordings have improved. China has also made further commitments on market access in the context of our November 1999 bilateral WTO agreement, which have now been incorporated into China's accession agreement.

i. Further Steps to Improve Protection for IPR and Market Access

China's last major revisions to its intellectual property rights laws and regulations occurred after the 1992 Bilateral Agreement. Based on its experience in implementing its intellectual property rights laws, Chinese authorities have revised the copyright, patent and trademark laws and are taking further steps necessary to comply with the requirements of the TRIPS Agreement. The United States has also urged China to do a comprehensive amendment to its copyright laws to implement two copyright-related agreements negotiated under the auspices of the World Intellectual Property Organization (WIPO) that China has signed but not yet ratified.

Chinese enforcement of copyrights and trademarks is still uneven from province to province. Guangdong province, for example, has significantly increased sanctions against piracy and counterfeiting. We are encouraging the national government and/or the other provinces to do likewise. Of concern is the unauthorized use of software by private enterprises (end-user piracy). Piracy rates of entertainment software (game compact discs) and other audiovisual products are also very high. Although strong steps have been taken to address the production of pirated software, CDs and VCDs, far too many pirated products remain available at the retail level.

Trademark counterfeiting in China has worsened considerably. During recent discussions we have also raised the growing problem with trademark counterfeiting, particularly in the area of consumer goods, protection for unregistered well-known trademarks and effective enforcement against counterfeiters. In part to address these concerns, the Chinese launched a nationwide anti-counterfeiting campaign in October 2000. The results are as yet inconclusive.

Access for foreign sound recordings has improved, but restrictions on distribution remain a key concern. Although imports of foreign video titles have increased rapidly, the Chinese still impose an unofficial quota on foreign motion pictures that are distributed on a revenue-sharing basis. China maintains this limit through a state-owned import monopoly.

China committed in its November 1999 bilateral WTO agreement with the United States to increase market access for the audiovisual sector, and these commitments were subsequently incorporated into China's accession agreement. China will allow foreigners to distribute videos, entertainment software and sound recordings through joint ventures, and will allow the importation of 20 motion pictures annually on a revenue sharing basis.

ii. WTO Agreement on Trade-Related Intellectual Property Rights

With its acceptance of the TRIPS Agreement when it acceded to the WTO, China took on the obligation to adhere to internationally accepted norms to protect and enforce the intellectual property rights of U.S. and other foreign companies and individuals in China. In 2001, as part of its efforts to comply with the TRIPS Agreement, China was in the process of modifying the full range of intellectual property laws and regulations, including those relating to patents, trademarks, trade secrets, integrated circuits and copyrights. In addition, provisions in its accession agreement require China to strengthen the enforcement of these laws and regulations by its courts and the responsible administrative agencies.

d. 1992 Market Access Agreement

The United States and China signed a Memorandum of Understanding on Market Access in 1992. This Agreement committed China to changes in its import regime over a five-year period, including increased transparency, elimination of quotas and licenses, a guarantee that no trade law or regulation could be enforced unless published, uniform application of trade rules, elimination of import substitution policies, and agreement that any sanitary and phytosanitary measures would be based on sound science. While China phased-out formal measures, such as certain quotas and licenses, serious problems remained during 2001 as China continued to restrict imports by retaining non-uniform application of trade rules, import substitution policies and use of sanitary and phytosanitary (SPS) standards.

China's accession agreement includes these same commitments as well as many additional ones. Consequently, the commitments made by China in the 1992 Memorandum of Understanding have been, in effect, multilateralized, and therefore the United States will no longer be alone in seeking compliance from China.

e. Satellite Launch Services

The 1989 Bilateral Agreement on International Trade in Commercial Launch Services with China was extended in 1995 to cover the period through 2001. The Agreement was intended to balance the interests of the U.S. satellite and commercial space launch industries, while encouraging free trade by allowing China to enter the international market for commercial space launch services in a fair and non-disruptive manner. The extended Agreement continued quantitative and pricing disciplines established under the earlier Agreement. The Agreement also specifically provided that nothing in the Agreement limited the operation of U.S. export control laws.

In March 2001, the government of China hosted a delegation from the United States for consultations under the terms of the Agreement. The consultations included an exchange of information on the commercial satellite launch market and new developments in China's commercial space program as well as a review of the implementation of the Agreement.

The Agreement expired, pursuant to its terms, on December 31, 2001. No determination has been made regarding any future arrangement with China governing international trade in commercial launch services.

6. Japan

The United States redoubled its efforts in 2001 to promote deregulation and structural reform, improve market access for U.S. goods and services, and support the adoption and successful implementation of pro-competitive policies throughout the Japanese economy. The United States has been encouraged by positive trends in corporate restructuring and Prime Minister Koizumi's determination to "promptly and swiftly" carry out regulatory reform. Nonetheless, the Japanese economy continues to underperform largely as a result of structural rigidities, excessive regulation, and market access barriers. Over the past year, the U.S. Government and the Government of Japan have addressed concrete steps for Japan to further open and deregulate its markets. These measures will help Japan revitalize its economy and generate sustainable economic growth in the medium and long-term.

The United States also relied on a wide range of regional and multilateral fora in 2001, including the WTO and APEC, to advance its trade agenda with Japan. The United States is working to ensure that our trade priorities in these fora, including on agriculture and services, are well coordinated with our bilateral agenda so that the various initiatives are mutually reinforcing and complementary.

The highlights of our 2001 bilateral and multilateral trade agenda with Japan follow.

Overview of Accomplishments in 2001

U.S.-Japan Economic Partnership for Growth

The United States promoted much-needed regulatory reforms and obtained improved access for U.S. goods and services in a number of areas in Japan in 2001. The most significant step forward was the launch of the U.S.-Japan

Economic Partnership for Growth (the Partnership) by President Bush and Prime Minister Koizumi in June 2001. The main objective of the Partnership is to promote sustainable growth in both countries by addressing such issues as sound macroeconomic policies, structural and regulatory reform, financial and corporate restructuring, foreign direct investment, and open markets. A key feature woven into the various components of the Partnership is the opportunity for the U.S. and Japanese private sectors to be more fully integrated in our bilateral economic work. This has been done to help cultivate creative solutions to the economic and trade challenges facing our two countries and nurture stronger private-sector support for pro-reform policies. While regulatory and structural reform remains of paramount importance, the United States and Japan will also address new and lingering trade issues in a variety of sectors.

The following provides a brief description of each component of the Partnership along with 2001 accomplishments:

Subcabinet Economic Dialogue: Co-chaired by the NSC/NEC and Japan's Ministry of Foreign Affairs (MOFA), the "Subcabinet" sets the tone and direction of the Partnership, with Deputy/Vice Ministerial level officials meeting on an annual basis to discuss a broad range of bilateral, regional, and multilateral issues. Recommendations from these meetings are given to the respective Governments for use in developing policy. At the first meeting in October 2001, participants covered a range of issues, including the problem of non-performing loans in Japan and bilateral cooperation on terrorism. The next meeting is expected in early 2002, coincident with the first meeting of the Private Sector/Government Commission, which is described below.

Private Sector/Government Commission: The "Commission," which is led by USTR and the Department of Commerce, is designed to integrate the U.S. and Japanese private sectors more fully into the economic work of the two Governments. Private sector delegates from Japan and the United States will meet annually with the Subcabinet to discuss issues of key importance to both countries. The first meeting will convene in early 2002 to address the topic "Creating an Environment for Sustainable Growth: Raising Productivity and Corporate Revitalization" and will focus on corporate restructuring.

Regulatory Reform and Competition Policy Initiative: Co-chaired by USTR and MOFA, the "Regulatory Reform Initiative," which is detailed further in section 1 below, aims to promote economic growth and open markets by focusing on sectoral and cross-sectoral issues related to regulatory reform and competition policy. In an effort to create a new, constructive tone in the U.S.-Japan bilateral trade and economic relationship, the United States has made a concerted effort to focus on issues that Prime Minister Koizumi and his Administration have identified as important areas for reform, such as information technologies, telecommunications, medical devices and pharmaceuticals, energy, and competition policy. Working Groups met throughout the fall of 2001, setting the stage for a High-level Officials Group meeting in early 2002.

Investment Initiative: The Investment Initiative addresses laws, regulations, policies, and other measures intended to improve the climate for foreign direct investment (FDI). Led by the Department of State and Japan's Ministry of Economy, Trade, and Industry (METI), the first "Investment Group" met in October 2001 in Washington just prior to the Subcabinet meeting. Key topics discussed included recent developments related to FDI in the United States and Japan, while investment issues to be taken up in 2002 include mergers and acquisitions, and tax, labor and land policy.

Financial Dialogue: The Financial Dialogue serves as a forum for the Department of Treasury, Japan's Ministry of Finance (MOF) and the Financial Services Agency (FSA) to exchange information on key macroeconomic and financial sector issues, including non-performing loans. As appropriate, the report to the leaders under the Regulatory Reform Initiative will include progress in financial sector liberalization achieved under this Dialogue. The first meeting was held in November 2001 and future meetings will be held annually.

Trade Forum: The Trade Forum, which is led by USTR and MOFA, was created to foster focused and substantive discussion on a wide-range of sectoral trade issues of interest and concern to both Governments, including those related to the manufacturing, services, and agricultural sectors. It will also serve as an "early warning" mechanism to facilitate resolution of emerging trade problems. The first meeting of the Trade Forum, which will meet at least annually, is expected to take place in early 2002.

Fourth Joint Status Report

In June 2001, the United States and Japan issued the Fourth Joint Status Report under the Enhanced Initiative on Deregulation and Competition Policy (the Enhanced Initiative), the precursor to the Regulatory Reform Initiative. Japan agreed to a number of important deregulation measures in the report, and notable achievements were made in various sectors, including telecommunications, information technology, energy, medical devices and pharmaceuticals, financial services, and housing. Important progress was also made in key areas such as competition policy, transparency and other government practices, legal system reform, revision of Japan's Commercial Code, and distribution. (The deregulation measures undertaken in these sectors and areas are highlighted in the Regulatory Reform section below.) The two Governments affirmed in the Fourth Joint Status Report their determination to build upon the progress achieved under the Enhanced Initiative through the Regulatory Reform Initiative.

Automotive Consultations

A third significant accomplishment in 2001 was the creation of the Automotive Consultative Group (ACG) to address barriers in, and improve U.S. companies' access to, the domestic Japanese automotive market and Japanese auto plants in the United States. The Bush Administration is committed to addressing the U.S. auto and auto parts industries' concerns related to Japan, and the ACG will serve as the focal point for addressing lingering as well as emerging issues in this key sector of both countries' economies. More specifically, the group will assess trends in the industry based on a series of trade and economic data on autos and automotive parts to be provided by both countries and work to identify areas in which specific action can be taken by Japan to address U.S. concerns. The group will meet at least annually and will be co-chaired by the Department of Commerce and USTR on the U.S. side, and METI and the Ministry of Land, Infrastructure and Transport on the Japanese side. The first meeting is expected to take place in the first half of 2002.

In addition to meetings under the Automotive Consultative Group, the United States has continued to address cross-cutting issues impacting the automotive sector under the Partnership. This has included expanding opportunities for foreign investment, increasing transparency, and promoting corporate restructuring in the Japanese economy.

a. Regulatory Reform

A key component of the Partnership, the Regulatory Reform and Competition Policy Initiative, is designed to further deregulate the economy, and to bolster competition and open markets in Japan. It focuses on five key sectors: telecommunications, information technologies, energy, medical devices and pharmaceuticals, and financial services. The Initiative also addresses five important cross-cutting structural areas: competition policy, transparency and other government practices, legal system and infrastructure reform, commercial law, and distribution.

In October 2001, the United States presented

Japan with 47 pages of recommendations under the Initiative, which called on Japan to adopt bold regulatory reforms. Consistent with the overall objective of the Partnership, these recommendations include reform measures intended both to open markets and help Japan return to sustainable growth. Further, to create a more constructive tone in the U.S.-Japan bilateral trade and economic relationship, the United States made a concerted effort to focus on issues that Japan has identified as priorities for reform. Another important feature of this Initiative is integration of the private sector into the work of the two Governments. Working Groups meeting in November and December of 2001 included presentations from private sector officials, who offered their expertise, observations, and recommendations on key issues.

The October 2001 recommendations presented to Japan will serve as the basis for bilateral discussions over the coming year in a High-level Officials Group and the various Working Groups established under the Regulatory Reform Initiative. These discussions will in turn serve as the basis for an annual report to the President and Prime Minister in 2002 specifying the progress made under this Initiative, including specific measures to be taken by each Government.

As mentioned above, the Regulatory Reform Initiative was preceded by the Enhanced Initiative and the deregulation achievements obtained during 2001 under the Enhanced Initiative were included in a Fourth Joint Status Report. This report was endorsed by President Bush and Prime Minister Koizumi in June 2001. Highlights of these achievements, together with key reform recommendations submitted this year to Japan under the Regulatory Reform Initiative are as follows:

i. Sectoral Regulatory Reform

Telecommunications: The inability of competitive telecommunications carriers to dislodge Nippon Telegraph and Telephone (NTT) from its control of 99 percent of subscriber lines and 60 percent of mobile customers has hampered access by residential and business users to innovative, low-cost services. The difficulties in establishing new competitive services in turn have restricted growth and investment in Japan's $130 billion telecommunications market, the world's second largest.

In the Fourth Joint Status report, Japan agreed to implement effective dominant-carrier regulation in all sectors of the telecommunications market in order to ensure that NTT's control does not impede competition. Regulations to implement "asymmetric regulation" over the mobile market and other improvements to regulation over essential wireline facilities enacted by the Diet in June 2001 took effect in November. These regulations added safeguards to prevent NTT from discriminating against competitors in favor of group companies, and will provide a basis for corrective measures to ensure cost-based interconnection to the network of the dominant mobile carrier, NTT DoCoMo. The regulations also will help competitors gain access to NTT's optical fiber, rights of way, switching offices, and other facilities, as well as to wholesale rates for services provided by NTT. The regulatory reforms were supplemented by guidelines written jointly by Japan's telecommunications ministry and the Japan Fair Trade Commission (JFTC) to clarify anticompetitive and other behavior that is proscribed by the Antimonopoly Act and the Telecommunications Business Law. In addition, Japan is developing guidelines to ensure that market entry by NTT East and NTT West into Internet or other services does not impair competition. Japan also will eliminate unnecessary regulations for carriers which do not possess market power in order to promote competitive services and new entrants. These reforms ease the regulatory burden facing new entrants by eliminating some filing tariffs and contracts and shifting from an approval system to a notification system for some filings.

In the Fourth Joint Status Report, Japan also agreed to ensure the fair, non-discriminatory and transparent provision of access to rights of way for carriers, facilitating their ability to build out their networks. Japan enacted some other measures to ensure cost-based access to NTT's fiber optic cables. Further, Japan will continue to reduce interconnection rates through the introduction of an appropriate costing methodology, improve the existing interconnection pricing model, and in the case of mobile interconnection, ensure that tariffs for NTT DoCoMo are publicly disclosed and reflect costs. In addition, Japan will ensure that any universal service funding mechanism is limited to basic voice services, open to competitors, and based on a cost model reflecting an efficient operator. In recognition of the need for an impartial dispute resolution function, Japan also set up the structure for a commission to handle disputes between carriers, which is a positive step towards fully separating regulation from the government's industrial promotion policies. These steps will clearly improve opportunities for access by U.S. firms to Japan's telecommunications sector because they begin to rebalance the overwhelming advantages NTT has had in its monopoly position in favor of new entrants, who have invested billions of dollars in new networks but have had little success in capturing significant market share. The added flexibility new entrants will gain in quickly introducing new services should accelerate innovation and price competition which is essential to stimulating overall growth in the telecommunications, information technology, and other key sectors.

In its October 2001 Regulatory Reform submission, the United States urged Japan to build on the progress achieved in the past year and complete the process of instituting and implementing a pro-competitive regime. The United States provided several recommendations to achieve this goal, including the establishment of a strong, independent regulator, divestiture of the government's shares in NTT, and the strengthening and implementation of dominant carrier regulation. Moreover, the United States called on Japan to continue reducing rates and to correct a sometimes skewed pricing structure that prevents new entrants from offering profitable services over the NTT network, and to fully evaluate whether a universal service subsidy program is necessary. In addition, the United States recommended that Japan eliminate unnecessary filing and reporting requirements and further facilitate access to infrastructure for competitive carriers, as well as expand the resale and unbundling of services and facilities to promote new competitive services. The first meeting of the Telecom Working Group took place in December 2001.

Information Technologies: Japan has recently embarked on an ambitious plan to become a global leader in information technologies (IT), which includes plans to revise laws for the digital age that will further facilitate electronic commerce. Even so, development of the Internet and electronic commerce in Japan lags behind other developed countries. As Japan responds to the challenges that lie ahead in this pivotal sector, the U.S. Government is working with Japan to promote a thriving IT sector that will provide significant opportunities for U.S. firms and their leading technology products in a market that is expected to reach nearly $136 billion by the end of 2004.

IT sectoral issues and problems were raised for the first time in conjunction with the Telecommunications Working Group under the fourth year of the Enhanced Initiative on Deregulation and Competition Policy, and in expert-level talks which took place in March 2001. To promote growth in its IT sector, Japan agreed in the Fourth Joint Status Report to take steps to strengthen the protection of intellectual property rights on the Internet by expeditiously ratifying the WIPO Performances and Phonograms Treaty, which would protect the rights of performers and producers of phonograms online. In addition, Japan will continue discussions with the U.S. Government to implement legislation in Japan so as to adequately and effectively protect copyright and related rights, and provide clear-cut Internet Service Provider (ISP) liability rules, as well as to ensure that temporary copies and business method patents are adequately protected under Japanese law. Moreover, Japan will promote the growth of electronic commerce with privacy legislation that protects personal information and facilitates paperless transactions by considering the amendment of existing laws and regulations which hinder the development of e-commerce. Japan also agreed in the Fourth Joint Status Report to promote electronic government procurement by creating a consolidated database for that purpose and introducing electronic bidding for public works projects. Japan also will work closely with the U.S. Government on network security issues.

A separate IT Working Group was established under the Regulatory Reform Initiative in June 2001. The primary focus of this working group is to work with Japan to establish an environment that will promote the development of IT-related businesses and innovative information technologies that can be utilized to spur growth in other key sectors of the economy and help Japan return to sustainable growth. In its October 2001 Regulatory Reform Initiative submission, the United States made several recommendations which focused on protecting intellectual property, increasing user confidence in electronic commerce, and reinforcing the leadership role of the private sector in IT, as well as proposals for cooperative efforts in the areas of electronic education, the promotion of electronic commerce and IT in the private sector, and network security. Specifically, the United States called on Japan to establish a legal framework that is appropriate for the digital age and strengthens the protection of intellectual property, particularly on the Internet, including the need for clear-cut and balanced ISP liability rules. Moreover, the United States made several recommendations for online privacy, consumer protection, and the facilitation of electronic transactions, including in government, which can spur greater use of IT and electronic commerce in the private sector and increased use of U.S. IT-related products and services. The United States conveyed these recommendations in detail during the first round of talks of the IT Working Group, which took place in November 2001.

Energy: With the highest energy prices in the OECD, Japan has taken steps in recent years to deregulate both its gas and electricity sectors. In 2000, for example, Japan opened 28 percent of its electricity market to competition, permitting large-lot customers to choose their electricity supplier. Despite these efforts to deregulate, the Japanese electricity market remains dominated by 10 vertically integrated regional utilities. As of August 2001, new entrants commanded a meager 0.39 percent of the newly liberalized portion of the electricity market. The gas sector has seen limited new entry as well. As a result, Japan's energy sector remains less efficient than it should be, innovation has been stifled, and new entry by domestic and foreign companies continues to be minimal.

In the fourth year of the Enhanced Initiative, the United States urged Japan to take bolder steps to promote a regulatory and competitive environment in both its wholesale and retail energy sectors. This would enable Japan to achieve its goals of reducing electricity costs to internationally competitive levels, while encouraging innovation and efficiency and increasing the share of natural gas in its primary energy supply. The United States also called on Japan to remove impediments that discourage market entry. To address these problems, Japan agreed in the Fourth Joint Status Report to promote open access to its electricity transmission grid by monitoring the transparency and neutrality of wheeling services and by conducting an audit of utility accounts to assess whether wheeling tariffs are just and appropriate. In addition, Japan agreed to foster fair and transparent treatment of new entrants' requests for transmission capacity expansion, and to facilitate new entry into electricity and gas markets through such means as consultations with potential market entrants and studies of existing regulatory requirements for siting new generating units, transmission lines, gas pipelines and LNG facilities. Japan also agreed to fully implement and enforce measures intended to ensure fair, open, and non-discriminatory access to its gas transportation services. Furthermore, Japan said it would actively enforce its Antimonopoly Act

(AMA) and relevant guidelines to promote access to electricity and gas markets, and conduct evaluations of the progress of electricity and gas market liberalization by 2003.

Building on progress achieved in the Fourth Joint Status Report, the United States made numerous energy sector recommendations in October 2001 under the Regulatory Reform Initiative. Initial working-level meetings were held a month later in Tokyo, where the United States recommended that Japan adopt numerous reforms measures to further liberalize its energy sector. The United States, for example called on Japan to articulate concrete measures to promote independence of the energy sector regulatory authorities in METI and define specific policy goals for the energy sector reform process. The United States also recommended that Japan take steps to promote equal access to transmission and retail services for all market participants, establish guidelines to determine the need for transmission construction, and promote construction between electricity service areas. In addition, the United States suggested that Japan expand transmission infrastructure in the gas sector, and promote a competitive gas and LNG market through unbundling and transparency of usage charges and information.

These reforms are designed to foster Japan's economic recovery, help U.S. firms compete in the Japanese electric and gas markets, and create new opportunities for competitively priced, high-quality exports to the Japanese market for electrical generation equipment.

Medical Devices and Pharmaceuticals: Continued over-regulation, inefficiencies, and a misguided focus on short-term budget savings have slowed the introduction of innovative and cost-effective products into Japan's medical device, pharmaceutical, nutritional supplement, and health care delivery sectors. Increasing the availability of these products is key to helping Japan meet the challenge of providing increased quality health care to its aging population while containing overall health care costs.

In the Fourth Joint Status Report, Japan agreed to take twenty-four concrete deregulation measures that are critical to ensuring that the steady stream of innovative medical devices and drugs being developed by U.S. firms gain timely access to the Japanese market. Importantly, Japan agreed to ensure that its reform of medical device and pharmaceutical pricing systems would result in appropriate valuations for innovative products. The U.S. Government is very concerned, however, that severe fiscal and political pressures are leading Japan to undertake pricing reforms that will contravene its Enhanced Initiative agreements. The United States is actively engaging Japanese officials at all levels to ensure that Japan does not implement reforms that arbitrarily target U.S. products for price reductions.

Although pricing issues have become a source of trade friction, issues relating to the regulatory approval of medical devices and pharmaceuticals are moving forward. Consistent with its Enhanced Initiative agreements, Japan has taken steps to harmonize its application review and approval processes and improve and expand the use of foreign clinical data. These steps are critical to enhancing the transparency and consistency of regulatory approvals, which are helping to reduce approval times, lessen burdens on applicants, and expedite patient access to new treatments. Japan also implemented a new system to allow nutritional supplement manufacturers to make health benefit claims. Lastly, Japan relaxed regulations governing advertising by hospitals to allow for more comprehensive service information to be offered to patients.

Building on these steps, the United States in its October 2001 Regulatory Reform Initiative submission proposed that Japan: 1) introduce competitive market forces and pursue structural reforms by improving public access to medical information and expanding the roles of private companies in hospitals and nursing care facilities; 2) encourage the introduction of innovative medical devices and pharmaceuticals and ensure that these products receive timely and appropriate valuations; 3) continue to expedite regulatory approvals of medical devices and pharmaceuticals, particularly for products that are available in other countries; 4) continue to work within the International Council on Harmonization process to promote broader use of foreign clinical data and facilitate more efficient utilization of Japan's clinical trial system; and 5) further deregulate the sale of nutritional supplements. The United States elaborated on these recommendations at the first meeting of the Medical Devices and Pharmaceuticals Working Group, which met in November 2001.

Financial Services: The Government of Japan has implemented the majority of its "Big Bang" financial deregulation initiative, which aimed to make Tokyo's financial markets "free, fair and global" by allowing new financial products, increasing competition within and between financial industry segments, and enhancing accounting and disclosure standards. "Big Bang" liberalization has substantially improved the ability of foreign financial service providers to reach customers in most segments of the Japanese financial system.

In mid-2001, the Financial Services Agency (FSA) announced a package of securities market reforms, including the prohibition of broker churning. October brought the long-awaited introduction of defined contribution pensions, the removal of the ban on corporate holding of their own stock acquired through buy-backs, and the introduction of safe-harbor rules to reduce insider trading and market manipulation. In April 2001 Japan increased the access of investment advisory companies to fund management of public pension funds by allowing funds to be managed through a direct, on-shore trust arrangement, and by eliminating the requirement to convert investment holdings to cash when changing fund managers. To improve the transparency and predictability of the regulatory process, the FSA has initiated a system of response to written inquiries, including requests for published guidance and "no-action" letters. Banks were granted limited entry into the insurance business in April 2001, and further removal of restrictions on banks' insurance activities is under consideration. In January 2002, the FSA will submit legislation eliminating the requirement for physical certificates for Japanese government bonds (JGBs) and corporate debentures. This follows legislative action in 2001 to eliminate a similar requirement for commercial paper effective April 2002. The FSA has also announced its intention to allow exchange-traded funds (ETFs) based on foreign stock price indices.

The United States welcomes Japan's progress in increasing the efficiency and competitiveness of its financial markets. In its October 2001 submission, the United States put forward proposals to support further opening and development of the Japanese financial markets, which will allow Japan to take full advantage of international financial expertise and support future Japanese growth. These include: (1) permitting postal financial institutions to employ investment advisory companies through direct onshore trust arrangements without the requirement to convert asset positions into cash before changing asset managers on terms similar to those now in use for public pensions; (2) granting regulatory approval to prototype plans for defined contribution pensions; (3) eliminating the requirement for physical certificates for privately placed fixed income securities and investment trusts; (4) permitting multiple classes of shares for investment trusts; (5) requiring full mark-to-market accounting for all investment trusts; (6) revising the E-Notification Law to include lenders subject to the Moneylending Business Law; and (7) studying the feasibility of increasing electronic record-keeping and notification.

These issues were discussed in November 2001 in the inaugural meeting of the U.S.-Japan Financial Services Working Group. The Working Group is one component of the U.S.-Japan Economic Partnership for Growth.

For information on deregulation in the insurance sector, please see the Insurance entry under "Existing Bilateral Agreements."

Housing: Japan's $40 billion home building materials market is the second-largest in the world. Numerous restrictions on building size and design and the traditional emphasis on new housing versus maintenance and renovation have impeded market access for foreign building products and systems designs, limiting choice for consumers, and driving up housing costs.

In the Fourth Joint Status Report, Japan agreed to address these problems through several measures. Specifically, Japan will cooperate with the private sector to create a standard appraisal system for resale housing that accurately reflects the value of maintenance and renovation. Japan also will remove or significantly limit key financial disincentives associated with the purchase of used homes, such as permitting longer repayment periods for higher quality resale detached homes and extending the reduction from five percent to three-tenths percent for registration taxes on sales of existing homes. In addition, Japan pledged to cooperate and work with the U.S. Government to obtain recognition of the equivalency of the U.S. standards system for grading and certifying wood products, and to accept that Oriented Strand Board is functionally equivalent to plywood. Moreover, Japan will also continue to review with the United States its implementation of performance-based building codes through various bilateral fora. This particular on-going review will address serious U.S. concerns about Japan's use of performance criteria, transparency and testing methodologies, which impede the use in Japan of building materials and systems commonly used in the United States and elsewhere.

In June 2001 the United States and Japan also agreed in the Fourth Joint Status Report to continue future technical discussions on issues related to performance-based codes, implementation of test methodologies and procedures in evaluating fire resistance and other housing/wood product-related issues in the Wood Products Subcommittee, the Building Experts Committee, and Japanese Agricultural Standards (JAS) Technical Committee. The Building Experts Committee and the JAS Technical Committees met in Ottawa in September 2001 and discussed progress in implementing a number of measures announced in the Fourth Joint Status Report related to housing/wood products, including Japan's implementation of performance-based building codes. In October 2001, the U.S. Government held additional discussions with the relevant Japanese ministries on this issue and on the issue of equivalency for the U.S. standards system for grading and certifying wood products. Subsequently, the U.S. Government submitted to the Ministry of Agriculture, Forestry and Fisheries (MAFF) the remaining information necessary for MAFF to make a positive determination on the United States' request for equivalency.

The next Wood Products Subcommittee meeting will take place in early 2002, at which time the United States will review the progress made on performance-based building codes, equivalency, and other key issues.

ii. Structural Regulatory Reform

Competition Law and Policy: A key goal of our regulatory reform efforts is to ensure steps to deregulate Japan's economy are not undone by anticompetitive actions by private-sector players. An active and strong antitrust enforcement policy is needed to restrain anticompetitive behavior, including by incumbent firms, in once heavily regulated sectors.

In the Fourth Joint Status Report, Japan agreed to review the status of the JFTC within the central government to ensure its independence and neutrality. Japan also undertook to examine the introduction of new legislation to enable the JFTC to uncover violations of the AMA more effectively. For its part, the JFTC established the Information Technology and Public Utilities Task Force to investigate and take enforcement action against violations of the AMA in industries undergoing deregulation. The JFTC and the Ministry of Public Management, Home Affairs, Posts and Telecommunications (MPHPT) agreed to cooperate in promoting competition in the telecommunications sector and subsequently issued joint guidelines for business activities in that sector. With respect to measures to combat bid rigging, procuring agencies at the central and local government level were required by the Act for Promoting Proper Tendering and Contracting for Public Works, which came into effect on April 1, 2001, to report facts raising suspicions of bid rigging to the JFTC. Moreover, the Japanese Cabinet issued a Decision adopting the "Guiding Principle," which obligates central and local government procuring agencies to make efforts to seek recovery of overcharges from bid rigging participants and to suspend such participants from eligibility to bid on future government contracts. In addition, Japan agreed to examine the introduction of new legislation to address the problem of government procuring officials who assist bid rigging activities.

In its October 2001 Regulatory Reform submission, the United States recommended that Japan increase substantially the staff levels of the JFTC and make it an independent agency under the Cabinet Office. The United States urged that the JFTC's investigative tools be brought up to modern international standards by strengthening the deterrent effect of the administrative fine (surcharge) system, making changes to permit adoption of a cooperation leniency program, and providing greater criminal investigation powers. The United States also recommended that Japan take effective measures to address the epidemic of bid rigging, which should include new legislation to prevent so-called "bureaucrat-led bid rigging." The submission called on the JFTC to step up its promotion of competition in regulated sectors and to devote additional resources to monitoring recently deregulated sectors to ensure that government regulation is not replaced by anticompetitive administrative guidance or private-sector restraints. Competition policy issues were discussed further at the first meeting of the Cross-Sectoral Working Group in early November 2001.

Transparency and Other Government Practices: Despite improvements in recent years, Japan's regulatory system continues to lack the transparency and accountability necessary to ensure all players have the same access to government information and the policymaking process. New market entrants and competitors need adequate information on Japan's regulatory system in order to base their decisions on accurate assessments of potential costs, risks and market opportunities. This is especially true for foreign firms, which do not have the same access to the bureaucracy as domestic firms.

Japan took several steps in 2001 that will increase the transparency and accountability of its regulatory system. It has introduced a government-wide "No Action Letter" system that will enable businesses to submit inquiries to, and receive responses from, Japanese agencies on the interpretation of laws and ordinances and their application to specific factual situations. Japan also has implemented a government information disclosure law, similar to the U.S. Freedom of Information Act; introduced a government-wide policy evaluation system; and improved its Public Comment Procedures by making all of the public comments available for review by the public. In the Fourth Joint Status Report, Japan agreed that each ministry and agency will adopt detailed rules related to the implementation of the new "No Action Letter System" by the end of Japanese Fiscal Year 2001. Japan also agreed to make continuous efforts to enhance and strengthen the government-wide policy evaluation system.

Building on these measures, the United States recommended in its October 2001 submission that Japan undertake additional improvements in its regulatory system to support its reform efforts and ensure that all players have the same access to government information and the policymaking process. These recommendations include: (1) revising the Public Comment Procedures to make them an effective regulatory mechanism by establishing a central registry for all solicitations, requiring a minimum 30-day comment period, authorizing an independent review of use of the Procedures, and establishing a study group to examine the Procedures; (2) reducing the use of administrative guidance and requiring all administrative guidance to be issued in writing (except in special cases); (3) developing a mechanism that would enable all interested domestic and foreign parties to review and comment on draft legislation before governmental agencies make their submissions to the Diet; and (4) increasing the authority of the courts to review administrative actions of governmental agencies. Further discussions on transparency issues took place in early November 2001 during the inaugural meeting of the Cross-Sectoral Working Group.

Legal System and Infrastructure: Reform of the Japanese legal system is essential to establishing a legal environment that is conducive to international business and investment and supportive of deregulation and structural reform. In keeping with this objective and its Enhanced Initiative agreements, Japan took significant steps in 2001 toward modernizing and liberalizing its legal system. Most notable was the establishment of a Judicial Reform Council (JRC), which in June 2001 made important recommendations on needed legal reforms. These recommendations included: deregulating the requirements for specified joint enterprises (*tokutei kyodo jigyo*) to promote cooperation and collaboration between *bengoshi* and foreign lawyers; studying the restriction that prohibits foreign lawyers from hiring Japanese lawyers; increasing the number of legal professionals; increasing the speed and efficiency of civil litigation; facilitating litigants' collection of evidence at early stages of litigation; increasing the number of judges; making the specialized intellectual property rights departments at Tokyo and Osaka District Courts function as "patent courts;" reforming Japan's 100-year-old Arbitration Law; and undertaking a comprehensive study of judicial oversight of administrative agencies.

The United States has welcomed these steps and recommended in its October 2001 submission additional measures. These include: (1) expeditious and effective implementation of the JRC's recommendations; (2) elimination of all prohibitions against freedom of association between Japanese and foreign lawyers; (3) removal of restrictions on foreign lawyers; (4) improvements in the foreign lawyer regulatory system; and (5) modernization of the judicial system, including by improving pre-trial evidence gathering mechanisms, augmenting protection of trade secrets during court proceedings, and strengthening the powers of judges to fashion more effective injunctive orders. Further discussions on Japan's legal system and infrastructure took place under the Cross-Sectoral Working Group, which met in early November 2001.

Commercial Law: The United States recommends that Japan revise its Commercial Code to introduce greater flexibility to the organization, management, and capital structure of Japanese companies, and improve efficiency and accountability. Comprehensive revision of Japan's commercial laws should have a profound effect on both domestic and foreign firms. The liberalization of restrictions on equity securities, for example, would facilitate the acquisition of capital necessary for restructuring and new investment. Revision of the Commercial Code also would have significant implications for the ability of foreign firms to invest and operate effectively in the Japanese market, bringing crucial technologies, know-how and employment to Japan's economy.

In the Fourth Joint Status Report, Japan agreed to revise its commercial code in a manner that would create a more positive business environment for both domestic and foreign firms. Steps agreed to included eliminating restrictions on the use of stock options and establishing new corporate governance rules designed to encourage the use of outside directors on corporate boards. Japan took a positive step toward necessary reforms with the Legislative Council's issuance of its Interim Tentative Draft of the Outline of Commercial Code Revision in April 2001, proposing some major revisions to the commercial law system, including elimination of restrictions on recipients of stock options and on the issuance of new shares, and allowing companies the option of adopting a Western-style corporate governance system. Legislation to implement some of these recommendations was submitted to the Diet in the Fall of 2001, and the final recommendations are due for release in early 2002.

The United States continues to recommend significant revisions to Japan's commercial law. In its October 2001 Regulatory Reform submission, the United States urged Japan to: 1) permit and promote cross-border share exchanges and other legal mechanisms to facilitate foreign merger and acquisition activities; 2) introduce greater flexibility to the capital structure of Japanese corporations, including the elimination of restrictions on the quantity and recipients of new stock options; 3) strengthen corporate governance mechanisms, including allowing publicly trade companies the option of adopting an executive committee and outside director system; 4) oppose any proposal requiring foreign corporations to appoint statutory agents who would be jointly and severally liable for all liabilities of the corporation; and 5) allow greater input by the international business community into the formulation of proposed commercial law revisions. These and other issues related to the Commercial Code were raised in early November during the inaugural meeting of the Cross-Sectoral Working Group. Also during that meeting, members of the private sector gave a presentation on the importance of permitting cross-border share exchanges in Japan.

Distribution: Japan's rigid and inefficient distribution and customs systems restrict market access for imported products and work against the competitiveness of foreign-made products. On the customs front, the United States believes Japan needs to modernize clearance procedures to fully open its market to imported goods. Regarding distribution, Japan's new Large Store Location Law (SLL) enacted in June 2000 marked an important step forward in addressing some of the inefficiencies in the sector, but burdensome regulations continue to hamper the efficient movement of goods. Enforcement of the SLL also must be carefully monitored to ensure that it does not unfairly discriminate against large stores.

In the Fourth Joint Status Report, METI agreed to continue to take measures to facilitate the implementation of the SLL in a consistent, transparent, and predictable manner by: 1) monitoring local governments to ensure that they do not impede the purpose of the law; and 2) providing information regarding the application of the Law through meetings and technical training of local government officials. In response to requests by the United States, METI has established official contact points in Tokyo and around the country to field complaints by large store developments and to facilitate their resolution. On the issue of customs clearance procedures, the U.S. Government noted its appreciation for Japan's willingness to consider the concerns of express carriers and other companies faced with increased fees for the use of the Nippon Automated Cargo Clearance System (NACCS) for air-cargo. Discussions between users of the new system, which was introduced in October 2001, and the NAACS Operation Center took place throughout the year, starting with the initiation of a public comment procedure in March 2001.

Our reform recommendations to the Government of Japan in October 2001 recognized that Japan has implemented and plans to implement additional positive measures to simplify and automate customs processing. The submission recommended extending the new Simplified Declaration Procedures Act to express carriers and raising the de minimis level for customs duties from yen 10,000 to yen 30,000. At the same time the United States urged Japan to continue its dialogue with companies to ensure that a fee structure equitable to all NACCS air-cargo users is installed after the expiration of the current three-year arrangement. The U.S. Government continues to monitor progress on customs processing procedures and the fair and uniform implementation of the SLL. In early November 2001, the Cross-Sectoral Working Group met to discuss these and other issues.

b. Bilateral Consultations

i. Insurance

The 1994 and 1996 bilateral insurance agreements have made significant contributions to the deregulation of the Japanese insurance market. The agreements included sweeping measures that resulted in significant improvements in the product approval process, greater use of direct sales of insurance products, and the introduction of risk differentiated automobile insurance. As a result, foreign insurance companies have continued to visibly and substantially increase their presence in both the life and non-life insurance sectors in Japan.

Bilateral consultations under the two insurance agreements were held in Tokyo in July 2001. The 2001 review included an analysis of data provided by Japan, a discussion of changes in the FSA's policies/regulations, and an exchange on important and timely changes in Japan's insurance sector. As in past years, a representative from the National Association of Insurance Commissioners participated in the talks in order to promote U.S.-Japan regulator-to-regulator discussions of various aspects of the U.S. and Japanese insurance regulatory systems. More specifically, the United States and Japan discussed recommendations by an FSA study group to streamline Japan's product approval process and increase needed personnel and technical resources. In addition, the United States emphasized its concerns about the case agent system and life and non-life Policyholder Protection Corporations. The two countries also addressed a number of new issues that have arisen as Japan continues to restructure its financial system, such as the implementation and supervision of Japan's new pension system, the expansion of sales of insurance by banks, and the possible reduction of guaranteed interest rates by insurers.

The United States also raised concerns voiced by U.S. industry regarding future plans for the postal financial institutions – the postal insurance system (*Kampo*) and the postal savings system (*Yucho*) – which currently fall under the purview of MPHPT. There has been increasing concern over the effect these institutions have on the efficient operation of Japan's financial market. As such, the planned transfer of the three postal services (mail delivery, savings and insurance) from the Postal Services Agency to a public postal corporation in 2003 provides an important opportunity for the Government of Japan to take concrete steps to address key transparency and competition issues related to these services. The U.S. Government put forward concrete recommendations regarding the transfer in its October 2001 Regulatory Reform submission to Japan, as well as in response to draft MPHPT plans regarding *Kampo* and *Yucho* put out for public comment in November, 2001. These recommendations included ensuring transparency throughout the process, extending the same standards of regulation to the postal financial institutions as applied to the private sector, and prohibiting these institutions from underwriting any new insurance products or originating any new non-principal-guaranteed investment products.

Over the past year, the Government of Japan has taken a number of steps to increase transparency in its decision-making processes related to the insurance sector, including use of public comment procedures by the FSA and MPHPT as well as the inclusion of foreign representatives on various government advisory committees. The United States strongly encourages the FSA and MPHPT to continue their efforts in this regard. The next annual consultations are scheduled to be held mid-year in 2002, at which time the United States anticipates a full discussion on a wide range of issues.

ii. Autos and Auto Parts

Improving access to the Japanese auto and auto parts markets is an important objective of the Bush Administration. While there has been a trend toward closer integration as well as important technological advancements in the global automotive industry over the past several years, the effect of these changes on market access and competition in this sector remains unclear. Unfortunately, Japan's lingering economic slump, limited market access, and weak competitive environment have continued to disproportionately hurt foreign vehicle and auto parts manufacturers in Japan. The United States remains highly disappointed that, after rising steadily in 1995 and 1996, sales of North American-made vehicles have fallen for the past five years, with sales in 2001 expected to be substantially less than in 1994. In an effort to contend with these economic conditions and position themselves to better compete in the future, U.S. auto companies have continued to consolidate distribution networks and rethink corporate strategies. The auto parts sector also remains problematic: U .S. exports to Japan declined from a record level of $13 billion in 1995 to an estimated $11.3 billion in 2001.

In order to address barriers in and improve U.S. companies' access to the domestic Japanese automotive market and Japanese auto plants in the United States, the United States and Japan established a new Automotive Consultative Group (ACG) in October 2001. The ACG will serve as the focal point for addressing lingering as well as new, emerging issues in this key sector of both countries' economies. More specifically, the group will assess trends in the industry based on a series of trade and economic data on autos and automotive parts to be provided by both countries and work to identify areas in which specific action can be taken by Japan to address U.S. concerns. This would include further deregulation (particularly with respect to the automotive parts aftermarket), increased transparency in rules and regulations governing this sector, and more rigorous application of Japanese competition laws. The group will meet at least annually and will be co-chaired by the Department of Commerce and USTR on the U.S. side, and METI and the Ministry of Land, Infrastructure and Transport on the Japanese side. The first meeting is expected to take place in the first half of 2002.

In addition to meetings under the ACG, the United States is continuing to address cross-cutting issues impacting the automotive sector under the Partnership, announced by President Bush and Prime Minister Koizumi in June 2001. This includes expanding opportunities for foreign investment, increasing transparency, and promoting corporate restructuring in the Japanese economy.

iii. Government Procurement

NTT Procurement: The U.S. Government has urged Japan to increase its public sector purchases (including purchases by NTT companies, part of a group in which the Government of Japan held a majority of shares until early 2001) of U.S. telecommunications equipment through a series of bilateral agreements with Japan dating back to 1980. As a result of the NTT Agreements, U.S. suppliers have made some significant inroads as suppliers to NTT, the largest single procurer in the Japanese telecommunications equipment market. NTT accounts for approximately one third of the $36 billion market for terminal and network equipment. Before the first NTT Agreement was concluded in 1980, less than 1 percent of NTT purchases were from foreign firms. These successive Agreements have helped move NTT toward procurement decisions based on market-driven, competitive factors. As a result, purchases of foreign equipment have increased, to the benefit of U.S. telecommunications equipment suppliers and the NTT companies.

In June 2001 the United States and Japan conducted the final annual review under the most recent bilateral agreement – the 1999 U.S.-Japan NTT Procurement Agreement. At the review, the United States focused discussion on changes in procurement brought about by the NTT restructuring which took effect in 1999. These procedures include the process through which suppliers qualify to bid, the criteria used by NTT to select suppliers, the functioning of the Supplier Proposal Process, and the use of Japan-specific national versus internationally-adopted technical standards. The NTT companies provided data on foreign procurement during Japan Fiscal Year (JFY) 2000, which showed an increase in procurement from foreign telecommunications equipment suppliers.

The 1999 Agreement expired in July 2001. Due to the substantive progress made under the series of NTT Agreements, the United States, after consultations with U.S. industry, determined that the best way to pursue the goal of a fully open NTT market after July was to continue to monitor NTT purchases and procurement practices closely and in coordination with U.S. industry. The U.S. Government will examine information provided by U.S. industry, and will pursue with the Government of Japan problems or issues related to NTT procurement as they arise. In addition, the United States will look to NTT to narrow the gap between the noticeably lower foreign share of the NTT equipment market and that of the Japanese private sector telecommunications market, in order to provide new opportunities for globally competitive U.S. suppliers with their leading technology products.

Construction/Public Works: The U.S. share of Japan's $250 billion public works market has consistently remained well below one percent – a troubling fact given the competitiveness of American design/consulting and construction firms throughout the rest of the world. Discriminatory practices in Japan's public works sector continue, despite the existence of the 1994 U.S.-Japan Public Works Agreement, under which Japan is obligated to use open and competitive procedures for procurements valued at or above the thresholds established in the WTO Agreement on Government Procurement. These problematic practices include failure to address rampant bid-rigging, use of discriminatory qualification and evaluation criteria, unreasonable restrictions on the formation of joint ventures, and the structuring of individual procurements so they fall below thresholds established in international agreements. The United States is very concerned with these practices, which seriously impede American companies' ability to participate in Japan's public works sector. The 1994 Agreement remains in effect, but the consultative provision in the 1994 Agreement expired in March 2000. The United States will continue to engage Japan on specific matters of concern related to construction, using appropriate opportunities such as the 2002 inaugural meeting of the Trade Forum, established under the Partnership.

In September 2001, Japan hosted the third U.S.-Japan Construction Cooperation Forum (CCF), which is designed to facilitate the formation of joint ventures between U.S. and Japanese design/consulting and construction companies and to make it possible for U.S. firms to participate more fully in Japan's public works market. The United States looks forward to tangible results from the CCF. However, these private sector meetings are not a substitute for government-to-government consultations.

Medical Technology: The 1994 Medical Technology Procurement Agreement has been successful in providing improved market access and increased sales for foreign suppliers in Japan's government procurement sector. The last review of this agreement in March 2001 showed that overall foreign market share had increased to just under 47 percent. In key areas where U.S. manufacturers are major suppliers, foreign market share was even more substantial, for example cardiac pacemakers (98.5 percent), magnetic resonance (82.5 percent), and artificial joints and bones (77.4 percent). Although the annual consultation mechanism of this agreement expired at the end of March 2001, all of the procedural provisions remain in force. The U.S. Government will continue to engage the Government of Japan on specific matters of concern.

Other: In March 2001, the United States and Japan conducted reviews of the bilateral Computer and Telecommunications Procurement Agreements, concluded in 1992 and 1994, respectively. Both agreements aim to expand Japanese public sector procurement of foreign goods and services in these sectors. The March reviews included an analysis of data on recent government purchases provided by Japan and addressed issues of importance to the United States, such as transparency of the procurement system, continued high use of sole-source tendering, and the use of "overall greatest value" methodology in evaluating bids. In addition, the United States and Japan discussed the Japanese Information Technology Initiative and how procurement under the Initiative will be conducted. The United States remains concerned over the relatively low level of Japanese public procurement of highly competitive U.S. computer and telecommunications goods and services and will continue to address any issues that arise in all appropriate fora.

iv. Investment

Changing Japanese attitudes toward inward foreign direct investment (FDI), depressed asset values, and improvement in the regulatory environment enabled U.S. and other foreign firms to continue to gain significant new footholds in the Japanese economy, mostly through mergers and acquisitions. As a result, although FDI in Japan remains the lowest among OECD countries, investment in JFY 2000 (which ended in March 2001) hit $28 billion (Yen 3.1 trillion), more than 30 percent above the level of JFY 1999. Banking/insurance and telecommunications sectors showed particularly high growth. FDI in JFY 2000 in banking/insurance increased by more than 100 percent over JFY 1999 levels to approximately $9.2 billion and telecommunications showed healthy growth with FDI inflows of approximately $6.7 billion. U.S. direct investment into Japan mirrored these changes with increases in investment flows up to approximately $9.2 billion in JFY 2000, mostly due to transactions in the financial sector. More recently, however, FDI into Japan has slumped, likely as a result of continuing economic problems in Japan and a slowing global economy. From April through September 2001, total FDI was down almost 19 percent from a year earlier. U.S. investment plunged more than 33 percent.

Japanese and foreign businesses continue to be significantly affected by the implementation of several laws passed in 1999 which included suggestions raised by the United States during the dialogue carried out under the 1995 foreign direct investment agreement. The Securities Exchange Law, for example, now mandates consolidated and market-value accounting for listed firms and the new bankruptcy law (Civil Reconstruction Law) encourages business reorganization, including spin-offs, rather than forced liquidation of assets. In addition, the concept of corporate governance, such as the role of boards of directors, is changing in ways that bode well for increased investments, mergers and acquisitions.

Nevertheless, government and business observers from both countries recognize that much more remains to be done and the U.S. and Japanese Governments have agreed to continue to consult on investment issues. In October 2001 the inaugural meeting of the U.S.-Japan Investment Group set forth a framework for bilateral discussions on investment that will highlight and resolve possible impediments. The Group met again on December 13 and reviewed in detail the impediments to FDI inflows to Japan. In response to specific requests from the United States, Japan explained that it is working to strengthen accounting practices and increase the number of accounting and legal professionals. The U.S. private sector was also given an opportunity to directly present their investment concerns to the Government of Japan during the meeting. More talks will be held in early 2002, culminating in a joint report on investment.

c. Sectoral Issues

i. Agriculture

Although Japan is the United States' largest food and agriculture export market, Japan maintains many barriers to imports of U.S. food and agricultural products.

Rice: Japan's highly protected rice market has long been a target for liberalization efforts. In the Uruguay Round, Japan agreed to market access for rice in the form of an import quota. In 1999, Japan converted the quota to a tariff-rate quota, with a prohibitively high out-of-quota duty.

The United States has expressed ongoing concern over the market share of U.S. firms in Japan's overall rice imports in 2001 as compared to recent years. U.S. market share in Japan's Simultaneous-Buy-Sell (SBS) tenders was particularly low. (SBS tenders, which are conducted by the Japanese Food Agency, are designed to allow Japanese rice wholesalers and retailers to purchase high value, identity-preserved rice from foreign suppliers for retail sale, and as such are desired by the U.S. rice industry.) The United States will continue to monitor this situation closely.

Over the last year, the U.S. Government raised another problem related to Japanese imports of U.S. rice – the increasing percentage of low quality, broken rice in Japanese tenders of U.S. rice. The United States has pointed out that recent levels of broken rice imports from U.S. firms (17-18 percent) exceed what the industry would view as a normal broken percentage of around 11 percent. Japan has claimed that "brokens" in rice shipments normally exceed 11 percent, and points out that the high quality of Japanese rice harvests in recent years has pushed the domestic supply of brokens down, forcing those that normally use brokens (pastry, brewing and animal feed industries) to turn to the Japanese Food Agency for imports of this product. In Japan's November 2001 import tender, there was some decrease in the percentage of broken rice purchased from the United States. The United States has told Japan that it expects this trend to continue in future import tenders, particularly as the quality of Japanese rice harvests return to more normal levels.

Sanitary and Phytosanitary: Japan's use of sanitary and phytosanitary measures has created many barriers to U.S. food and agricultural goods. In April 2001, Japan instituted measures limiting the number of phytosanitary inspections of imported fruits and vegetables. With quick intervention by the Administration, the impact of that initiative was negligible on U.S. shipments. However, Japan continues to maintain overly restrictive quarantine measures on a number of U.S. products, such as apples, cherries and lettuce.

Organic Food: In May 2001, Japan accepted a U.S. proposal to permit certification of U.S. organic processed ingredients to Japanese organic standards by USDA accredited certifiers, allowing a continuance of approximately $50 million in U.S. organic food exports. Negotiations are underway with Japan to expand the certification to all U.S. organic food, valued at $100 million.

ii. Steel

Steel issues are detailed in Chapter V, "Other Multilateral Activities."

iii. Flat Glass

U.S. flat glass manufacturers continue to face high hurdles in their efforts to sell their products in Japan, despite gaining extensive market shares in other industrialized economies. Japan's three domestic producers constitute an oligopoly that exerts tight control over distribution channels by, for example, maintaining extensive equity and financial ties to distributors. In addition, Japanese flat glass manufacturers adjust prices, capacity, and product mix at virtually the same time, contributing to a lack of competition in the market.

To address these interrelated problems, the United States engaged Japan in discussions in 2001 under the Enhanced Initiative, the outcome of which was contained in the Fourth Joint Status Report. In that report, the Government of Japan recognized the economic benefits of competition in the distribution sector. It also confirmed that it would be detrimental to competition and a violation of Japan's Antimonopoly Act for distributors to reach agreements among themselves designed to exclude imported or other competitors' products from entering the market. In addition, the Government of Japan suggested that enterprises and foreign governments notify the JFTC of anticompetitive practices in the flat glass market and other highly oligopolistic markets. In the Fourth Joint Status Report, METI also agreed to continue to pursue economic reforms to ensure competition in the distribution sector.

The United States continues to raise glass market access issues with Japan and to work with U.S. industry on ways to improve market access and enhance competition in this sector.

d. Multilateral/WTO Disputes and Settlements

Varietal Testing of Fruits: In October 1997, the United States invoked dispute settlement procedures against Japan regarding its varietal testing requirements. Japan required repeated testing of established quarantine treatments each time a new variety of an already approved commodity was presented for export. This redundant requirement had no scientific basis and, because it imposed expensive and time-consuming testing on American producers, served as a significant barrier to market access. The United States challenged these requirements as inconsistent with Japan's obligations under the WTO Agreement on the Application of Sanitary and Phytosanitary Measures (the "SPS Agreement").

In March 1999, the WTO Dispute Settlement Body (DSB) adopted panel and Appellate Body findings that Japan's varietal testing requirement was: (1) maintained without sufficient scientific evidence, in violation of Article 2.2 of the SPS Agreement; (2) not based on a risk assessment, in violation of Article 5.1; and (3) inconsistent with Japan's transparency obligations under paragraph 1 of Annex B, since Japan did not publish its requirements.

In June 1999, Japan and the United States notified the DSB of their agreement that a reasonable deadline for Japan's implementation was December 31, 1999. Japan announced that it eliminated its varietal testing requirement on December 31, 1999, and continued consultations with the United States on fumigation requirements on the eight horticultural products at issue. In September 2001, Japan approved fumigation procedures for the final product, apples, and the United States and Japan notified the DSB that the case was finally resolved.

Fire Blight: Following the termination of technical discussions in October 2001, the Administration initiated dispute settlement procedures in the WTO against Japan's quarantine measures on U.S. apples due to fire blight in early 2002. Japan's Ministry of Agriculture, Forestry and Fisheries (MAFF) maintains highly restrictive requirements for western U.S. apples due to concerns about fire blight, without either a formal risk analysis or sufficient scientific evidence. In February 2001, USDA presented to MAFF the results of joint U.S.-Japan research which confirmed that mature symptomless apple fruits produced in the western United States are not a pathway for transmission of fire blight. This research supports earlier USDA research from 1989 and 1998 that was peer reviewed and published in scientific journals.

7. Taiwan

Trade Ministers at Doha, Qatar approved Taiwan's WTO membership in November 2001, recognizing Taiwan's important position in the global trading system. Taiwan became a member on January 1, 2002.

Taiwan's accession to the WTO will benefit most sectors of the U.S. economy. Taiwan's WTO commitments will increase access to a broad range of U.S. goods and services, including agricultural exports to Taiwan. Highlights of Taiwan's WTO commitments include:

- Tariffs on industrial goods reduced to less than 5 percent on average;
- Agricultural tariffs will fall to 12 percent on average, with most of these reductions taking place upon accession;
- Taiwan's state trading monopoly on tobacco and alcohol eliminated;
- Tariffs on construction and agriculture equipment, wood (except plywood), paper and paper products, furniture, distilled spirits, beer, certain steel products, civil aircraft, dolls, toys and games will all be reduced to zero (some by accession, most by 2004);

- Taiwan has agreed that on accession it will increase foreign access to a number of service sectors, including professional services (architects, accountants, engineers, lawyers), audiovisual services, express delivery services, advertising, computer services, construction, wholesale and retail distribution, franchising, and environmental services; and
- Taiwan will have the obligation to adhere to the WTO TRIPS Agreement to protect intellectual property rights.

a. Agriculture and Industrial Quotas

During 2001, the United States continued discussions with Taiwan regarding its commitments to import pork and chicken products at levels agreed to in February 1998 and in multilateral access arrangements that opened these "U.S. only" quotas to all WTO members in 2000. U.S. exporters experienced logistical difficulties as the result of Taiwan's implementation of a quarterly allocation system for these products in 2001. Taiwan's WTO commitments on tariff-rate quotas for chicken, pork, fish, autos and other products and a minimum market access commitment for rice were to replace the previous system on January 1, 2002. As 2001 came to a close, the United States was working closely with Taiwan to ensure timely implementation of these commitments.

b. Intellectual Property Rights

Taiwan moved toward strengthening its intellectual property rights protection regime during the past year with passage of several key legislative bills. However, the level of piracy in Taiwan remains at a very high level; serious enough to warrant placing Taiwan on the 2001 Priority Watch List. Taiwan has implemented a new chip marking system which allows identification of the manufacturer and designer of computer chips suspected of containing counterfeit software. During the Fall legislative session, Taiwan passed several amendments to existing laws and one new bill to address optical media piracy. Taiwan amended its patent law to extend the term of protection for certain existing patents from 15 to 20 years, consistent with WTO requirements. In the area of copyright protection, Taiwan amended its law to extend the term of protection for computer programs to the life of the writer plus 50 years. Taiwan also passed legislation requiring licensing of optical media (such as CDs, video CDs, and DVDs) manufacturing facilities in an attempt to reduce its high level of copyright piracy. However, the optical media law, as passed, appears to fall short in a number of areas. We will work closely with Taiwan on implementation of this bill to assure Taiwan aggressively enforces its provisions. Only with aggressive enforcement will Taiwan begin to address its seriously high rates of piracy and exports of pirated product.

We will continue to monitor Taiwan's progress in combating its high IP piracy rates, in particular, whether Taiwan aggressively enforces its existing laws, takes active measures to crack-down on pirate activities, and makes other efforts to reduce all types of IPR violations. We also look forward to working with Taiwan on further amendments to its copyright law to conform with existing international IPR norms.

c. Telecommunications

Several international telecommunications companies are interested in providing fiber-optic broadband submarine cable service to Taiwan customers. The United States has been actively involved in discussions with the Taiwan authorities during the past few years to assure that these companies can effectively compete in the Taiwan market in a manner consistent with Taiwan's WTO commitments. In the Fall of 2001, Taiwan agreed to allow these firms to construct their own back-haul facilities without first negotiating such construction with the incumbent telecommunications providers. In addition, Taiwan agreed to allow submarine cable firms to directly sell their services to Internet Service

Providers, as well as to existing fixed-line providers. We will continue to monitor Taiwan's progress toward full market opening of its telecommunications sector in a WTO-consistent manner.

d. Government Procurement

In August 2001, the United States and Taiwan reached an understanding clarifying Taiwan's commitments for its accession to the WTO's Government Procurement Agreement (GPA). The understanding affirms Taiwan's commitment to full and effective participation in the international rules-based trading system, brings Taiwan further into conformity with WTO GPA requirements, and ensures that barriers against U.S. companies in Taiwan's government procurement market will be lifted. Taiwan's commitments cover both infrastructure projects and procurement of a wide range of other goods and services.

8. Hong Kong (Special Administrative Region)

a. Intellectual Property Rights

Hong Kong continued enforcement actions during the past year to address piracy of copyrighted works. The Hong Kong public continues to become much more aware of the damage being sustained by its own industries, notably movies, music, and toys, from copyright and trademark infringement. Legislation that criminalized the corporate use of unlicensed software and subjects corporate pirates to the same penalties, including fines and jail sentences, as other pirates became effective in April 2001. However, soon after implementation, opposition was raised to certain provisions of the bill as applied to the photocopying of newspapers and magazines, and by supporters of small businesses that would like to decriminalize parallel imports of software for end-users. Certain provisions of this bill were suspended and a review is currently underway. We will continue to monitor this situation and other anti-piracy efforts closely.

b. Telecommunications

Hong Kong continued to make progress in opening its telecommunications market during the past year. We will continue to monitor progress in this sector closely as Hong Kong prepares for full market liberalization on January 1, 2003.

E. Mediterranean/Middle East

Overview

U.S. trade relations with the countries of Northern Africa and the Middle East, while to date relatively modest, have considerable potential value in terms of both U.S. commercial and foreign policy interests. The events of September 11 highlighted the importance of supporting peace and stability in the region by fostering economic development. The U.S.-Jordan Free Trade Agreement (FTA) and the U.S.-Israel Free Trade Agreement, together with the Trade and Investment Framework Agreements (TIFAs) established with several countries in the region, provide the context for our bilateral trade policy discussions with these countries, which are aimed at increasing U.S. exports to the region and assisting in the development of intra-regional trade.

2001 Activities

1. U.S.-Jordan Free Trade Agreement

The U.S.-Jordan Free Trade Agreement (FTA) took effect on December 17, 2001. The FTA will eliminate nearly all tariffs on industrial goods and farm products within 10 years, as well as commercial barriers to bilateral trade in goods and services originating in the United States and Jordan. The FTA includes, for the first time ever in the text of a trade agreement, substantive provisions on electronic commerce. Other provisions address intellectual property rights protection, balance of payments, rules of origin, safeguards, labor, environment, and procedural matters such as consultations and dispute settlement. Because the United States already has a Bilateral Investment Treaty with Jordan, the FTA does not include an investment chapter (the treaty has not yet entered into effect pending exchange of the instruments of ratification).

The agreement builds on other U.S. initiatives in the region designed to encourage economic development and regional integration. These include the 1985 U.S.-Israel Free Trade Agreement and its extension to areas administered by the Palestinian Authority in 1996, and the 1996 Qualifying Industrial Zone (QIZ) program.

2. Qualifying Industrial Zones

In 2001, USTR designated the eleventh Qualifying Industrial Zone (QIZ) in Jordan, the Zarqa Industrial Zone, in order to attract investment and strengthen economic integration in the region. Since the establishment of the first in 1998, QIZs have been a bright spot in Jordanian economic performance. They played an important role in helping to boost Jordan's exports to the U.S. from $16 million in 1998 to a projected $200 million in 2001. Jordan estimates that QIZs have created up to 15,000 jobs. Peak QIZ employment is forecast at 40,000 to 45,000. Investment in the establishment of QIZs is approximately $85-100 million, which is expected to grow to $180 to $200 million when all projects are completed.

To date all QIZs have been established in Jordan. Five QIZs were designated in 2000: The Investors and Eastern Arab for Industrial and Real Estate Investments Company Ltd. (Mushatta International Complex), El Zay Ready Wear Manufacturing Company Duty-Free Area, Al Qastal Industrial Zone, Aqaba Industrial Estate, and Industry and Information Technology Park Company (Jordan CyberCity Company). Four QIZs were designated in 1999, Al-Tajamouat Industrial City, Ad-Dulayl Industrial Park, Al-Kerak Industrial Estate, and Gateway Projects Industrial Zone. The first QIZ in Jordan, Irbid, opened in 1998.

QIZs are established pursuant to legislation passed by the Congress in October 1996, authorizing the President to proclaim elimination of duties on articles produced in the West Bank, Gaza Strip, and qualifying industrial zones in Israel and Jordan and Israel and Egypt. The President issued a November 1996 proclamation delegating the authority to designate qualifying industrial zones to the U.S. Trade Representative and providing duty-free treatment to products of the West Bank and Gaza.

The steady growth of QIZs testifies to the economic potential of regional economic integration. In addition to the competitive benefit of duty-free status for QIZ exports to the United States, QIZs increasingly offer participating companies the advantages of modern infrastructure and strong export expertise and linkages. This evolution should serve to increase the economic benefits of QIZs.

3. Trade and Investment Framework Agreements

In 2001, the United States concluded a Trade and Investment Framework Agreement (TIFA) with Algeria. TIFA agreements were previously negotiated with key regional partners, Egypt, Jordan, Turkey, and Morocco. Each TIFA establishes a bilateral Trade and Investment Council that enables USTR-chaired representatives to meet directly with their counterparts regularly to discuss specific trade and investment matters and to negotiate the removal of impediments and barriers to trade and investment. In 2001, Trade and Investment Council talks with the Government of Turkey were inaugurated. In October 2001, follow up talks on agriculture import issues were held.

4. WTO Accession

Negotiations on accession to the WTO of Saudi Arabia and Algeria continue, in which the United States is seeking entry based on implementation of WTO provisions upon accession and commercially meaningful market access commitments for U.S. goods, services, and agricultural products.

5. Intellectual Property Rights

Protection of intellectual property rights remains a leading priority in the Middle East region. Because of continuing concerns with Israeli efforts to reduce and eliminate piracy of intellectual property, Israel remained on the "Special 301 Priority Watch List" in 2001. Egypt and Turkey are also on the Priority Watch List, while Lebanon, Kuwait, Saudi Arabia, and the United Arab Emirates (UAE) are on the Watch List.

F. Africa

Overview

The United States enjoys a vibrant and growing trade and investment relationship with the countries of sub-Saharan Africa, and the region remains a key strategic partner. Total two-way trade between the United States and sub-Saharan Africa topped $22 billion in the first nine months of 2001 – an increase of 8 percent compared to the same period in 2000. Sub-Saharan Africa is home to more than one-tenth of the world's population, supplies 18 percent of U.S. oil needs, and represents the largest bloc of WTO members (38 countries).

The African Growth and Opportunity Act (AGOA) is the centerpiece of U.S. trade policy towards this important region and is helping to achieve key Administration objectives in sub-Saharan Africa – including promoting economic reform, growth and development; expanding bilateral and regional trade and investment relationships; and facilitating the region's full integration into the multilateral trading system. Meeting these objectives will open new markets for U.S. exports and create healthier economies and more democratic governments in sub-Saharan Africa. The United States made significant progress in each of these areas in 2001 and plans to continue its efforts in 2002.

1. Implementing the African Growth and Opportunity Act

The AGOA provides powerful incentives for economic growth in one of the poorest regions of the world by granting duty-free and quota-free access to the $10 trillion U.S. market for nearly 6,500 products. The Act also institutionalizes a process for strengthening U.S. relations with sub-Saharan African countries by establishing a U.S.-Sub-Saharan Africa Trade and Economic Cooperation Forum co-hosted by the USTR and the Secretaries of State, Treasury and Commerce. The AGOA is authorized through September 30, 2008.

The United States held the first Trade and Economic Cooperation Forum in Washington, DC on October 29-30, 2001. President Bush officially opened the Forum, which included participation by Ministerial delegations from every AGOA-eligible country. During the event, the USTR co-hosted a successful plenary session on AGOA implementation with the Minister of Industry, Trade and Marketing of Lesotho, where Trade Ministers from across the region discussed strategies for promoting regional economic reforms and strengthening U.S.-Sub-Saharan African trade and investment ties. USTR was joined at the Forum by four Cabinet Secretaries, the National Security Advisor, and the AID Administrator, reflecting AGOA's importance to the Bush Administration.

In 2001, the Administration worked to designate countries as eligible for AGOA and to ensure that the benefits of the Act are broadly shared. The AGOA requires the President to determine annually whether sub-Saharan African countries are, or remain, eligible for benefits based on criteria set out in the Act. USTR chairs the interagency AGOA Implementation Subcommittee responsible for advising the USTR on country eligibility. Based on the USTR's recommendation, the President determined in December 2001 that all 35 countries that were designated as eligible for AGOA benefits in 2001 will remain eligible in 2002. The 35 countries are

Benin, Botswana, Cameroon, Cape Verde, Central African Republic, Chad, Republic of Congo, Djibouti, Eritrea, Ethiopia, Gabon, Ghana, Guinea, Guinea-Bissau, Kenya, Lesotho, Madagascar, Malawi, Mali, Mauritania, Mauritius, Mozambique, Namibia, Niger, Nigeria, Rwanda, São Tomé and Principe, Senegal, Seychelles, Sierra Leone, South Africa, Swaziland, Tanzania, Uganda and Zambia.

Under AGOA, eligible countries that meet certain requirements to prevent illegal transshipment may also receive preferential duty-free and quota-free treatment for certain textile and apparel articles. In 2001, USTR approved submissions for AGOA textile and apparel benefits from 12 countries (Botswana, Ethiopia, Kenya, Lesotho, Madagascar, Malawi, Mauritius, Namibia, South Africa, Swaziland, Uganda and Zambia), including nearly all of the region's leading apparel producers. The AGOA Implementation Subcommittee expects to recommend approval of pending submissions of another nine countries in 2002.

As part of its ongoing AGOA implementation efforts, USTR has coordinated more than 20 regional technical assistance seminars on AGOA across sub-Saharan Africa. These seminars, designed to ensure that the sub-Saharan African public and private sectors are equipped to fully utilize AGOA benefits, were organized in conjunction with U.S. Customs, USAID and the Departments of State and Commerce. Throughout 2001, USTR also worked closely with the Overseas Private Investment Corporation (OPIC), the U.S. Export-Import Bank and the U.S. Trade and Development Agency (TDA) to address regional infrastructure and supply-side constraints. USTR and other federal agencies plan to host additional national and regional AGOA seminars in sub-Saharan Africa this year.

The United States continues to actively promote public and private sector understanding of AGOA and U.S. trade policy towards Africa, and these efforts are raising awareness of the many opportunities available through expanded trade with the region. In addition to numerous AGOA technical assistance and training seminars, USTR officials have organized briefings for Congress and private sector business groups and met frequently with the African diplomatic corps, Industry Sector Advisory Committees (ISACs) and companies interested in AGOA. USTR and other members of the interagency AGOA Implementation Subcommittee have also produced a matrix of steps involved in AGOA implementation and a comprehensive *AGOA Implementation Guide*, and they continue to maintain a website dedicated to AGOA information (www.agoa.gov). In 2002, the USTR will institute a Trade Advisory Committee on Africa (TACA) to provide a formal vehicle for regular private sector and NGO input into AGOA implementation and broader U.S. trade and investment policy towards sub-Saharan Africa.

2. Promoting Economic Reform, Growth and Development

In its first 18 months, the AGOA has prompted important economic and social reforms across sub-Saharan Africa and delivered new jobs and new opportunities for economic growth and development to the region. The AGOA's eligibility requirements create incentives for countries to reform their economies and create an environment conducive to increased trade and investment. To receive benefits, countries must demonstrate the existence of, or progress toward establishing, a market-based economy, the rule of law, reduction or elimination of barriers to trade and investment, policies to reduce poverty, and systems to combat corruption and protection of worker rights. These criteria represent global best practices to attract and maintain trade and investment, and are essential for the transfer of technology, increasing labor force skill, promoting competition and increasing exports.

The United States consulted extensively with sub-Saharan African countries on AGOA eligibility requirements in 2001, and many eligible countries are implementing needed reforms as a result. These reforms include measures to combat corruption, accelerate privatization, deregulate key industries, promote more open trade, and strengthen intellectual property and labor law protections. Countries have ratified ILO Convention 182 on the elimination of the worst forms of child labor and are working to change, or have changed, laws on child trafficking or on worker rights.

By bringing increased investment to and creating new jobs in sub-Saharan African countries, the AGOA is also demonstrating how trade can benefit developing countries. In 2001, Lesotho attracted an estimated $120 million in new investment as a result of AGOA, four times the amount it receives annually in overseas aid. Kenya attracted nine new investors and the country predicts that AGOA will create over 150,000 jobs. Namibia won $100 million in new investment, and U.S. apparel industry leaders active in Madagascar attribute about 30,000 new jobs in that country to AGOA. South Africa has also achieved significant results, exporting to the United States in over 18 different sectors. Overall, anecdotal evidence suggests that AGOA's incentives have brought the entire region nearly $1 billion in new investment.

In addition, U.S. firms say they have increased their sourcing from sub-Saharan Africa by roughly 75 percent as a result of AGOA. In the first half of 2001, almost 85 percent of U.S. trade with the region was with the 35 AGOA eligible countries, and U.S. imports under the Act accounted for 58 percent of total U.S. imports ($11.6 billion) from sub-Saharan Africa over the same period. While most of U.S. imports were in the energy sector, AGOA is beginning to diversify our trading relationship. For example, textile and apparel imports from the region rose nearly 30 percent ($343 million to $438 million) in the first half of last year, compared to the same period in 2000. Imports of minerals and metals were up 14 percent ($1.5 to $1.7 billion) and machinery imports grew 78 percent ($80 million to $142 million).

3. Expanding Bilateral and Regional Trade and Investment Relationships

AGOA successes are helping to strengthen and expand U.S. bilateral and regional trade and investment ties with sub-Saharan Africa. Growing interest in trade with the United States led to negotiation of a new Trade and Investment Framework Agreement (TIFA) with the twenty-country Common Market for Eastern and Southern Africa (COMESA) and a Joint Declaration on E-Commerce with Nigeria in 2001. The COMESA TIFA is the first U.S. regional TIFA in sub-Saharan Africa and adds to an existing network of Trade and Investment Framework Agreements with individual countries (South Africa, Nigeria and Ghana). The Administration has used these agreements to successfully further bilateral trade promotion initiatives and resolve commercial disputes.

AGOA successes are also creating new commercial opportunities for U.S. exporters. Even as trade preferences granted under the Act have increased U.S. demand for African goods, U.S. exports to the region have grown significantly. Indeed, U.S. sales to sub-Saharan Africa were up nearly 30 percent (to $5.2 billion) in the first nine months of last year, compared to the same period in 2000. For those nine months, South Africa was the largest regional consumer of U.S. exports, followed by Nigeria, Kenya, Namibia, Angola, Cameroon, Ghana and the Seychelles. In order to sustain and build upon this success we need to ensure growth of new trade opportunities and increasing AGOA exporters' familiarity with the U.S. market. Africans, too, will have to continue their pursuit of new trade opportunities and work to develop efficient shipping links and other infrastructure.

a. South Africa

The United States and South Africa enjoy a broad and mutually beneficial trade and investment relationship. Total two-way trade grew 9 percent to $5.7 billion in the first half of 2001, compared to the same period the previous year. Leading

U.S. exports to South Africa include transportation equipment, chemicals, electronic products, machinery and agricultural goods. Imports include minerals and metals, transportation equipment, chemicals, machinery and textiles and apparel. South Africa is a valued partner in the WTO and is the largest U.S. supplier of AGOA eligible products in sub-Saharan Africa, with sales worth more than $290 million in the first nine months of 2001.

As with many diverse and growing bilateral trading relationships, certain disputes have arisen between the United States and South Africa. These include concerns related to South Africa's December 2000 antidumping order against imports of certain U.S. poultry products, and ongoing problems related to South Africa's basic telecommunications monopoly, Telkom, and its failure to provide facilities necessary for U.S. value-added network services (VANS) providers to operate and expand. The USTR held a videoconference with the South African Minister of Trade and Industry to discuss poultry in September 2001, and the Administration hopes to resolve this matter early in 2002. The United States worked with U.S. VANS providers in 2001 to address concerns related to the South African Telecommunications Amendment Bill signed into law in November, and will continue these efforts in 2002.

b. Nigeria

Nigeria is the largest overall U.S. trading partner in sub-Saharan Africa. Total two-way trade topped $7.9 billion in the first nine months of 2001, a four percent increase over the same period in 2000. Nigeria is a major global consumer of U.S. agricultural products and was the largest foreign purchaser of U.S. red winter wheat in 2001. Nigeria is also the fifth largest U.S. petroleum supplier, and energy products account for the vast bulk of the country's sales to the United States. Under AGOA, however, the country is diversifying its export base to encompass other products, including footwear and manufactured goods.

The United States is working closely with the Government of Nigeria, both through the U.S.-Nigeria TIFA and other initiative, to promote expanded trade and investment and a more diversified economy. Earlier this year, U.S. and Nigerian governments officially launched a multi-million dollar gum arabic production project in the northern Nigerian state of Jigawa. U.S. gum arabic processors have agreed to purchase all Nigerian production that meets quality standards.

c. Other Countries and Regions

The Administration plans to continue ongoing efforts to strengthen bilateral trade and investment ties throughout sub-Saharan Africa and promote regional economic integration through work with the Organization for African Unity (OAU), the Economic Community of West African States (ECOWAS), the West African Economic and Monetary Union (WAEMU), the Economic and Monetary Community of Central Africa (CEMAC), COMESA and the Southern African Development Community (SADC). This year, the United States will co-chair the inaugural U.S.-COMESA TIFA Council meeting and host the U.S.-SADC Forum in Washington, DC.

4. Facilitating Sub-Saharan Africa's Integration Into the Multilateral Trading System

The AGOA has also helped to promote sub-Saharan Africa's integration into the multilateral trading system and encourage support for new global trade negotiations in a region that accounts for more than a quarter of WTO membership.

The United States worked closely with sub-Saharan African governments throughout 2001 to prepare for the successful Fourth WTO Ministerial Conference at Doha. Between June and November, the USTR consulted directly with Trade Ministers and/or Heads of State or Government from Gabon, Ghana, Kenya, Lesotho, Mauritius, Nigeria, Senegal, South Africa and Tanzania to discuss WTO and other matters. He also co-hosted a WTO Roundtable for Trade

Ministers at the October U.S.-Sub-Saharan Africa Trade and Economic Cooperation Forum and led a similar discussion in Doha. Responding to invitations from COMESA and the OAU, USTR officials participated in meetings in Cairo, Egypt in July and Abuja, Nigeria in September where African leaders were coordinating regional positions on WTO issues and preparing for the Doha Ministerial.

This year, the United States is working with sub-Saharan African countries to achieve common objectives in Geneva and ensure that regional governments have the capacity to participate effectively in new WTO negotiations and implement the results. The Administration has developed a comprehensive strategy for delivering WTO technical assistance to the region based on needs identified by African governments, and will be cooperating with other bilateral and multilateral donors on implementation.

These efforts build on a solid track record of delivering trade capacity assistance to developing countries in sub-Saharan Africa and beyond. Between 1999 and 2001, the United States devoted more than $110 million to technical assistance on WTO agreements, awareness and accession worldwide, and U.S. spending on these programs increased by more than 650 percent over the same period. In 2001, the United States pledged $1 million to the WTO's Global Trust Fund for Technical Assistance to help developing country members meet their Uruguay Round commitments and participate more fully in the international trading system. USTR will continue to coordinate regional seminars and workshops on key WTO issues (agriculture and services) and fund scholarships for 30 sub-Saharan African trade officials to participate in comprehensive WTO courses in Geneva in 2002.