Report on UNITED STATES TRADE BARRIERS AND UNFAIR PRACTICES 1991

PROBLEMS OF DOING BUSINESS WITH THE US

Services of the
Commission of the European Communities

EC REPORT ON US TRADE BARRIERS AND UNFAIR PRACTICES

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INTRODUCTION

In a world of rapid technological progress and growing economic interdependence, the expansion of international trade in goods and services remains an indispensable condition for sustained economic growth. The recognition of this fact has been the prime motivation behind the effort to reinforce and extend the world trading system through the Uruguay Round of multilateral trade negotiations. The outcome of these negotiations is still uncertain, although it is clear from the work which has already taken place in the fifteen negotiating groups that substantial improvements to the multilateral trading regime are not only desirable, but also feasible.

This report seeks, in the interest of transparency, to identify obstacles to trade and investment and other unfair practices which exist in the US, as a first step towards their elimination either through existing multilateral procedures, in the course of the Uruguay Round of GATT negotiations or through a bilateral dialogue between the Community and the United States. It is hoped that the new impetus to the process of bilateral consultation and cooperation provided by the recently adopted Transatlantic Declaration will facilitate the removal of such barriers on both sides of the Atlantic.

Like the European Community, the United States has repeatedly expressed its commitment to the free flow of trade and investment . This shared belief in the value of free economic exchange is largely reflected in practice. The EC and the US are each other's largest single trading partner, to their mutual benefit. Two-way trade in 1990 amounted to more than $174 bn. While two-way direct investment in each other's economy (in 1989) added up to $385 bn.

However, as this report illustrates, the United States, while in general terms a comparatively open economy, nevertheless maintains numerous unfair or discriminatory practices and legislative provisions which impede and distort trade in goods and services, as well as international investment flows. The report also demonstrates that the United States is itself not free of the type of trade and investment barriers it condemns in others. Measures identified in the US National Trade Estimate Report on Foreign Trade Barriers, for example, are also to be found in its own legislation and practice.

The list of measures set out in this report is, as in earlier years, intended to be illustrative, not exhaustive. The sections on services and investment have been expanded in comparison to the entries in last year's report to reflect more accurately their economic significance, however, other problems, such as the extraterritorial reach of US legislation or obstacles to the flow of technology, could be treated in greater detail.

A further issue of concern related to technology, is the significance of US Department of Defence spending in support of Research and Development. Much of the ensuing technology has applications in the purely commercial sphere, as well as that of defence. Such support represents an effective indirect subsidisation of commercial production. Yet another type of measure not covered in detail, is the expanding body of legislation, at Federal and State level, for the protection of the environment. The, often unintended, impact on trade of such measures is growing. Finally, it should also be remembered that the US maintains a number of protectionist measures such as quantitative restrictions on imports as well as voluntary restraint agreements.

Despite its non-comprehensive character, the report gives a representative cross-section of the types of problem which can be encountered by those doing business with or in the US and of the pressures and uncertainty to which they are subjected as a result of the often arbitrary and unilateral nature of much of US Trade legislation. It should be emphasised that not all of the problems are the deliberate result of protectionist-inspired policies or legislation. Some are certainly the unintended outcome of measures adopted for valid domestic reasons. Yet others arise from the differences which exist between the regulatory systems in the EC and the US. It is in the interests of both sides, given our economic interdependence, to make a conscious and sustained effort to bring about a greater degree of convergence between regulatory systems on a multilateral basis. Bilateral dialogue can also make an important contribution to this.

However, many of the barriers and practices listed in the report do seem in large measure the product of a certain current of protectionism and isolationism, triggered by the economic and trade deficit problems of the United States in recent years. This is particularly the case with those elements of US trade legislation which are incompatible with multilateral obligations of the United States (e.g. unilateral action under Section 301). Other practices which cast doubt on the multilateral commitment of the United States include the inordinate time taken to bring US legislation into conformity with GATT Panel rulings (the Customs User Fee is a good case in point), as well as the lukewarm attitude to international standard setting, its non-adherence to the relevant annexes of the Kyoto Convention on origin rules and its refusal to guarantee the compliance of its States with international obligations undertaken by the Federal government.

The order of the chapters is not intended to denote any order of economic importance. Instead the report deals in turn with general legislative provisions, measures affecting trade in goods and services, and measures affecting investment.

To some extent the listed measures are grouped together according to the common characteristic or principle involved. This can be helpful in understanding the fundamental issues at stake. This approach has been used in chapter II, for example, to highlight unilateralism as a characteristic element of many US legislative provisions. This generally takes the form of unilateral sanctions or retaliatory measures against offending countries or natural or legal persons. Such measures are to be found in legislation ranging from Section 301 of the Trade

Act, as well as its special provisions for intellectual property, telecommunications and public procurement (see chapter I), to environmental and conservation legislation (see chapter II B and C). Clearly such an approach is not compatible with the GATT and, moreover, it does nothing to foster the kind of multilateral collaboration necessary to maintain a viable and expanding international trade regime.

The extraterritorial reach of much of US legislation represents another category of problem. US legislation often attempts to extend the application of its provisions to persons, natural or legal, who are outside American jurisdiction. Examples of this are to be found, inter alia, in the various export control measures such as the Export Administration Act (see chapter II), which lapsed last autumn but which has been reintroduced in Congress this year. This provides for sanctions against foreign companies, e.g. in the form of a ban on the importation of their products into the US, which are deemed to have violated US export controls or, even the national export controls of their own country. Similarly, extraterritorial elements are to be found in legislation as diverse as anti-drug measures (see chapters II A and IX B 2) and taxation and investment measures (see chapter XI B). The efforts of US legislators to apply US laws outside the jurisdiction of the United States ignore a fundamental principle of international law. While the EC recognises the need for tight export controls on drug precursors, arms etc., the best means of achieving the desired objective is through multilateral cooperation in order to establish agreed rules and to ensure that they are respected.

These tendencies to unilateralism and to extraterritoriality stand in regrettable contradiction to the United States' declared commitment to multilateral action to solve problems in an increasingly interdependent world, to which the Community fully subscribes.

Another type of difficulty for those doing business with the US arises from the denial of national treatment or discrimination against foreign individuals or companies or against foreign products which is to be found in a wide array of legislative provisions. Examples include the Buy American restrictions (see chapter VII A) and other restrictions on procurement of foreign products or services (see chapters VII C and D, IX), as well as discriminatory taxation of foreign products, services or companies (see chapters III D, V, XI B) and restrictions on foreign investors (see chapters IX B and D, XI).

The US attempts to justify a number of the above measures on the grounds of national security, the latter concept being stretched to lengths which are clearly unwarranted. Barriers introduced on national security grounds are numerous and are found in many areas , including public procurement (see chapter VII), services (see chapter IX) and investment (see chapter XI). Misapplication of national security provisions to areas which are essentially in the commercial domain introduces a substantial, additional element of uncertainty to business decision-making.

Not least among the difficulties faced by those doing business with or in the United States is the growing problem of fragmentation of the US market and regulatory system and a seemingly growing number of barriers are being encountered at the State rather than the Federal level. In the field of public procurement, for example, a large number of buy national or buy local provisions are to be found at state level. Given the growing proportion of public spending by the States as opposed to the Federal authorities, this is an issue of ever-increasing concern in the EC (see chapter VII C 1). Similarly, regulatory activity by the States in areas such as standards and environmental protection or taxation, is causing difficulties to those seeking to export goods to the US or to provide services or carry out direct investment projects (see chapters VI, VIII, XI). Restrictions on financial services also remain a problem. This is an issue of great concern to the European Community. This concern has been heightened by the US refusal, in both the Uruguay Round of Gatt negotiations and in the ongoing talks in the OECD on the reinforcement of the National Treatment Instrument, to give a clear undertaking that its States will be bound by any agreement; up till now, the US has only been prepared to offer a commitment on the basis of best endeavours.

To conclude, the Commission firmly believes that it is in the interest of all concerned to make a determined effort to address the various types of problems illustrated in this report through dialogue rather than unilateral action. The opportunities to resolve many of these issues offered by the Uruguay Round negotiations and by existing multilateral rules and procedures should be exploited in full.

The Commission expects the reinforcement of EC-US relations and the improved understanding resulting from the deepening and extension of the bilateral dialogue to promote multilateral efforts for the liberalisation of economic exchanges, to facilitate the resolution of bilateral problems with the minimum of disruption to economic operators and, over time, to reduce the extent of regulatory divergence.

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This report was finalised on 15 March 1991

I US TRADE LEGISLATION

I.A Section 301 of the Trade Act

Description

Section 301 is the statute under US law dealing with "unfair" foreign trade practices and measures to be taken to combat them. Major changes were made to Section 301 of chapter 1 of title III of the Trade Act of 1974 by the Omnibus Trade and Competitiveness Act of 1988. By substantially reducing the discretion available to the US authorities in administering the Act, the changes make it much more likely that GATT-illegal unilateral action will be taken to redress allegedly unfair trade practices. In fact, mandatory action, subject only to a few narrowly drawn waivers, is required in certain cases. In others some discretion, albeit reduced, remains. Furthermore, the scope of the statute has been enlarged to include new categories of practices.

The Trade Act also introduced a new procedure for the years 1989 and 1990 - the so-called "Super 301" - whereby USTR was required to identify priority unfair trade practices and priority foreign countries and initiate Section 301 investigations with a view to negotiating an agreement to eliminate or compensate for the alleged foreign practice, failing which unilateral retaliatory action had to be taken. This provision has now lapsed. However pressure exists in Congress for the reintroduction of a similar provision. A bill to this end has already been tabled before Congress.

An additional provision introduced by the 1988 Trade Act is the "Special 301" procedure concerning intellectual property (IP) protection. This provision requires the Administration to identify priority foreign countries it considers to be denying adequate IP rights to US firms. This can, under certain conditions, lead to unilateral measures by the US.

Comments/Estimated Impact

Unilateral action under Section 301 on the basis of a unilateral determination without authorisation from the GATT contracting parties is illegal under the GATT. Such unilateral action runs counter to basic GATT principles and is in clear violation of specific provisions of the General Agreement. Except in the fields of dumping and subsidisation, where autonomous action is possible, measures taken against other parties must be sanctioned by the GATT Contracting Parties.

The US used the Section 301 procedure twice against the Community in 1989: first on 1 January when retaliatory measures were introduced against the EC in the hormones dispute (see below), and then, on 5 July, the USTR made a determination of unfairness with respect to the EC oilseeds regime.

Additionally, the US repeatedly used the threat of Section 301 action in 1989, in flagrant violation of GATT rules. The disputes concerning canned fruit, shipbuilding and Airbus were cases in point. The Community will continue to defend its GATT rights whenever Section 301 is used to the detriment of its trading rights.

The elimination of the unilateral provisions of the Trade Act has been an important EC objective in the Uruguay Round of GATT trade negotiations. The Community has sought an unequivocal undertaking from the US and other GATT Contracting Parties to bring their domestic legislation into conformity with GATT rules as part of the final Uruguay Round package.

I.B Hormones Dispute - US Unilateral Action

Description

An example of the use of Section 301 action by the US was the retaliation against the EC in the hormones dispute when the US raised tariffs to 100% in January 1989 on selected EC foodstuffs (Community directive 146/88 prohibits the use of certain hormones in livestock farming but does not discriminate between Community producers and those of third countries).

Comments/Estimated Impact

These trade sanctions were estimated to be worth $100 million annually. In an attempt to de-escalate the trade dispute a Task Force was set up in February 1989. The Task Force met several times and agreed an interim measure in May 1989 under which certain meat exports could take place on the basis of producer guarantees. However, US exports of beef to the Community did not significantly improve as the traditional big US exporters do not produce hormone-free beef and beef prices in the US have been going up so that there is little incentive to export. Consequently, the US have only readjusted their retaliation measures marginally.

Within the GATT, the large majority of Contracting Parties have voiced their disapproval of the retaliation measures. The Community, on 11 October 1989, obtained the consent of the Chairman of the GATT Council and the Director General to hold informal consultations in their personal capacities, in an endeavour to find a solution to the hormones dispute. It is the Community's assumption that these illegal US unilateral retaliatory measures will be removed in the context of the successful conclusion of the Uruguay Round negotiations.

The Harkin Amendment, signed by the President in mid-December 1989 relates to the supply and transport of US meat to US Military Commissaries in Europe who would normally buy European beef. The Congressional background to this measure leaves no doubt as to its purpose. The Congressional Record of 1 August 1989 indicates that Senator Harkin "offered his amendment because the EC put a ban on all US meat and meat products that were using hormones". The first shipments began in July 1990 and up to the end of October 1990 it was estimated that roughly 4,000 tons of beef have been shipped, with a loss of approximately $16 million to EC beef producers.

I.C Telecommunications - Trade Act

Description

The "Telecommunications Trade Act of 1988" is analogous to 'Super 301' in that it is based on identification of 'priority countries' for negotiation and the threat of unilateral action (e.g. termination of trade agreements, use of Section 301 and bans on government procurement) if US objectives are not met.

The stated objectives are to "provide mutually advantageous market opportunities", to correct imbalances in market opportunities and to increase US exports of telecommunications products and services.

Comments/Estimated Impact

The Community has been designated as a priority country under the Act, despite the fact that a major liberalisation of the EC market is taking place in the context of the 1992 programme and that negotiations on a multilateral services agreement are still under way in the GATT-Uruguay Round negotiations. Community legislation has now paved the way for liberalisation of the procurement sector, the terminal sector, and value-added and data services. Liberalisation in the satellite and mobile fields is also under way. In the Uruguay Round, the Community has put forward substantial offers on procurement and services.

The Community cannot accept a unilateral determination by the US of what constitutes a barrier or when "mutually advantageous market opportunities" in telecommunications have been obtained. US efforts to initiate negotiations under threat of unilateral retaliation can only hinder the multilateral negotiations. In addition, such sectoral reciprocity is inconsistent with the principles of the multilateral trading system.

Nevertheless in informal meetings the Community has provided the US with information relating to the EC legislation on the construction of the Single Market for telecommunications. It has also addressed actual or potential barriers to trade in the US market which have been identified in the telecommunications sector (see relevant sections of this Report).

The US continues to enjoy a substantial surplus in bilateral trade with the EC in this sector.

I.D Public procurement-Trade Act

Description

The Trade Act of 1988 (Title VII) stipulates that US procurement of goods, from signatories to the GATT Code that are "not in good standing" with the Code, shall be denied. Procurement prohibition is also mandated against any country which discriminates against US suppliers in its procurement of goods or services, whether covered or not by the Code, and where such discrimination constitutes a "significant and persistent pattern or practice" and results in identifiable injury to US business.

To this effect, the US President is required to establish, as from <u>30 April 1990, and on an annual basis a report on the foreign countries which discriminate against US products or services in their procurement</u>.

By 30 April 1991, those foreign countries, which discriminate against US suppliers, have to be identified by the USTR. Two possible courses of action would then be possible:

- *the USTR may resort to unilateral action against the offending foreign country, if the Code dispute-settlement fails to give satisfaction to the US (for the procurement covered by the Code). The dispute-settlement procedure should be initiated within 60 days after 30 April 1991 (first week of July 1991) and should be concluded within one year (July 1992). After that date, the President is required to deny such countries access to US procurement (1);*

- *the USTR shall identify foreign countries discriminating against US suppliers in procurement not covered by the Code, and 60 days after 30 April 1991 (first week of July 1991), deny such countries access to US procurement[1].*

<u>Comments/Estimated Impact</u>

However, the USTR did not, in 1990, which was the first year of implementation of this provision, resort to identifying "discriminatory" countries.

Unilateral US determination on whether Code signatories are in compliance with the Code represents a violation of GATT procedures. The latter would require the US to raise the matter in the relevant committee and pass through a process of consultations and dispute settlement. Unilateral action, at any stage, to reinstitute preferences or to ban certain countries from access to US procurement would clearly be contrary to the Code provisions. Such measures could only be authorized by the relevant committee.

Furthermore, no amendment or elimination of this provision, has been offered by the US up to now in the Uruguay Round Procurement Code negotiations.

(1) The procurement prohibition is set in Section 4 of the Buy America Act of 3.3.1933.

II OTHER UNILATERAL/EXTRATERRITORIAL LEGISLATIVE MEASURES

II.A Extraterritorial aspects of US laws

Description

For reasons of domestic or foreign policy, the US has adopted a number of laws which entail to some extent extraterritorial application. Despite the fact that the Community may in some cases understand the underlying reasons and might agree with the objectives, such legislation nevertheless can expose Community enterprises to conflicting requirements.

Extraterritorial reach affects inter alia:

- *importers and exporters based outside the US, who have to comply with US export and re-export control requirements and prohibitions;*
- *manufacturers, which have to keep track of end-users or potential mis-users of sensitive items;*
- *banks or financial institutions, which have to comply with "money-laundering" reporting requirements or to disclose documents covered by professional secrecy (cf chapters IX B 2 and IX D 2).*

The most blatantly extraterritorial element of US legislation is the Export Control Regulations issued under the IEEPA(1) and the EAA(2). The latter lapsed last Autumn but has been reintroduced in Congress this year. These regulations require companies created under the law of the Member States and operating in the Community to comply with US export and re-export regulation. This includes compliance with US prohibitions on re-exports for reasons of US national security and foreign policy. Even when goods have left US territory, they are still regarded as being subject to US jurisdiction. These regulations have been criticized many times already by the Community and its Member States, notably during the Siberian pipeline dispute of 1982, but they continue to be applied.

Serious extraterritorial concerns have also been raised by the US Trade Act of 1988 amendment to section II of the EAA which provides for sanctions against foreign companies which have violated their own countries' national export controls, if such violations are determined by the President to have had a detrimental effect on US national security. Moreover these sanctions are of such a nature (prohibition on contracting/procurement by US entities and the banning of imports of all products manufactured by the foreign violator) that they are contrary to the GATT and its Public Procurement Code.

New legislative proposals with extraterritorial reach, tabled this year will, if enacted, aggravate the situation further.

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(1) *International Economic Emergency Powers Act of 1977 (50 USC Sec 1701-1706)*

(2) *Export Administration Act of 1979, as amended.*

Comments/Estimated Impact

The impact on business is often increased red tape and legal arguments with foreign administrations as regards to jurisdiction over the business concerned.

It is generally recognized that the extraterritorial application of US laws and regulations, where it exposes companies to conflicting legal requirements, may have a serious effect on international trade and investment (cf. in particular the work of the OECD on "Minimizing conflicting requirements. Approaches of Moderation and Restraint"). Moreover, in many instances the extraterritorial application of certain laws implies an intention to replace the US laws or fundamental policy of another country or international entity, such as the EEC, within its own territory, by the policy or laws of the foreign country in question. This is clearly contrary to international law.

It is also the reason why many states including Community Member States have adopted blocking statutes in order to counteract the consequences of the extraterritorial application of foreign legislation.

For these reasons the continued extraterritorial application of US laws contributes to serious jurisdictional conflicts between the US and the Community and its Member States and has a negative influence on the climate for trade and investment between the US and the Community.

II.B Marine Mammal Protection Act

Description

The US Marine Mammal Protection Act of 1972, as amended through 1988, is aimed at the protection of different species, including dolphins.
The Act notably sets a ratio of dolphins mortality in the fishing operations of US tuna vessels in the Eastern Tropical Pacific Ocean as the desired level of dolphin fatalities.
This US legislation also provides for trade sanctions on countries failing to observe comparable standards for protection of dolphins.
In this context, an embargo on exports to the US of yellowfin tuna products has been placed on Mexico since 20.2.1991. A previous embargo on Panama was lifted when this country adopted measures to ban completely dolphin by-catches by its vessels.

The law also applies the embargo to exports to the US of yellowfin tuna products from "intermediary nations". "Intermediary nations" are defined as countries which import tuna from countries under direct US embargo. These "intermediary" countries are required to ban imports of yellowfin tuna products from the country embargoed by the US. All "intermediary nations" who do not comply within 60 days of the initial US embargo will be the subject of a secondary embargo on their exports of yellowfin tuna products to the US.

Comments/Estimated Impact

The Community does not contest the validity of the objective of this environment protection law, which it shares. However, the Community considers that measures for the conservation of living resources, including dolphins should be based on scientific information/advice; this would be better achieved through multilateral work than through the unilateral setting of trade restrictive conservation/ecological rules.

Furthermore, certain provisions are, in the Community's view, incompatible with international law or principles. In relation to GATT, for example, it could be said that the imposition of a secondary embargo on intermediary nations, first on tuna products and after a certain period on all fisheries exports from these countries to the US, appears to be out of all proportion with the objective of the reduction of dolphin mortality, and therefore GATT-illegal.

Four Member States of the Community (Italy, France, Spain, Portugal) are being threatened by this secondary embargo. The value of the tuna exports concerned was 4 million ECU in 1989. Furthermore, a total ban on all fisheries products from these countries to the US can be implemented 6 months later (value of the EC exports concerned: 62 million ECU).

II.C Fisheries legislation

Description

The Fishery Conservation Amendments of 1990 introduce changes in US fisheries legislation, especially in the Magnuson Fishery Conservation Act of 1983, which have a particular impact on international fisheries matters and the US relationship with its partners, including the Community.
For example, in addressing the problem of large-scale pelagic driftnet fishing, the introduction in the Governing International Fisheries Agreements (GIFA) concluded by the US for access to US waters of a number of unilateral control measures beyond the US 200 miles exclusive economic zone is envisaged (US access to positions of driftnet fishing vessels, US right to board and inspect such vessels, US right to have on-board observers etc.).
The amendments also prescribe that the Department of Commerce lists the nations whose nationals engage in large scale driftnet fishing in a manner which is considered by the US as either diminishing the effectiveness, or as being inconsistent with any international agreement governing such practices observed by the US. The nations so listed are "certified" for a boycott of their marine products under the so-called "Pelly amendment" (the Fisherman's Protective Act of 1967).

<u>Comments/Estimated Impact</u>

The US is entitled to link access to the living resources in its exclusive economic zone to certain conditions.
Moreover, the US Administration declared its intention to use some of the new Congressional directives as advisory guidelines for relations with third countries, stressing that it would prefer to make use of international cooperation to achieve the aims set out by Congress.
However, the amendments passed by Congress confirm a tendency of the US to use their own measures (e.g. US definition of large driftnets) as benchmarks for third countries' policies. The US authorities are also empowered to seek to impose these measures unilaterally, if necessary by means of a total boycott of the fisheries trade. However, well founded the US objectives, their actions should reflect the work of international cooperation. Otherwise, such unilateral measures can be disproportionate to the objective of conservation and destabilising for international trade.

III IMPORT BARRIERS

III.A Tariff problems

III.A.1 High tariffs

Description

Numerous products exported from the EC are subject to high US tariffs. Certain textile articles, ceramics, tableware, glassware, vegetables and footwear are all subject to tariffs of 20% or more. The following examples illustrate high US tariffs (the corresponding EC tariff rates are in brackets) :

Certain clothing (see note (1), end of sub-chapter A)	20-34.6% (13-14%)
Including soccer uniform and warm ups	35%
Silk and MMF/woollen-blended fabrics (2)	38% + 48.5 cents/kg (11%)
Ceramic tiles, etc. (3)	20% (8-9%)
Certain tableware (4)	26-35% (5.1-13.5%)
Including hotel porcelain dinnerware	35%
Certain glassware (5)	20-38% (12%)
Certain footwear (6)	37.5-48% (4-6-8-20%)
Garlic and dried or dehydrated onions(7)	35% (16%)
Zinc alloys (8)	19% + 48.5 cents/kg (3,5%)

Comments/Estimated Impact

Such high tariffs reduce EC access possibilities for these products.

Although it is difficult to measure this impact, tariff reductions on these products would significantly increase the competitiveness of EC firms on the US market. High tariffs have been singled out for considerable reductions in the Community's proposal for tariff reductions in the Uruguay Round in accordance with the Montreal Declaration which foresees the reduction or elimination of tariff peaks.

Tariff reductions are negotiated within the framework of the Uruguay Round. Unfortunately, the method of tariff negotiation adopted by the US, a "request-offer" approach, does not facilitate these reductions. Contrary to the EC approach of across the board formula cuts the US has taken a pick and choose approach for sectors of interest to the US which concentrates on eliminating low tariffs but generally leaves high tariffs untouched and thus maintain the high level of protection of US industry in these sectors.

III.A.2 Tariff Reclassifications

Description

As a result of decisions by US Customs services and following the introduction of the Harmonised System (HS), the United States has periodically and unilaterally changed the tariff classification of a number of imported products. This has in most cases resulted in an increase in the duties payable.

In particular, in its Harmonized Tariff Schedule (HTS), the US has increased its duties on certain textiles. Duties on wool-woven fabrics and wool/silk blends (see note (9) at end of sub-chapter A) have been increased from 15 to 39%, 33% to 36% and 39% and from 8% to 33% respectively as a result of a change in classification by chief value to classification by chief weight of fabric.

In addition, US tariffs for certain wool-blended tapestry (10) and upholstery fabrics have increased from 7% to 33% and 38% as a result of the merging of several tariff lines. For acrylic textile wall coverings US tariffs have increased from 8.5% to 12.5% (11).

Furthermore, the new classifications of gaskets and gaskets material (12) and red dye (13) have led to increases in duty rates from 3.5 and 3.7% to 18% and from 3.1% to 15 % respectively, without having been subject to joint HS negotiations. In the same manner, a classification of sugar confectionery (including white chocolate) has led to increased duty rate from 7% to 17.5% (14). The duty increases under the new tariff reclassification are not justified and contravene the agreed GATT guidelines for transposition to the HS.

Similarly, the Community has cause to complain about other reclassifications which effectively constitute a unilateral extension of a quantitative restriction. For instance, US Customs reclassified wire ropes with fittings so that these now require an export certificate for entry into the US.

Comments/Estimated Impact

The overall impact of tariff reclassification is difficult to quantify. However, the textile tariff increases outlined above have serious repercussions for EC textile exports to the US : extra duties on wool-woven fabrics and wool/silk blends, mainly supplied by the EC, amount to approximately US $1.5 m. (average 86, 87, 88).

<u>Notes to points A1 and A2</u>

Harmonized system (HS) codes of the items concerned :

(1) The items concerned can be found in the following headings :

61.01	61.09	62.01	62.09
02	11	02	11
03	12	03	12
04	14	04	16
05	15	05	
06		06	

(2)	54.07.9105	54.08.3105		
	9205	3205		
	9305	3305		
	9405	3405		
(3)	69.07	69.08		
(4)	6911.1010	6911.10.50		
	35	6912.00.20		
(5)	70.13.1050	70.13.2920	70.13.3920	70.13.9940
	2110	3110	9110	9950
	2910	3220	9910	
(6)	64.01.1000	64.02.1950	64.02.9170	64.04.1170
	9100	3050	64.06.1025	1920
	9290	3060	1030	1935
	9960	3070	1050	1940
	9990	9150	64.04.1150	1950
	64.02.1930	9160	1160	
(7)	07.12.2020	07.12.9040		
(8)	7901.2000			
(9)	51.11.1160	51.12.1100	54.07.9105	
	1960	1960	54.08.3205	
	2060	2000	3305	
	3060	3000		
	9070	9060		
(10)	51.11.2060	51.11.9060		
	3060	51.12.1960		
(11)	59.05.0090			
(12)	45.04.90.20	45.04.10.50		
(13)	32.05.00.10			
(14)	17.04.90.40			

III.B User fees

Introduction

As a result of laws enacted in 1985 and 1986, the United States imposes user fees with respect to the arrival of merchandise, vessels, trucks, trains, private boats and planes, as well as passengers. The Customs and Trade Act of August 1990 and the Omnibus Budget Reconciliation Act of October 1990 extend and modify these provisions, among other things, by considerably increasing the level of the fees. This legislation indicates a certain tendency to seek to use fees rather than taxes, as a source of revenue. Excessive fees levied for customs, harbour and other arrival facilities, that is for facilities particularly used by importers, place foreign products at an unfair competitive disadvantage vis-à-vis US competition.

III.B.1 Customs User Fees

Description

The most significant of the Customs User Fees (CUF) is the Merchandise Processing Fee levied on all imported merchandise, except for products from the least developed countries, from eligible countries under the Caribbean Basin Economic Recovery Act, or from United States insular possessions as well as merchandise entered under Schedule 8, Special Classifications, of the Tariff Schedules of the United States. In addition, the US/Canada Free Trade Agreement provides for a progressive phasing out of the fees, effective from 1.1.94.

The merchandise processing fee from December 1, 1986, to September 30, 1987 was 0.22 percent of the value of the imported goods and has been fixed at 0.17% ad valorem for 1988 and 1989.

The Customs and Trade Act of 1990, effective 1 October 1990, provides a number of modifications to the previous law for one year. The Omnibus Budget Reconciliation Act of October 1990 extends it for four more years, to 30 September 1995. It also provides for discretionary adjustment of fees.

The main provisions of the current law are :

new law	*previous law*
- *0.17 percent ad valorem rate on formal entries*	*idem*
- *$21 minimum and $400 maximum on formal fees*	*no floor or ceiling*
- *$3 surcharge for manual formal entries*	*no surcharge*
- *discretionary adjustment of fees for formally entered merchandise within a range of 0.15 to 0.19% so as to offset Customs' salaries and expenses*	*no adjustment*
- *informal entries $2 for automated informal entries, $5 for manual and $8 for Customs prepared informal entries*	*no charge on informal entries*

Comments/Estimated impact

It is estimated on the basis of the total value of about $92 billion of US imports from the Community in 1990 that the Merchandise Processing Fee cost the EC approximately $190 million (fees for informal entries not included).

At the request of the EC, the GATT Council instituted a Panel in March 1987, which concluded in November 1987 that the US Customs User Fees for merchandise processing were not in conformity with the General Agreement. The Panel ruled that a Customs User Fee was not in itself illegal but that it should be limited in amount to the approximate cost of services rendered. The GATT Council adopted the panel report in February 1988.

The new legislation of 1990 provides a somewhat more equitable Customs User Fees structure, since the fixing of a ceiling makes the CUF less onerous for high-value consignments. Furthermore, the possibility remains of an adjustment of the level of fees : this would be a step towards a system which reflects the costs of the customs' services rendered. However, the fee is still likely, in many cases, to exceed the cost of the service rendered since the fee, irrespective of the level, is still based on the value of the imported goods. This is admitted in a recent GAO study, which concludes that it is unclear whether even modified ad valorem fees would approximate the costs of processing an importer's individual shipment.

In addition, US Customs is still likely to have a net surplus from the introduction of a minimum fee, as well as from the surcharge for manual entries, and the introduction of fees for informal entries. There is no means of verifying the fairness of the charges until more information on costs is made available. The Budget Agreement of October 1990 requires a report within 30 calendar days of the enactment of the customs Appropriations Act. This will probably be in the Autumn of 1991, and should provide the information required.

The possible adjustment of fees is limited to a range of between 0.15 and 0.19%, and there could still remain a surplus in the CUF fund, even if the adjustment is made. Furthermore, the adjustment is discretionary,. and there are no guarantees that this will in practice be made. A key issue will be the extent to which overcharging in the past will be taken into account in adjusting the fees.

III.B.2 Harbour Maintenance Fee

Description

In October 1986, the United States enacted a Harbour Maintenance Fee. The fee was set at 0.04 percent of the value of commercial cargo loaded or unloaded at US ports and on commercial ship passenger fares. Revenues from the tax were transferred to the Harbor Maintenance Trust Fund. The objective of the fee was to cover 40% of the cost incurred.

The Budget Reconciliation Act of 1990 increases the fee to 0.125 percent, effective 1.1.1991. The new legislation allocates revenues to the navigational programmes undertaken by the National Oceanic and Atmospheric Administration, as well as to the Harbor Maintenance Trust Fund.

Comments/Estimated Impact

The increase in fees is more than three fold. The new fees would appear to have an impact equivalent to the Customs User Fees. In Fiscal Year 1990 (Oct. 1.1989 - Sept. 30.1990) the Harbor Maintenance Fees, levied at the earlier rate of 0.04% ad valorem, raised US $109 million for all imports into the US. Given the trebling of the rate the impact on trade could now be of the order of US $330 million. The EC share could be estimated to be about $60 million.

The Harbor Maintenance Fees are nominally non-discriminatory, because they are levied on imports and exports alike, as well as on cargo transported internally. However, the case appears to be similar to the Customs User Fees. The ad valorem structure of the fees and any cross-subsidiation of activities constitute grounds for a GATT challenge.

III.C Quantitative Restrictions and Import Surveillance

III.C.1 Agricultural and Food Import Quotas

Description

The United States regulates imports of a variety of agricultural products through the establishment of quotas. These cover certain dairy products (including cheese), ice-cream, sugar syrups, certain articles containing sugar (including chocolate crumb), cotton of certain staple lengths, cotton waste and strip, and peanuts. While these restrictions are covered by a GATT waiver, and by the headnote to the Customs Tariff in the case of sugar, they restrict certain EC exports to the US and have a considerable negative effect on world markets.

Section 22 of the US Agricultural Adjustment Act of 1933 requires import restrictions to be imposed when products are imported in such quantities and under such conditions as to render ineffective, or materially interfere with, any United States agricultural programme. Such restrictions are a breach of GATT Articles II and XI. Therefore, the United States sought and was granted in March 1955 a waiver, subject to certain conditions, for its GATT obligations under the above articles with respect to Section 22 quotas. More than 35 years have since elapsed and in the Community's view the continuation of the waiver cannot be justified. In GATT practice a waiver is usually of limited duration.

Unilateral decisions of the US administration on the application of the cheese import quota in 1988 and 1989 resulted in a globalisation of certain EC allocations in favour of other third countries. Such a decision was incompatible with the provisions of the 1979 cheese arrangement between the EC and US.

Comments/Estimated Impact

EC exports potentially most heavily affected by United States quotas are dairy products, cheese and sugar-containing articles. In 1989 Community exports to the US of dairy products and cheese were approximately 402 million ECU, while exports of sugar and related products were approximately 119 million ECU.

III.C.2 Untimely product sampling

Description

US Customs follow a sampling and inspection procedure which does not distinguish between perishable and non-perishable goods. For example, in the past whole shipments of citrus fruit have had to be dumped while imports of cut flowers have been subject to very lengthy procedures to determine what insect species if any might be present, leading to quality decreases of imported flowers. More recently, the American authorities caused considerable damage to European shipments of cocoa powder during a routine drug inspection and rendered the contents unfit for later food-manufacturing because of the methods used. Furthermore, *In accordance with the provisions of the Federal Food, Drug and Cosmetic Act, the Food and Drug Administration (FDA) takes samples and analyses for listeria in the case of consignements of smoked salmon destined for import into the US from certain Member States of the Community. As a result of this and other measures, consignments of goods stand in line waiting to be tested, and during the period of inspection deteriorate and in some cases become unacceptable for their intended market. Furthermore, only a handful of ports of entry have suitable testing facilities, which creates further outlays and causes additional deterioration of products.*

Comments/Estimated Impact

The EC does not dispute the right of the US authorities to check imported perishable products for sanitary reasonsU. But the Administration has a responsibility to perform the tests efficiently and without imposing unacceptable commercial losses on foreign exporters. US practice amounts to an impediment to trade in perishable products with evident effects on EC businesses.

III.C.3 Excessive invoicing requirements, delays in customs clearance

Description

Invoice requirements for exporting certain products to the US can be excessive. This is particularly the case for textiles/clothing where all shipments are subject to the completion of a very detailed and complicated form (Customs Form N° 5515).

Many points on this form would appear to be irrelevant for customs or statistical purposes. For example, for garments with an outershell of more than one construction or material, it is necessary to give the relative weight, percentage values and surface area of each component ; for outershell components which are blends of different materials, it is also necessary to include the relative weights of each component material.

Community exporters of footwear and machinery are faced with the same type of complex/irrelevant questions (e.g. a requirement to provide the names of the manufacturers of wood-working machines, and of the numerous spare parts).
The US Customs and customs house brokers can also request proprietary business information (e.g. listing of ingredients in perfumes or composition of chemicals).

In addition, a new US Customs Directive (Accurate and Complete Invoices) applicable to a wide range of products (chemicals, textiles, ball or roller bearings, machines, machine tools, plastics, printed matter, etc.) may be introduced shortly, under which reporting requirements for information on imports will be further increased. Concerning textiles, for example, detailed indications of prices, the composition of garments *and parts of the body covered by garments will be required if this directive is introduced. Similarly, requirements for data on products such as chemicals, pharmaceuticals and essential oils are tantamount to the disclosure of commercial secrets (exact composition of a dyestuff, individual components of a surface-active preparation, etc.)*

Moreover, under the new directive the importer, rather than the exporter, would be responsible for supplying detailed information to the US authorities. This means that the importer becomes responsible for complying with US regulations. Thus, in case of non-respect, penalties would be applied to the importer. This can have the effect of discouraging US importers from dealing with European manufacturers.

In addition to excessive invoicing requirements, customs clearance delays, which can exceed 2 months, represent an additional burden for exporters to the US.

The abolition of informal entry procedures for textiles in February/March 1986 have also caused particular hardship for certain companies who send small consignements of textiles or clothing on an irregular basis to the US, as they now have to employ customs brokers or arrange for the importers to attend at Customs to clear goods formally.

Comments/Estimated Impact

The information required by the US Customs Service on trade invoices goes far beyond the information which is necessary for a customs declaration and tariff procedures. The new US provisions, if implemented, would not have the effect of standardizing or improving the handling of invoices and/or customs declarations but rather constitute obstacles to exports to the US. They would in particular increase information costs for exporters and constitute a barrier against new entrants and small companies. As a result, large established suppliers are privileged and small new competitors disadvantaged. These effects are particularly disruptive in diversified high-value and small-quantity markets which are of special relevance for the Community. Excessive delays in customs clearance procedures can prevent exporting companies from complying with delivery deadlines and can hinder future involvement in projects which are on tight deadlines.

III.D *Measures affecting vessels*

III.D.1 **Tax on maritime equipment and repair of ships abroad**

Description

The United States applies a 50% ad valorem tax on:

- *non-emergency repairs of US owned ships outside the USA and;*
- *imported equipment for boats, including fish nets.*

The basis of this tax is Section 466 of the Tariff Act of 1930, amended in 1971 and in July 1990. Under the later amendment the tax would not apply, under certain conditions, to foreign repairs of LASH barges and spare vessel repair parts or materials.

Comments/Estimated Impact

The direct revenue from the tax on repairs outside the US is $10-15 m. on an annual basis but its effect in terms of loss of activity for European shipyards is much greater (the turnover of shipbuilding repairs inside the US amounts to $1.5 bn., as compared to $30 m. spent on repairs outside the US).

III.D.2 Buy American requirements for certain categories of vessels

Description

The use of certain categories of foreign-built vessels is restricted in the US. This is the case for:

- ***Fishing vessels***

  A US flag vessel when foreign-built, cannot be documented for fisheries in the US's 200 mile exclusive economic zone (section 12108 of volume 46 of United States Code).

  This prohibition is wide-ranging since the definition of fisheries includes processing, storing, and transporting (Commercial Fishing Industry Vessel Anti Reflagging Act of 1987).

  The US has, however, entered into Governing International Fishing Agreements (GIFA), which give some foreign flag vessels rights to fish in the US fishing zone.

- ***Vessels used in coastwise trade***

  Foreign-built (or rebuilt) vessels are prohibited to engage in coastwise trade either directly between two points of the US or via a foreign port. Trade with US island territories and possessions is included in the definition of coastwise trade (US Merchant Act of 1920 = Jones Act, section 883 of volume 46 of United States Code). Moreover, the definition of vessels (Jones Act and section 390 of volume 46 of US Code) has been interpreted by the US administration to cover hovercraft and inflatable rafts. The limitations on rebuilding act as another discrimination against foreign materials: the rebuilding of a vessel of over 500 Gross Tons (GT) must be carried out within the US if it is to engage in coastwise trade. A smaller vessel (under 500 GT) may lose its existing coastwise rights if the rebuilding abroad or in the US with foreign materials is extensive (see section 883 of volume 46 of US Code, amendments of 1956 and 1960).

- ***Special work vessels***

  No foreign-built vessel can be documented and registered for dredging (see section 292 of volume 46 of US Code), towing or salvaging in the US (see points a) and d) of section 316 of volume 46 of US Code).

Comments/Estimated Impact

The analysis of EC exports to the US of certain categories of vessels shows the negative impact of US restrictions on EC imports (average 84/89):

category CN code	average EC exports in 1000 ECUs	
	to the world excluding EC	US share
fishing boats 8901.40 + 74	183,789	0
vessels for towing or pushing 89.02	68,927	0
dredgers 8903.11 + 91	41,078	0
vessels for the transport of goods and passengers 8901.61 + 65	853,034	9.5%

The "Buy American" requirements for various categories of vessels mean that third countries will not be able to have access to the US market at a time when part of the ageing US fleet needs to be renewed.

III.D.3 Subsidies and tax policies

Description

The Merchant Marine Act of 1939, as amended provides for various subsidies schemes or tax deferment measures in the shipbuilding sector which contain domestic build requirements. They are as follows :

- ***Construction differential subsidy (CDS)***

  Title V of the Merchant Marine Act of 1939, as amended, provides for a direct Federal grant for the construction of US-flag merchant ships in US ship yards under Buy American requirements.

  Although no public source funding seems to have been provided by the Government since 1981, the legislation is still on the statute book and can be used in the future.

- *Capital Constructions Fund (CCF) + Construction Reserve Fund (CRF)*

Section 607 of the Merchant Marine Act, as amended, enables US shipowners to defer certain taxable income via the CCF or CRF to buy or transform vessels under the condition that they use American material or goods (Buy America) except for fisheries vessels (under the CCF program).

Approximately $1.3 billion in funds had cumulated in the CCF as of the end of 1989. The CRF fund was 5 million in Fiscal Year 1989.

However, it should be noted that in recent years use of these funds has been limited.

- *Operating Differential Subsidy (ODS)*

Section 601 of the Merchant Marine Act, as amended, provides for the payment of an Operating Differential Subsidy (ODS) to US operators of ships built in the US of US materials so as to place their operating costs on a parity with those of foreign competitors.

No new ODS contract has been given since 1981. During Fiscal Year 1991, the US authorities have distributed in excess of $261 million on old ODS contracts.

- *Federal Ship Financing Guarantees*

Title XI of the Merchant Marine Act, as amended, authorizes the US Government to provide direct guarantees to US shipowners to obtain commercial loans for the construction or reconstruction of nearly all categories of vessels (except fishing vessels). Guarantees may be granted for up to 75% of the vessel's actual cost. In order for a new non-fisheries vessel to be eligible for these financial guarantees, it must be built entirely in a US shipyard, all components of the hull and superstructure fabricated in the US and the vessel entirely assembled in the US.

For Fiscal Year 1988, the guarantees covered 3700 vessels.

As of September 30, 1990, Title XI guarantees in force amounted to just over $3 billion.

<u>Comments/Estimated Impact</u>

The Buy America requirements imposed in these different types of subsidies clearly favour US shipbuilders and equipment manufacturers and act as a restriction to imports. Even if certain of these measures have not been used for some years, there is no guarantee that they will not be implemented in the future.

IV. EXPORT AND OTHER SUBSIDIES

IV.A Export Enhancement Programme (EEP)

Description

The Food Security Act of 1985 (the Farm Bill) required the United States Department of Agriculture (USDA) to use Commodity Credit Corporation stocks worth $1 billion over a three-year period to subsidise exports of US farm products, with the option of going up to $1.5 billion. This programme was intended to support wheat exports to a limited number of countries, most of which are traditional EC markets. It is now used for a wide range of commodities (mainly wheat, wheat flour, barley, feed grains, vegetable oils, poultry, eggs and dairy cattle) and for exports to all food-importing countries except Japan and South Korea. In particular, in 1987, the United States added China and the USSR to the list of countries to which EEP can apply .

The 1988 Trade Act prolonged the programme to 1990 and increased it from $1.5 billion to $2.5 billion, thus extending further its depressive effect on world markets.

The 1990 Farm Bill reinforced the tough US attitude, providing for the continuation of EEP without specified programme limits. It maintained a minimum of $500 million per year, for five years, though the recent Budget Reconciliation Act reduced this amount by $75 million for Fiscal Year 1991. Through 1st February 1991, $315 million of this $425 million had been spent and Secretary Yeutter has asked the Office of Management and Budget to lift this ceiling for Fiscal Year 1991 (the estimate for Fiscal Year 1991 EEP expenditure is now approximately $900 million and $1.2 billion for Fiscal Year 1992).

Comments/Estimated Impact

As of 4 October 1990 about 76.9 million tons of wheat, 3.5 million tons of wheat flour, 8.2 million tons of barley, 0.18 million tons of frozen poultry, and substantial quantities of eggs, dairy cattle, malt, vegetable oil, and feed grains have been announced for export subsidisation within the programme. In financial terms, subsidies already granted are valued at approximately $2,874 million.

This programme would appear to be against the spirit of the Mid-Term Review of the Uruguay Round of trade negotiations which commits participants, "to ensure that current domestic and export support and protection levels in the agricultural sector are not exceeded". The Uruguay Round provides an opportunity to address this and other forms of US agricultural subsidies.

IV.B Marketing Loans

Description

Marketing loans were provided for in the Farm Act of 1985, on a discretionary basis for feedgrains, wheat and soyabeans but on a mandatory basis for rice and upland cotton. They permit the repayment of government buying-in loans for certain agricultural commodities at less than the loan rate and thus function as an additional measure of internal support. The Agricultural Competitiveness and Trade Act of 1988 established a mechanism for automatically triggering marketing loans for wheat and feedgrains if it were judged by the US that there had been insufficient progress in the agricultural negotiations in the Uruguay Round. The 1990 Farm Bill provided for the continuation of mandatory marketing loans for upland cotton and rice and extended the scope of same to include soyabeans and other oilseeds.

Comments/Estimated Impact

Marketing loans, which may be considered extended subsidies for agriculture, have the effect of continuing to exert downward pressure on world prices at a time when it is important to work towards improving conditions on the world markets.

Though the deadline for the automatic triggering of marketing loans was postponed in 1990, this remains contrary to the spirit of the Standstill Commitment reached at Punta del Este (part III concerning the notion of not taking measures to improve negotiating position). Furthermore, the Mid-Term Review of the Uruguay Round of trade negotiations committed participants "to ensure that domestic and export support and protection levels in the agricultural sector are not exceeded".

IV.C Market Promotion Program (Targeted Export Assistance)

Description

The Food Security Act of 1985 established a new programme, entitled Targeted Export Assistance (TEA). Under this programme, the Secretary of Agriculture had to provide $110 million (or an equal value of Commodity Credit Corporation commodities) each fiscal year until FY 1988, specifically to offset the adverse effect of subsidies, import quotas, or other unfair trade practices abroad. For fiscal years 1989 and 1990 figures of $200 million and $220 million were approved.

For the purposes of the TEA programme, the term "subsidy" includes an export subsidy, tax rebate on exports, financial assistance on preferential terms, financing for operating losses, assumption of costs of expenses of production, processing, or distribution, a differential export tax or duty exemption, a domestic consumption quota, or any other method of furnishing or ensuring the availability of raw materials at artificially low prices.

Under the 1990 Farm Bill the TEA programme was renamed the Market Promotion Program (MPP) and expanded to "encourage the development, maintenance and expansion of commercial export markets for agricultural commodities". Whereas the TEA programme was limited to commodities where the US considered that exports had been adversely affected by unfair foreign trade practices, the MPP, while according such exports priority for assistance, allows consideration also to be given to other commodity groups.

Comments/Estimated Impact

For Fiscal year 1988 about $100 million was used to provide subsidies for the TEA programme for promoting exports of high value products (e.g. wine, fruits, vegetables, dried fruits and citrus), mostly to Europe and the Far East. TEA programme expenditure in 1989 amounted to $200 million and also $200 million in 1990. Maximum level of funding of MPP for Fiscal Year 1991 amounts to $200 million.

Agricultural subsidies which are trade distorting are to be addressed within the Uruguay Round.

IV.D Deficiency Payments

Description

The US supports its agriculture by commodity loans which guarantee the farmer a minimum price (loan rate) if he cannot sell his produce above this price on the open market and by deficiency payments which are calculated as the difference between a government-established target-price and the higher of the market price and the loan rate.

Comments/Estimated Impact

Deficiency payments are an internal support measure which, nevertheless, may impact substantially on external trade. Whether they function as an import barrier or as an export subsidy depends on whether the country is a net importer or a net exporter.

Thus, it is justified to consider the US deficiency payments for cereals as an export subsidy because they are a net exporter of cereals and would certainly export less if such a system were not in place. The real effect is, however, difficult to calculate as the US combine deficiency payments with the obligation to set aside certain percentages of farmland in order to benefit from the system.

The present deficiency payment for wheat in the US is $1/bushel or 36.74/ton which represents the difference between the target price ($4/bushel or $147/ton) and the domestic market price. However, it is the target price which the farmers receive and which determines their production decisions. No difference is made as to whether the product is used domestically or exported. As the US exports, on average, two thirds of its wheat production, it is fair to say that, in this case, two thirds of the deficiency payments are assistance to exports.

Deficiency payments allow the US to have lower internal prices than within the Community and to start with *__direct__* *export subsidies from lower levels. For the world market, however, it does not matter whether prices are determined by deficiency payments or direct export subsidies.*

In the Uruguay Round, both the EC and the US have proposed to reduce internal support (including deficiency payments) by means of reductions in an overall Aggregate Measure of Support. However, while the US requests the EC to make a specific commitment on export subsidies (higher reduction than for other support) they do not want to treat deficiency payments equally as export subsidies.

IV.E Credit guarantee and food aid programmes

__Description__

The Export Credit Guarantee Program (GSM-102) is the largest US agricultural export promotion program and has been functioning since 1982. It guarantees repayment of private, short-term credit for up to three years.

The Intermediate Export Credit Guarantee Program (GSM-103) was established by the Food Security Act of 1985 and complements GSM-102 by guaranteeing repayment of private credit for 3-10 years.

Public Law 480 (P.L. 480) has amongst its (generally altruistic) aims the expansion of foreign markets for US agricultural products. Its Title I makes US agricultural commodities available through long-term dollar credit sales at low interest rates for up to forty years. Donations for emergency food relief are provided under Title II. Title III authorises "food for development" projects.

__Comments/Estimated Impact__

Congressionally authorised levels for GSM-102 and 103 were only slightly modified by the 1990 Farm Bill. The legislation authorises not less than $5 billion annually for GSM-102 and $500 million for GSM-103. Additionally, the legislation calls for not less than $1 billion in export credit guarantees to be made available specifically to emerging democracies during the fiscal 1991-1995 period.

In fiscal year 1990, approval of credit guarantees under GSM-102 and 103 totalled $4.3 billion, a decrease of 17% from the fiscal year 1989 level. As of 9 November 1990, fiscal 1991 guarantee announcements were $1.6 billion under GSM-102 and $14 million under GSM-103. A total of $147 million in guarantees had been approved under the programmes.

Food aid under the P.L. 480 programme for fiscal 1991 is budgeted at $1,546 million. This represents an increase of $25 million in programme funding over the 1990 level.

Agricultural subsidies which are trade distorting are to be addressed within the Uruguay Round.

IV.F Californian subsidies on water

Description

Each year, the Central Valley Project provides 7 million acre-feet of water to some 3 million acres of Californian farmland. In November 1989, the US Federal Government renewed this heavily-subsidised water supply contract for another forty years. The US Bureau of Reclamation, the federal agency concerned, supplied about 20% of all water used by agriculture in 1988. (It should be noted, however, that in order to deal with the prevailing drought conditions, the Federal government has requested one-year emergency authority from Congress to break its long-term contracts with Central Valley farmers! so that the water supply can be re-directed where it is most needed. The Central Valley Project recently cut water deliveries to farmers by 75%, while the State Water Project has completely cut off water supplies to farmers for this year.)

Comments/Estimated Impact

The amount of the federal subsidy has been calculated by the General Accounting Office to be worth half a billion dollars annually. Large variations in the price of water between urban and agricultural users have been reported ranging from 3-4 dollars/acre-foot in Fresno County (agricultural use) to 320 dollars/acre-foot in Contra Costa County (urban use).

Agriculture accounts for only 3% of California's domestic product. Yet farmers consume 85% of California's water supplies, with the 30 million non-agricultural users having to make do with the remaining 15%. In addition, the big "water guzzlers" are livestock, feedstuffs, rice, corn, cotton and sugar-beet. Some of these crops are heavily subsidised at federal level and the low rates charged for water had led farmers to waste it on high water-demanding crops of comparatively low value.

This indirect agricultural support for irrigation places Community exports at a disavantage vis-à-vis domestic US production.

IV.G Double Price System

IV.G.1 Rock Phosphate/Fertilizer

Description

Producers of rock phosphate have an export cartel which results in this raw material for fertilizers being sold for export at a price well above the domestic price and only marginally below the price of the phosphate-based fertilizers sold by the selfsame producers.

European fertilizer manufacturers are thus forced to pay excessively high prices for their raw material, the rock phospate, and face low priced competition in the EC and on third markets from fertilizer manufacturers who have privileged access to the rock phosphate raw materials.

Comments/Estimated Impact

The US Department of Justice explicitly approved the export cartel for rock phosphate.

The effect is to reduce sales and squeeze profits on those sales made by EC fertilizer producers by forcing up input costs while charging low prices for the finished fertilizer sold in competition by US fertilizer manufacturers.

According to the 1989 report of the US Bureau of Mines, average prices for rock phosphate were the following for 1988 and 1989:

	price for US market $/mt*	price for exports $/mt*	Difference $/mt*	%
1988	18.36	25.58	7.22	39
1989	20.40	28.98	8.58	42

* - metric tonnes

According to some estimates, the additional cost for EC fertilizers producers was $26 million in 1989 (based on EC import figures from the US of 3 million tonnes in 1989). Indirect losses were higher because of lost sales by EC producers.

IV.G.2 **Molybdenum**

Description

US producers of molybdenum control access to the raw material, molybdenum salts. As a result, sales of molybdenum salts are made to European producers at much higher prices than the US producers pay. US producers of molybdenum, especially in bars used for super alloys for the aeronautical industry, thus have much lower raw material input costs than their EC competitors.

Comments/Estimated Impact

As up to 80% of the cost of molybdenum bars is accounted for by the cost of the molybdenum salts, the effect of much higher prices charged to EC molybdenum producers for these salts, effectively excludes European producers from being competitive either in the US market or in the EC.

Superalloys used in aero-engine gas turbines contain a significant amount (4%) of molybdenum. The cheaper US bar impacts negatively on the competitiveness of EC aero-engine manufacturers.

V TAX BARRIERS AFFECTING TRADE

Introduction

Much attention has been devoted in recent years to macroeconomic imbalances among the world's major trading partners. In particular, it has been pointed out that there is a relationship between the persistence of the US deficit on current account and the inability of the US legislative process to reduce the Federal budget deficit. Under these circumstances, the Community welcomes, in principle, US efforts to reduce Federal expenditure and raise Federal revenues by appropriate means. 1990 has, however, shown an unfortunate tendency to introduce revenue-enhancing measures (higher taxes, user fees, etc.) which discriminate, either de jure or de facto, against foreign citizens, companies, or products. The following sections illustrate this tendency.

V.A Automobiles

U.S. Federal law, including provisions of the Internal Revenue Code (IRC) and the United States Code (U.S.C.) impose certain taxes and penalties which function as trade barriers on imported automobiles.

While the EC does not contest the validity of the environmental and energy policy objectives of these two measures, it questions their application which discriminates against Community exports. In addition, it should be noted that the current application of these provisions does not efficiently fulfill their objectives (see in particular point A2).

V.A.1 The "Gas Guzzler" tax

Description

Since model year 1980, Section 4064 of the IRC has levied a U.S. Federal Excise Tax on any individual passenger automobile "of a model type" sold in the US whose fuel economy, as prescribed by the U.S. Environmental Protection Agency (EPA), is less than the determined standard. As of 1986, if the EPA determines that fuel economy is at least 22.5 miles per gallon (MPG) then no tax is imposed. As of 1.1.1991, the Omnibus Budget Reconciliation Act of 1990 has doubled the tax rates (beginning at $1,000 for the automobiles that do not meet the 22.5 miles per gallon standard and increases to $7,7000 for the automobile models with fuel economy ratings of less than 12.5 miles per gallon). The tax, paid by the ultimate customer of a vehicle, is collected by the manufacturer or importer for the Internal Revenue Service (IRS).

Although the gas guzzler has the appearance of a non-discriminatory domestic tax, in practice the methodology for calculating the tax benefits the U.S. domestic industry and discriminates against Community exports. The benefit to domestic manufacturers derives from the EPA definition of "model type" (MT) which is the basis for determining the applicability of the tax. The EPA regulations define MT as any vehicle with the same engine, car line, and transmission. Generally, with limited-line European manufacturers, only one vehicle constitutes a MT.

In contrast, full-line U.S. manufacturers have for years utilized a single engine, car line and transmission to market several different models. When this domestic practice is coupled with the mathematical procedure of sales weighting fuel economy calculations, it results in domestic manufacturers being able to market vehicles with equal and even lower fuel economy values than foreign-made vehicles without being subject to the gas guzzler tax.

An example of this practice is evident from a situation where a U.S. manufacturer has four vehicles that are classified as the same model type (MT). The actual fuel economy of the vehicles is 23.4; 21.8; 21.0 and 21.0 MPG. If the gas guzzler tax is intended to encourage fuel efficiency, one could expect that all but one of these vehicles should be subject to the tax. However, because the EPA regulations allow all four vehicles to be grouped as a single fuel economy class based on MT all four escape the tax. The domestic manufacturer is able to project sales of each of the four vehicles so that a single fuel economy figure above 22.5 is achieved as follows :

$$\frac{\text{10.000 total MT sales}}{\frac{\text{6000 MTI Sales}}{\text{23.4 mpg}} + \frac{\text{2000 MT2}}{21.8} + \frac{\text{1000 MT3}}{21.0} + \frac{\text{1000 MT4}}{21.0}} = 22.6 \text{ mpg}$$

The sales numbers for the foregoing examples are not actual sales figures but are relative to the actual projections used by the manufacturer. In this example the manufacturer is permitted to sell cars with EPA mileage ratings of 21.8, 21.0 and 21.0 without the imposition of the gas guzzler tax.

Importers of European cars tend for marketing reasons to offer only a limited range of vehicles using different engine sizes. This does not allow them to average the fuel consumption rates figures. The tax therefore falls disproportionately on imported vehicles.

Even though the Omnibus Reconciliation Act of 1990 has repealed the previous exemptions from payment of the tax for stretch limousines as well as the special rules permitting Treasury to set the rate of tax for small manufacturers, off-road and sport utility vehicles are still exempt from the gas guzzler tax, which weakens its credibility with respect to its declared policy objectives.

Comments/Estimated Impact

The gas guzzler tax falls almost exclusively upon imports. US manufacturers are able to average gas mileage over fuel-inefficient and fuel-efficient models within a car line and in this manner for the most part escape the tax. This is evident from the fact that although significant numbers of U.S. manufactured vehicles have fuel economy values below 22.5, the 1990 Fuel Economy Guide indicates that the gas guzzler tax was applied to only two vehicles built by U.S. car makers.

Since 1984, the cars of several European importers have been subject to this tax. This has greatly increased the burden on American customers. This results in putting United States dealers of European cars at a serious competitive disadvantage.

About $100 million will be raised by the doubling of the gas guzzler tax.

V.A.2 Corporate Average Fuel Economy Law (CAFE)

Description

From model year 1978 and on virtually all car makers marketing cars in the U.S.A. are subject to the imposition of penalties for failure to achieve a minimum fuel efficiency, based on averages of the fuel economy of their entire U.S. sales. This penalty is levied on the manufacturers/importers.

The U.S. federal law imposing such standards is 15 U.S.C. Sec. 2008 (commonly known as the Corporate Average Fuel Economy law, "CAFE"). Enacted into law in 1975 by the U.S. Congress, CAFE is intended to increase fuel efficiency and thereby reduce the U.S.A.'s dependency on foreign sources of petroleum.

Comments/Estimated Impact

Although the CAFE tax applies theoretically to virtually all car makers doing business in the U.S., in reality the only makers who have paid the penalty are the limited-line premium car makers. The CAFE regulations are biased towards both the full line manufacturers (i.e. domestic manufacturers) that make both small, fuel-efficient and larger vehicles and limited line manufacturers that produce mostly small vehicles (e.g. Japanese manufacturers). Thus, the only CAFE penalties paid thus far have been paid by European limited-line car makers.
From 1983-89, a total of US $ 118 million has been levied on EC manufacturers.
Full-line car makers, such as General Motors have been able to meet the CAFE standard by averaging the fuel economy of small, fuel-efficient cars with large cars.

The high cost of the CAFE penalties on limited-line car makers gives full-line domestic car makers a competitive advantage over imported European cars. Both the inadequacy of the system for the purposes of its declared objectives and its discriminatory nature are further demonstrated by the fact that a foreign company bought by a U.S. manufacturer would be able to avoid the CAFE penalties it had been paying in the past through use of the US manufacturer's excess CAFE credits.

In addition to its discriminatory impact, this measure unduly favors local content without any effect on the average fuel efficiency. In effect, each car maker's actual fuel efficiency is determined each model year by the EPA and is expressed by two fuel efficiency figures:

- the first figure is the car maker's actual fuel efficiency for the category of cars domestically manufactured (i.e. with a local content of more than 75% of the total value of spare parts produced in the US);

- the second figure corresponds to "imported cars" (where less than 75% of the value of the spare parts is produced in the US).

If any of these two figures is lower than the threshold, the manufacturer or importer is subject to the tax for the corresponding category.

A US manufacturer who would have to pay the fine for his own line of domestic car could escape paying this penalty by increasing the local content percentage of imported small vehicles he sells. Thus, cars previously considered as imported would now be considered as domestically produced. In this way, the average fuel efficiency of manufacturers would appear to increase, so reducing the penalty.
The practical effect of these regulations would therefore be to "force investment" in the U.S. or to "Buy American" for car parts to the detriment of Community exports.

V.B Luxury Excise Tax

Description

The Omnibus Budget Reconciliation Act of 1990 introduced as of 1 January 1991 a 10% excise tax on the portion of the retail price of the following items in excess of specified thresholds:

- automobiles above $30,000
- private boats and yachts above $100,000
- aircraft (those of which less than 80% is for business use) above $250,000
- jewellery above $10,000
- furs above $10,000

The tax is applicable only to newly manufactured items (which are not exported) and is to be collected by the retailer who will remit it to the Inland Revenue Service (IRS). Passenger vehicles, boats, and aircraft used exclusively by the federal government or a state or local government for public works purposes are exempt. The tax applies to all items subject to the tax upon their importation into the US regardless of whether the item was used outside the US prior to importation. This provision is projected to raise $1.5 billion over five years.

Comments/Estimated Impact

This excise tax may be discriminatory in that imports account for much of the market for the designated items. For example, cars and jewellery import levels respectively represent 32 and 38 percent of the US markets.

For automobiles, the case can be made that the $30,000 threshold has been set at a level so as to exempt or cause minimum pain to the domestic automobile industry, whereas it will have a large impact particularly in terms of competitivity on foreign and notably, EC automobiles. Some estimates suggest that well over half the vehicles covered by the tax will be European.
According to Automotive News - May 1989, European Community imports into the US in 1989 totalled around 360,000 cars. Around half of these sold for over $30,000. A similar number (around 170,000) of American cars were sold for over $30,000 (excluding options) but this, according to some estimates only corresponds to 12% of the total sales of US cars.

The arbitrarily-designated threshold of $30,000 may mean that imported cars will be treated less favourably than are domestic autos even though they compete in the same market. Although these taxes are not discriminatory "de jure", their impact will certainly be heavier on imports than on domestic products.

V.C Beer & Wine Excise Taxes

<u>Description</u>

Previous law: (Internal Revenue Code Subtitle E: Alcohol and certain other excise taxes)

The tax on beer was formerly $9/barrel (but $7/barrel for certain small brewers). The tax on wine, assessed according to alcohol content, was levied as follows:

Wine containing:	
not more than 14% alcohol	17 cents/wine gallon
more than 14, but not more than 21%	67 cents/wine gallon
more than 21, but not more than 24%	$2.25/wine gallon
artificially carbonated wines	$2.40/wine gallon

New law: (Omnibus Budget Reconciliation Act of October 1990)

The tax on beer is raised to $18/barrel. The tax on wine is raised to the following rates per wine gallon :

Wine containing :	
not more than 14% alcohol	$1.07
more than 14, but not more than 21%	$1.57
more than 21, but not more than 24%	$3.15
artificially carbonated wines	$3.50

The Budget Act creates a new tax credit for domestic wine producers and augments the credit provided to domestic beer producers. In the case of wineries, a producer is afforded the credit if no more than 250,000 gallons (roughly 10,000 hectolitres) of wine are produced annually, applicable to the first 100,000 gallons of production, and for breweries, if no more than 2,000,000 barrels are produced annually, applicable to the first 60,000 barrels production.

Comments/Estimated Impact

The increase in these taxes is of less significance than the fact that the law provides for a tax exemption that is solely available to qualifying "small" domestic producers and not for third country producers. In addition, the law is crafted in such a way as to ensure that a large share of the domestic industry, at least in the wine sector, will qualify for the exemption (given the definition of "small" which has even been enlarged as compared to the original White House budget agreement) and thus be afforded an unfair advantage over importers.

In terms of the GATT the tax exemption for small domestic producers, which is not granted to foreign producers constitutes a tax discrimination contrary to Art. III.2, first sentence. Since this discrimination also seems to afford protection to domestic production it might also be contrary to Art. III.2, second sentence in conjunction with Art. III.1.

VI STANDARDS, TESTING, LABELLING AND CERTIFICATION

Introduction

There is a continuing concern in the EC with regard to the standardisation process in the United States. Whereas the European Community is fully committed to the implementation of international standards as a way of ensuring open access to markets, the United States still appears to place more emphasis on purely national solutions.

According to US sources[1], as of 1989, out of 89,000 standards used in the US, only 17 are directly adopted from ISO (International Organization for Standards) standards and none from IEC (International Electrotechnical Commission) standards, even though a larger number of tenders in the US may be "technically equivalent" to international standards. Furthermore, there are indications that US enthousiasm for international standardization is limited to those sectors in which US industry has a strong export interest. The Federal Government, for its part, refers to about half of these US national standards, many of which deviate from international standards, in its mandatory technical regulations. This situation is difficult to reconcile with the GATT Standards Code. Under this GATT Agreement the US Federal government is obliged to use international standards as a basis for its own technical legislation and therefore not to promote US standards which deviate from international standards. The US Federal government is also obliged to take such reasonable measures as may be available to it to ensure that private standardizing bodies and States use international standards. None of this seems to happen in practice. Thus, a state like California - with the 8th largest economy in the world - escapes obligations of transparency (notably notification) as well as substance (activities which may have a significant effect on international trade). The US also apparently refuses to notify Congressional draft technical legislation to GATT, such as the Fasteners Quality Act, even though this is clearly required by the GATT Standards Code.
This situation represents a fundamental problem for EC companies wishing to sell in the US market. They often have to produce a separate product for the US market, thus unnecessarily incurring extra costs and reducing their competitiveness.

Problems for EC exporters are further increased by the lack of any central standardizing body covering the entire US territory, as exists in the Community and in other countries such as Canada. In the US, nearly 300 private organizations are directly engaged in standardizing activities. There is no guarantee that by following one particular standard a product will be accepted throughout the US, the more so as States and other local government bodies often have additional legal requirements of their own. A similar situation exists for testing and certification requirements.

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(1) Congress research Service, April 1989 Report on International Standardization: The Federal Role, p. 16.

If one adds to this the fact that there is no central source of information on the entire range of standards and conformity assessment procedures, and the fact that the US has a very strict product liability system, it is easy to see that exporting products to the US for which standards exist can be a major headache, especially for small and medium enterprises. This general problem may be illustrated by the following examples under sections A, B, C and D.

The fact that US and EC labelling requirements often differ substantially can create considerable additional costs for Community exporters, particularly of food products. Dialogue has begun between the US Food and Drug Administration and the Department of Agriculture, on the one hand , and the Commission services, on the other, to address these issues with a view to facilitating Transatlantic trade.

VI.A Telecommunications

Description

With regard to telecommunication services, while recognising the problems arising from the speed of innovation and of standards-setting, the EC is concerned about certain developments taking place currently in the United States and is also concerned that these developments are not transparent. For example, the ONA (Open Network Architecture) plans of the BOCs (Bell Operating Company), approved by the Federal Communications Commission (FCC) in April 1990 are not closely related to international standards-setting. The indications are that ONA is being developed independently of national and international standardisation procedures, and that this is true for ISDN equipment and service plans also, although this is partly being redressed by the promotion of more uniformity.

With regard to network equipment, owing to the fact that the telecommunications technical environment. in the US differs to a large degree from that of most other countries, the costs of adapting European-based switching equipment to US specifications are much higher than the costs for the necessary adaptation work required for other countries, thereby effectively limiting entry to the market to large companies with substantial financial resources. This is all the more apparent given that even when the Bellcore evaluation has been completed, at a cost of perhaps many millions of dollars, a company has no guarantee that its products will be bought.

As regards standards for terminal equipment, although the FCC requirements are, in principle, limited to "no harm to the network", manufacturers, in practice, have to comply with a number of voluntary standards, set by industrial organisations, such as Underwriters Laboratories (UL), in order to ensure end-to-end compatibility and safety. For example, Los Angeles and Chicago require that terminal equipment be manufactured according to UL standards and that it be tested by UL. In addition, in practice today about two thirds of products which have to comply with the "no harm to the network" requirements in Part 68 of the FCC rules also have to comply with part 15 of those rules, relating to frequency requirements.

Moreover, under the National Electrical Code manufacturers of equipment to be attached to telecommunications networks will be required to submit their products to a nationally recognised laboratory to assess conformity with appropriate standards. Most US jurisdictions will make the Code mandatory. In reality, therefore, the FCC requirements are not the only ones which imported equipment will have to meet and it is not clear which requirements will apply in a given jurisdiction.

Comments/Estimated Impact

It is difficult to quantify the cost to exporters of the necessary testing and adaptation work.

Although officially, FCC requirements are the only mandatory standards imported terminals have to meet, exporters have no certainty as to which other standards will in practice need to be complied with in order to sell their products.

The multiplicity of "voluntary" standards and the absence of a central point where information on all relevant standards can be obtained represents an effective trade barrier.

VI.B Sanitary and phytosanitary barriers

Description

These often arise from divergences in the legal sanitary and phytosanitary requirements implemented on each side of the Atlantic.

For instance, the US insists on zero residue levels for substances which have not been approved for use in the US. In some cases, time-consuming or unduly delayed approval procedures have led to trade disruption.

Thus, when in February 1990, the Food and Drug Administration found residues of a fungicide "procymidone" in a round of random sampling of imported wines, the fact that the manufacturer had not applied to the Environmental Protection Agency to have a tolerance level fixed for this product led to an effective zero tolerance level being imposed and consequent disruption of EC wine exports to the US to the tune of $200 million in 1990. This situation prevailed despite the fact that a Scientific Advisory Panel subsequently found that the health risk to consumers of wine with residues of procymidone is negligible. The recent interim resolution of the trade dispute has allowed the resumption of the bulk of normal trade flows, but, the establishment by the EPA of a permanent tolerance is likely to take some time.

In this context, also, it is possible that further trade problems may arise in the future in respect of other pesticide residues, the EBDC fungicide being a case in point should the US adopt recently proposed legislation. The proposal does not, as currently drafted, take into account different agricultural practices existing outside the US.

Table olives and pickled vegetables from certain Community Member States, despite the fact that they constitute products of natural fermentation, are considered by the FDA to be either low acid or acidified, resulting in the obligation of registration of their producers. As attested by regulations of both the International Council of Olive Oil and FAO's "Codex Alimentarius", these are natural products for which the fermentation in brine lead to a slight natural level of acidity, rendering it unnecessary for acids or other chemical preservatives to be added. The obligation for registration with the FDA of the producers of these products, constitutes an administrative barrier, which seriously hampers imports, and often result in unjustified detentions at the US ports of entry.

In addition, imports into the US of certain types of meat products have been subject to a long-standing prohibition, part but not all of which may be justified by health reasons. Following repeated approaches by the Community, US import regulations were modified to permit importation of Parma ham. However, the US still applies a prohibition on other types of uncooked meat products, for example, San Daniele ham and German ham.

In addition, the US often insists on its own controls to make sure that the US requirements are fulfilled and the USDA does not recognize the certifications provided by Community Member States that imported horticultural products are free from pests or diseases covered by the US quarantine regulations. These regulations also result in the prohibition of the import of any growing medium or water, necessary for the survival of these products.

Comments/Estimated Impact

It is often difficult to measure the impact of these obstacles (except, for example, in the case of procymidone where the trade loss has been estimated at $200 million in 1990). In general, such obstacles deprive EC exporters of markets that they previously had in the US (e.g. certain meat products from certain Member States of the Community), or they prevent the EC exporters from taking advantage of potential markets (e.g. potted plants, fruit, vegetables, hams).

VI.C Electrical Products and Components

Description

Federal, State and local jurisdictions require product testing and certification of the safety of numerous electrical products and parts thereof. On the State and local level, there are more than 2,700 State, city and municipal governments in the US that require particular safety certifications on certain products sold or installed within their jurisdictions.

Comments/Estimated Impact

These requirements are not always uniform and consistent with one another and in some cases, a national standard may not exist. In addition, the electrical code requirements are more closely monitored and more problematic (due to the use of non-US components) for suppliers of imported equipment than for US manufacturers.

These requirements translate into lost sales and further expense (in terms of time and money) related to hiring a US inspector. Expansive product liability insurance (a far less significant factor in Europe) is an additional expense borne by manufacturers on sales in the US.

One company estimated the volume of lost sales in the US due to the multiplicity of standards and certification problems to be about 15% of their total sales. The expense of certification alone was put at 5% of total sales, as was the amount spent on product liability insurance.

Federal, state and local jurisdictions should reduce the divergence in safety certifications and adopt and use national standards for electrical safety certification. Such national standards should be based on the appropriate international standards set in the International Electrotechnical Commission (IEC) or the International Standards Organisation (ISO).

VI.D Assorted Equipment

Description

Various manufacturers have raised the issue that the US requires that their products be certified by US inspectors, despite having received certification by European authorities. European products can be put at a disadvantage by the US certification procedure itself.

Comments/Estimated Impact

European manufacturers of pressure vessels indicate that the US requires its pressure vessels to be certified as meeting the relevant standard only by a company allowed to use an official US stamp. The stamps of European testing laboratories are not accepted as such by the US. The requirement to use one of the small number of US testing laboratories granted access to the stamp costs the European company time and money.

Another example is given by a producer of safes which are tested and rated by independent European authorities prior to export and then required to be retested and labelled in the US by the US Underwriter's Laboratories (UL) for burglary and fire protection characteristics in order to be accepted by US insurance companies. In addition to these procedures, these companies must replace some of their European locks with UL-approved American locks at an additional cost to the European companies in order to be acceptable to US. Similarly, scientific instruments produced by European manufacturers must be approved by UL, yet they are unlikely to receive this approval if the components are sourced outside the US. Scientific instruments whose components are sourced inside the US receive an almost automatic approval.

VII PUBLIC PROCUREMENT

Introduction

This chapter will first give a brief description of US discriminatory procurement practices and, the so-called Buy American provisions in general, and second will distinguish between those violating the GATT Code and those subject to the current negotiations for the extension of the Code.

The European Community has repeatedly expressed its deep concern not only about the continuation of and increase in Buy American provisions at federal level, but also about the legislative barriers and discriminations operated against European suppliers at State and lower levels.

The European Community has already raised several cases in the GATT context with US authorities. It has complained generally about the restrictive interpretation made by the US of Article VIII of the Code on Government Procurement (national security) and in particular about their exception list concerning Department of Defense (DoD) purchases. This interpretation has led in practice to a substantial reduction of the DoD supplies covered by the Code.

The European Community will continue through a case by case analysis of unilateral reductions of coverage imposed by the US authorities, both to discuss these matters with the US authorities in GATT through consultations and panels and to seek an improvement, in the context of the negotiations in GATT, of the existing Defense exception lists in order to clarify the scope of the Code and the use of the national security exception. Concerning other cases of non-conformity with the GATT Code (non-defense related supplies), the European Community will initiate, if necessary, new consultations or pursue matters already engaged in with the US authorities.

The Uruguay Round multilateral trade negotiations give an unequalled opportunity to ensure the elimination of US discriminatory procurement practices. In the context of these negotiations, the EC is seeking to ensure that the Code will apply equally at the level of States and regional and local entities, in the sectors of utilities and in procurement of services (including public works). It is, of course, willing to commit itself to equivalent opening of its own procurement market in this context.

VII.A Buy American Restrictions (Bars)

Description

The **Buy American Act** (BAA) of 3 March 1933[1] applies to government supply and construction contracts. It requires that:

- federal agencies procure only domestically manufactured or unmanufactured supplies for public use[2] which have been mined or produced in the US and also only manufactured goods with a substantial local content defined as 50% by the Executive Order 10582 of 1954;
- only domestic materials shall be used in the construction, alteration, and repair of public buildings and public works.

Executive Order 10582 of 17.12.1954, as amended, expanded the restriction in order to allow procuring entities:

- to set aside procurement for small business and firms in labour surplus areas;
- to reject foreign bids either for national interest reasons or national security reasons.

The Buy American Act contains four exceptions. An executive agency may procure foreign materials when:

- items are for use outside the US;
- domestic items are not available;
- procurement of domestic items is determined to be inconsistent with the public interest;
- cost of domestic items is determined to be unreasonable.

Executive Order 10582 defines "unreasonable" as a cost differential greater than 6% of the bid price including duty and all costs after the arrival in the US. The Department of Defense applies a 50% price differential (exclusive of duty and costs) or 6% (inclusive of duty), whichever is the higher.

The **Trade Agreement Act** of 1979 (implementation of the Tokyo Round) waives the BAA for certain designated countries which grant reciprocal access to US suppliers.

As regards construction, foreign materials may be procured when:

- it is impractical to purchase domestic ones;
- procurement of domestic items will uneconomically increase the cost of a project.

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(1) PL 72-428, as amended by the Buy American Act of 1988 (PL 100-418, 102 Stat 1107, Title VII, 23.8.88)

(2) Title 41, § 10 a, American materials required for public use.

Buy American restrictions are also provided for in the following legislation:

- ***National Security Act of 1947 and the Defense Production Act of 1950,*** *which granted authority to the President and the Secretary of Defense to impose restrictions on foreign supplies to preserve the domestic mobilization base and the overall preparedness posture of the US. These restrictions "justified" by "national security" are considered in chapter VII D of this Report;*

- ***Department of Defense Balance of Payments Program,*** *which provides for a 50% price correction on foreign offers when compared with US offers;*

- ***US Federal Departments Specific Annual Budget Appropriations and Authorization Acts,*** *which give a 10% to 30% price preference to US offers, notably in the following sectors :*

  - *water sector utilities*
  - *transport sector utilities*
  - *shipping of US goods and commodities*
  - *highway construction*
  - *energy utilities*
  - *telecommunication utilities*

- ***Trade Agreement Act of 1979*** *requires the President to bar procurement from countries which do not grant reciprocal access to US supplies covered by the GATT Code on Procurement.*

- ***Competition in Contracting Act of 1984 (CICA),*** *which allows the procuring agencies to restrict procurement, on a case by case basis, in order to achieve industrial mobilization objectives,*

- ***Trade Act of 1988*** *modifies both the BAA of 1933 and the Trade Act of 1979 to allow the President to bar procurement from countries which do not provide access to US products and services.*

Legislation in at least 40 States also provides for Buy American restrictions on their procurement. US statistics show that State spending represents more than 70% of total US public procurement (see section C 1 below).

Comments/Estimated Impact

Buy American restrictions, provided for by federal and State legislation, are intended to secure procurement for domestic suppliers and to maintain a US industrial strategic base. In parallel to that, the US Federal budgetary policy has been to increasingly reduce federal expenditure and revenue. These policies have led to:

- *a continuing decline in the value of federal procurement and thus to the value of the procurement covered by the GATT Code;*
- *a shift in the financial (revenue-raising and funding) and procuring responsibilities from the Federal Government to the State and local governments.*

US procurement at federal level totals approximately $200 bn. The value of US procurement covered by the GATT Code has declined from $19 bn. in 1982 to $15 bn. in 1986. It should also be borne in mind that approximately 15% of Code-covered products fall below the $150,000 threshold and are therefore not governed by the GATT code.

It is worth noting that procurement worth $180 bn. is restricted through Buy American provisions solely to US suppliers. These Buy American provisions are waived by the Free-Trade Agreements with Canada and Israel, as well as by bilateral reciprocal defense procurement and industrial cooperation agreements (M.O.U.)(1). However, as mentioned earlier, these M.O.U.s can be unilaterally modified by the US.

There are at least 40 Federal Buy American legal instruments and at least 37 States have Buy American legal instruments, and there are many more at local governmental level. Buy American restrictions are usually in the form of a Buy American preference (ranging from 6% to 50%) in favour of domestic products, i.e. products with a 50% domestic content (in some cases, the content must be as high as 65%). In some instances, the Buy American restriction is absolute.

The Department of Defense (DoD) report to Congress (July 1989) considers that many BARs "provide protection and guaranteed business to US industries without any requirement or incentives for the industry to modernize and become competitive", and therefore do not fulfil the objective of a US industrial mobilization base. Furthermore, the report states that they maintain a climate of protectionism, in the international relations of the US with its trade partners, especially when they fail to comply with the M.O.U. by allowing various Buy American restrictions to affect M.O.U. countries procurement.

It is thus clear that the potential US market for Community exports is significantly affected by these restrictions.

(1) Cooperative industrial defense agreements or reciprocal procurement agreements (M.O.U) are concluded by the US with foreign countries including certain EC countries, to promote more efficient cooperation in research, development and production of defence equipment and achieve greater rationalisation, standardisation, and interoperability. The US has concluded such M.O.U. or similar cooperation arrangements with the UK (1975), France (1978), the Federal Republic of Germany (1978), Italy (1978), the Netherlands (1978), Portugal (1978), Belgium (1979), Denmark (1980), Luxemburg (1982), Spain (1982) and Greece (1986).

VII.B *Measures contrary to GATT*

The European Community considers that the following Buy American restrictions(1) as applied to sectors, products or entities covered by the GATT Code, constitute an unacceptable violation of the Code.

VII.B.1 ***Valves and machine tools***

Description

Although the Code on Government Procurement provides that machine-tools procured by DoD are generally included, the US has taken the approach since 1981 that most of these machine-tools are excluded for national security reasons. Furthermore, in 1986, Congress decided unilaterally to exclude machine-tools from the MOUs negotiated by the Administration with third countries.

This Buy American restriction, better known as the Mattingly Amendment, first adopted by Congress in 1986 and valid until the end of Fiscal Year (FY) 1991, is applied in a discriminatory fashion, since only Canadian or US bidders are allowed to supply the 21 Federal Supply Classes (FSCs) of machine-tools for use in DoD-owned or controlled facilities.

It may be waived if adequate and timely domestic supply is not available. The declared objective is to protect the US machine-tool industry against foreign competition in order to preserve the US industrial mobilization base.

Furthermore, US Federal procurement of machine tools has been made more difficult by a change last year in the rule of origin applied (DoD Appropriation Act). The rule previously required 50% local content, but now requires that assembly should also take place in the US/Canada. To be able to sell in the US, EC companies now have to consider having their products built under licence in the US. Such forced investment is then the only avenue open to Community producers for access to this market.

Following a Section 232 petition (Trade Expansion Act of 1962) by the US National Machine Tool Builders Association (NMTBA), the International Trade Commission (ITC) decided in February 1984 that imports of certain categories of machine tools threaten US national security.

As a result, in May 1986, the US President announced his intention to negotiate a series of voluntary restraint agreements (VRA) with Japan, the Federal Republic of Germany, Taiwan and Switzerland (79% of US imports) covering 7 of the 18 product categories identified in the Section 232 report.

Japan and Taiwan agreed to restrict their exports to market share levels they had in 1985 or 1981 depending on the product category.

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(1) This list is by no means an exhaustive one.

The EC did not accept the proposal to negotiate a VRA. The US then unilaterally set target market shares for imports of machine-tools from the Federal Republic of Germany and has monitored such imports. German exporters are therefore under the threat of a unilaterally introduced import ban on their products should the target be exceeded.

The US administration has also warned other non-VRA countries, including the United Kingdom, Spain and Italy not to allow their exporters to fill the gap created by the VRAs.

Comments/Estimated Impact

According to the US (the Defence Economic Impact Modelling System of 1985), the DoD procurement of machine-tools is estimated at $ 1 bn.

VII.B.2 Goods or equipment used by the Voice of America

Description

On 22 December 1987 the President signed the bill authorizing appropriation for, inter alia, the Voice of America (PL 100-204). The law includes a Buy American section (Section 403). The section will allow for a 10 % price preference in favour of US bidders unless :

- *the foreign bidder can establish that the US goods and services content (excluding consulting and management fees) of his proposal will not be less than 55 % of both the value of such a proposal and the resulting total contract (this clause also applies to domestic bidders) ;*
- *a Buy American preference is precluded by the terms of an international agreement with the host foreign country;*
- *the host foreign country offers US contractors the opportunity to bid on a competitive and non-discriminatory basis in its own radio and television sector;*
- *the Secretary of Commerce certifies that the foreign bidder is not receiving any direct subsidy from any government, the effect of which would be to disadvantage a US bidder on the project.*

The "overriding national security interest" is invoked to justify the preference for US contractors, as well as a domestic component requirement of 55%; in any case, a 10% price preference is also imposed. Voice of America procurement concerns transmitters, antennas, spare parts and other technical equipment (Title IV of Public Law 100-204, Section 403(a)).

Furthermore, Section 403(d) (A)-(F) provides for mandatory countervailing pricing of foreign bids, when the bidder has received subsidies (proportionate to the amount of the subsidy).

Comments/Estimated Impact

This restriction is set each year by the US Information Agency Appropriations and Authorizations Acts.

The value of Voice of America procurement as foreseen by the Foreign Relations Appropriation Act is $1.3 bn. per annum for the period 1988-91.

VII.B.3 ***Synthetic fibres (DoD Appropriation and Authorization Act):***

Description

This restriction is derived, according to DoD, from the so-called "Berry Amendment". DoD claims that it prohibits the use of synthetic fibres from a foreign source as long as they are available domestically. It is therefore not possible for products containing European (or other foreign made fibres) to be supplied to DoD.

Comments/Estimated Impact

Annual Procurement value of clothing is estimated by the DoD at $ 200 m.

The EC rejects the US argument that the articles covered by the Berry Amendment are ipso facto covered by the general exemption applied for reasons of national security.

VII.B.4 ***Automotive forging items***

Description

This restriction covers automotive propulsion shafts, as well as other forging items.

It is not applied to Canadian supplies.

Comments/Estimated Impact

Given that total DoD procurement of these items accounts for 5 % of the US forging consumption and less than 10 % of all DoD procurement for forging items, it is clear that defence mobilization would exist irrespective of DoD purchases. Hence it is difficult to see how national security can be used as a justification for these restrictions.

The DoD report to Congress itself (July 1989), states that this restriction on forging items in general does not need to be continued, because the US industry has become more competitive. Bilateral agreements with its military allies required that these items be covered in order to maintain an industrial base on both sides of the Atlantic.

The US is clearly in violation of the Code, since these items are covered by the Code and the restriction is discriminatory.

VII.B.5 Hand and measuring tools

Description

This restriction is based on the Berry Amendment and concerns the products listed in Federal Supply Classes (FSCs) 51 and 52. Implementing legislation, as enacted on 9 July 1987, gives a 75% price preference to US made tools.

Comments/Estimated Impact

The procurement value of this restriction is about 1 % of the total of procurement of the DoD. The EC considers that this restriction contradicts the US GATT Code obligation under which these items are listed as eligible if procured from the Contracting Parties to the Code. A similar view is taken by the DoD report to Congress.

VII.B.6 Antifriction bearings

Description

This restriction, justified for "national security" reasons is imposed on all types of bearings. The DoD rule will be applicable until October 1991 with the possibility to extend the restriction for another 2 years. However it is not applied to Canadian supplies.

Comments/Estimated Impact

US DoD Procurement of ball bearings amounted in 1988 to $800 m. according to the Department of Commerce Bureau of Census, which corresponds to 20 % of total US apparent consumption of ball bearings.

When this restriction was introduced, the EC expressed its doubts about the national security justification of a Buy America restriction on all ball-bearings. Since that time, evidence from US sources seems only to reinforce these doubts.

The International trade Administration (ITA) found in its Section 232 study of the effects of imports of anti-friction bearings on national security (July 1988) that national security was not threatened by imports in eight categories of bearings. Only two of the fifteen categories reviewed experience shortfalls attributable to substantial import penetration: viz. regular precision ball-bearings under 30 mm, and between 30/100 mm.

The DoD report to Congress on the "Impact of BAR affecting defense procurement" (July 1989) concluded that the "protection provided by DoD to the domestic industry has had some negative impact", affecting US relations with its military partners and increasing US capacity utilization rates leading to longer times for supply.

Furthermore, indication of the recovery of the US domestic production is to be found in the US Bureau of Census's Report on the US Industrial Outlook 1991 as well as its specific reports on antifriction bearings which have confirmed the opinion of the EC that the US ball-bearing industry has regained full competitivity and is now even in a position to compete abroad on export markets. Under these circumstances, there can be no justification for the continuation of the current Buy America restriction on ball-bearings on the grounds of a threat to the US industrial strategic base.

VII.C *Measures in areas covered by the GATT Code negotiations*

The European Community considers that the following US procurement restrictions[1] *should be eliminated through the current negotiation of the extension of the GATT procurement Code. These restrictions are implemented at State level, or in the so-called "excluded sectors", or in the procurement of services.*

VII.C.1 ***State procurement restrictions***

Description

The following US States impose Buy American requirements on their procurement:

Alabama:

Alabama legislation requires the use of US materials "if available at reasonable prices" for public works that are financed entirely by the State. It prohibits the purchase of foreign steel for highway and bridge construction.

California:

California legislation provides for total domestic supply. However, as regards public works, a price preference of 10% is used for products and services (Buy Californian Act of 1980).

Colorado:

Colorado legislation provides that only US produced or manufactured products are procured for highway projects.

Georgia:

Georgia legislation requires that only Georgia-made or US made products at equal quality and price are to be procured.

Hawaii:

Hawaii legislation requires that preference should be given to Hawaiian and other American products.

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1 This list is by no means an exhaustive one.

Idaho:

Calls for tender carry a clause restricting use of foreign items.

Illinois:

Illinois Domestic Procurement Act gives a price preference of 15% to US items. The Department of Transport (DoT) prohibits the procurement of foreign steel in highway and bridge construction.

Indiana:

Indiana legislation provides for a 15% price preference for domestic steel in all state and local public works, which may be increased to 25% in labour surplus areas, at the discretion of district officers of the Highway Commission. Calls for tender carry a clause restricting the use of foreign items.

Iowa:

The State Highway Commission prohibits foreign-made structural steel to be used in bridge construction.

Kentucky:

Under Kentucky statutes foreign supply is prohibited.

Louisiana:

The Department of Highways procures only US supplies of steel products.

Maine:

The Bureau of Purchases reserves its right to reject bids involving foreign products competing with US ones. Furthermore, bidders must disclose intent to use foreign items.

Maryland:

The State Highway Administration specifies in the call for tenders "domestic, not foreign, steel and cement". A 20% price preference for domestic steel in state and public works (up to 30% in labour surplus areas) is applied to contracts of at least 10,000 pounds of steel products.

Massachusetts:

Massachusetts legislation grants preference to in-state products first, and then to US products. The Department of Public Works stipulates that "structural steel regardless of its source shall be fabricated in the US".

Minnesota:

Minnesota legislation allows for specifications in calls for tenders to be determined in order to use only US items.

Mississippi:

The State Highway Department specifications for calls for tenders provides that "only domestic steel and wire products" may be used in road and bridge construction.

Montana:

Montana legislation gives preference to in-state and American products.

New Hampshire:

The Department of Public Works specifies in their calls for tenders that "all structural steel shall be restricted to that which has been rolled in the US".

New Jersey:

New Jersey legislation requires US domestic materials such as cement, to be used on public works projects.

New York:

New York legislation provides for a restriction on procurement of structural steel, or steel items for contracts above $ 100,000 unless domestic supplies are not available within a reasonable time or are not of a satisfactory quality. Calls for tenders carry a provision restricting the supply to domestic items, through terms of reference or specifications.

New York City imposes value-added conditions on procurement, such as the location of the manufacturing plant in its jurisdiction or employment of the local workforce.

North Carolina:

Contracting officers impose ad hoc restrictions on foreign supplies.

North Dakota:

Calls for tenders carry the provision "bid domestically produced material only".

Oklahoma:

Oklahoma legislation requires the purchase of domestic items unless foreign ones are cheaper or superior in quality at equal prices. This is also applied to steel products.

Pennsylvania:

Pennsylvania legislation prohibits procurement of foreign steel, cast iron and aluminium products made in countries that discriminate against US products and a restriction to solely US steel is applied to public works (State and local). Suppliers must prove compliance by providing bills of lading, invoices and mill certification that the steel was melted, poured and manufactured in the US.

Rhode Island:

Rhode Island legislation gives preference to US suppliers.

South Dakota:

Specifications in calls for tenders are designed to procure US items.

Virginia:

Virginia legislation stipulates that contracts of $50,000 or above must specify US steel products and give a price preference of 10% (including duties) to suppliers of US steel.

West Virginia:

West Virginia Law provides that contracts must specify US steel, aluminium, glass to be used in public works projects, and give 20% price preference for domestic steel, aluminium and glass in state and local public works (up to 30% in labour surplus areas).

Wisconsin:

Wisconsin legislation requires the procurement of US items.

District of Columbia:

The Federal Buy American Act applies in DC.

States with 5% price preference for in-state suppliers:

- *Alaska*
- *Arizona*
- *Arkansas*
- *New Mexico*
- *Wyoming*
- *Nebraska*
- *Kansas*

Comments/Estimated Impact

State and local government procurement represents 70% of the total US procurement. Federal funding to the States and local government represents 16% of the annual expenditures of States and local government, and such federal funding is usually conditioned by the respect of the BAR mandated by Congress (refund of federal money is the sanction in the procurement of foreign products/services by States or local government).

VII.C.2 Set-aside for small business

Description

Special legal provisions restricting procurement to U.S. small and disadvantaged business exist in relation to federal procurement.

The most important of these is Public Law 95-507 (October 1978), which made major revisions to the Small Business Act of 1958. This sets out the obligations of federal agencies regarding contracting with small and disadvantaged businesses in the field of public procurement of supplies, services and works. The Small Business Administration has established industry size standards on an industry-by-industry basis, based on the number of employees (varying from 500 to 1,500), or annual receipts which are considered to be the maximum allowed for a concern, including affiliates.

Federal agencies are required to award contracts to certain small businesses in accordance with different rules. An important example is the minority business set-asides which are operated by the General Services Agency (GSA). The purpose of these set-asides is to award certain contracts exclusively to small business. There are three classes of set-aside :

- *small purchase set-asides ("reserved procurements") which are limited to acquisitions of supplies or services that have an anticipated dollar value of $25,000 or less. These set-asides are authorized unilaterally by the contracting officer;*

- *total set-asides, where the entire amount of an individual acquisition or class of acquisitions, including construction and maintenance is set-aside for exclusive small business participation;*

- *partial set-asides, where the acquisition is split between a "set-aside portion" and a "non set-aside portion" (not applicable to construction contracts).*

The GSA also operates a number of Business Service Centres which may challenge a decision of a contracting officer who does not set aside a contract for small business.

At State and local level, legally established preferences for small business exist in 18 States but practices having similar effects are found in a larger number of States. A small business preference can take at least three forms :

- *an outright percentage preference which can be a fixed or varying amount up to a ceiling;*
- *a pure "set-aside" programme;*
- *a quota system whereby a percentage of total awards shall be made to small businesses.*

Futhermore, Fèderal regulations must be applied where projects undertaken at State and local level are financed by Federal grants.

Comments/Estimated Impact

The GATT Code contains a US reservation indicating that it does not apply to small and minority businesses set asides. However, according to figures of the Federal Procurement Data Centre, small and disadvantaged businesses are currently obtaining between 25 and 30 percent of total Federal procurement (these percentages include direct contracts and subcontracting).

VII.C.3 Restrictions in the sectors of utilities and public works

Descrition

The following legislation contains provisions, which give a preference to US suppliers.

- ***Pollution control equipment used in projects funded by the Federal Water Pollution Control Act and Section 39 of the Clean Water Act of 1977***

  Under the Waste Water Treatment Construction Program, the Environment Protecting Agency (EPA) provides funds to local units of government for up to 75% of the cost of the projects. The Federal Water Pollution Control Act, as amended by Section 39 of the Clean Water Act, provides for a 6% price preference for US suppliers.

- ***Steel, construction and transport equipment (Surface Transportation Assistance Act of 1978 as amended by the STAA of 1982 and Section 337 of the Surface Transportation and Uniform Relocation Assistance Act of 1987)***

  Section 401 of the Surface Transportation Assistance Act of 6 November 1978 (STAA) is managed by the Urban Mass Transportation Administration and binds the recipients of federal funds (federal, State or local government).

US States must meet the following requirements to receive federal funds from the Urban Mass Transit Administration:

- *the State must certify that its laws, regulations and directives are adequate to accomplish the objectives of Section 165 of STAA;*
- *standard specifications in contracts must favour US supplies;*
- *steel and cement must have been manufactured in the US.*

Violations of Section 165 by the States are sanctioned by the refund of the amount of federal appropriations used in the violating contracts (Federal Claims Collection Act of 1986 (31 USC 3711).

The above legislation is applied to mass transit equipment (rolling stock and other) and it requires that for all contracts, the local transit authorities give a 25% preference to bidders, supplying only US-made or assembled equipment with a substantial local content of 55% for contracts entered into on or after 1 October 1989 and of 60% for contracts entered into on or after 1 October 1991.

Furthermore, the domestic content requirement has also been extended to subcomponents (1987). Waivers for products or subcomponents may be granted by the Urban Mass Transportation Administration, when the use of domestic suppliers will prove non-economical and will result in unreasonable costs.

The Buy American preference has been tightened over the years. In 1978, the preference was 6% for US products and the US content requirement (for the purpose of determining the applicability of Buy America) was 50%. In 1982, the preference was raised to 10 % for rolling stock and 25% for other equipment. In 1987, the preference was raised to 25% for all equipment and the definition of a US product was changed from 50% US content to 55% for contracts concluded after 1 October 1989 and 60% for those entered into after 1 October 1991, and its application extended to subcomponents. In addition, final assembly of the vehicles must be carried out in the US.

Buy American provisions also apply to federally assisted programmes and contracts awarded by the Federal Highway Administration (23 CFR, 635-410), which do, however, allow for minimal procurement of foreign steel and cement (when foreign items value is under 0.01% of the total cost of a contract or $2,500).

Comments/Estimated Impact

The above rules effectively exclude foreign bidders from a sizeable market.

Annually, the federal budget provides $2 to 3 billion in capital construction funds through the Urban Mass Transit Administration of the Department of Commerce (UMTA-DoC).

- ***Extra high voltage equipment***

  The Energy and Water Development Appropriations Act of 1990 (PL 101-101) provides for a 30% price preference on extra high voltage equipment (EHVE) with a country exemption if the foreign country has completed negotiations with the US to extend the Government Procurement Code, or bilateral equivalent to EHVE, or which otherwise offers fair competitive opportunities to US suppliers in that country.

- ***Steel and transport equipment by the Amtrak Improvement Act of 1978, amending the Rail Passenger Service Act as amended by the Amtrak Reorganization Act of 1979***

  The legislation provides that steel products, rolling stock and power train equipment be purchased from US suppliers, unless US made items cannot be purchased and delivered in the US within a reasonable time.

Comments/Estimated Impact

Procurement by US utilities is estimated by USTR (US offer in GATT Code negotiations) to $493 bn. (this amount is a rough estimate since contracting procedures by State agencies vary from one State to another).

VII.C.4 Restrictions on the procurement of consulting services

Description

Federal contracts for consulting services (e.g. for US IDA and the DoD) require US citizenship or 51% US ownership. Certified US permanent residency is not sufficient for a consultant to compete for Federal contracts.

Comments/Estimated Impact

It seems evident that restrictions of this type completely exclude Community suppliers of these services from competing in these markets.

VII.C.5 Telecommunications Procurement

Description

Telecommunications equipment is at present excluded from the GATT Procurement Code - apart from the inclusion of NTT of Japan - but examination of a possible extension to this sector is currently taking place.

Any assessment of the level of Community access to the US network equipment market is difficult, because of a variety of factors, such as the insufficient transparency in Regional Bell Operating Companies (RBOC) and AT&T procurement procedures, the special rights and/or dominant position enjoyed by these utilities, the existence on this market of strong manufacturers who are also carriers, the influence of the Federal Communication Commission (FCC) and of State Public Utility Commissions (PUCs) on the procurement practices of these utilities, and the effect of a US standardisation policy which is not closely linked to international standards.

With regard to the long distance carriers, AT&T (the dominant long-distance carrier) and GTE (a provider of local services) also manufacture equipment, and therefore have little incentive to buy competitively. These companies are far better placed than outside companies to supply their own networks, and in practice they buy most of their equipment from themselves. AT&T in particular, with a 65% share of the switching market and a 75% share of the long distance services market, dominates both the equipment and services markets, and so benefits from a set of advantages. These include the company's large installed base; the fact that network specifications are based on the requirements of the AT&T telecommunications network; and the influence that the company has on the standardisation process in the US. At the same time, however, its procurement procedures are not transparent.

With regard to the RBOCs, the Community is aware that these companies are obliged to ensure that their procurement procedures are nondiscriminatory. However, these procedures fall short of those set out in the EC directive on procurement. Notably, the procurement process followed by RBOCs is not very transparent - intimate knowledge of their organisation and preferences is necessary. The process inherently favours those suppliers which are most familiar with the RBOCs.

A 6% Buy America preference applies to DoD procurement (unless waived under the Memoranda of Understanding with NATO allies) and to procurement of Rural Telephone Cooperatives financed by the Rural Electric Administration (USDA).

In addition, as noted in the chapter VI on standards, testing, labelling and certification, the expense of testing certain network equipment through Bellcore can be very high in some cases, so that although the system is open to all in theory, in practice it is open only to those suppliers with the ability to make this investment.

Since the RBOCs account for 80% of local traffic in the United States, and enjoy monopolies on provision of basic services in their areas of operation, they are subject to regulation in a number of different ways. The FCC must authorise the construction of new lines (S.214 of the 1934 Communications Act). They also regulate interstate tariffs through price caps. Intrastate communications are regulated by the local State Public Utility Commissions (PUCs) whose administration of price-setting involves them in all aspects of RBOCs' operations - indeed, it is estimated that as much as 70% of BOC revenue is regulated by PUCs rather than by the FCC. This means that irrespective of ownership, public or private, the major telephone companies in the US are subject to a major degree of federal and local government control. Companies are therefore not free to act on the basis of purely commercial criteria, and there is concern that this applies to their procurement also.

Draft legislation tabled in Congress in 1990 and 1991 would explicitly impose local content requirements on BOC procurement and is being closely monitored.

Comments/Estimated Impact

The Commission's services are at present examining how best to estimate the commercial impact of these impediments.

VII.D Abuse of national security provisions

Description

"National security" was initially used in the 1941 Defense Appropriation Act to restrict procurement by the DoD to US sourcing. It is remembered as the Berry Amendment which has been used as a model to restrict procurement to new types of products. This reads as follows:

"SEC. 721A. No part of any appropriation contained in this Act, except for small purchases in amounts not exceeding $10,000 shall be available for the procurement of any article of food, clothing, cotton, woven silk or woven silk bends, spun silk yarn for cartridge cloth, synthetic fabric or coated synthetic fabric, or wool (whether in the form of fiber or yarn or contained in fabrics, materials, or manufactured articles), or specialty metals including stainless steel flatware, or hand or measuring tools, not grown, reprocessed, reused, or produced in the United States or its possessions, except to the extent that the Secretary of the Department concerned shall determine that satisfactory quality and sufficient quantity of any articles of food or clothing or any form of cotton, woven silk and woven silk blends, spun silk yarn for cartridge cloth, synthetic fabric or coated synthetic fabric, wool or metals including stainless-steel flatware, grown, reprocessed, reused, or produced in the United States or its possessions cannot be procured as and when needed at United States market prices and except procurements outside the United States in support of combat operations, procurements by vessels in foreign waters, and emergency procurements or procurements of perishable foods by establishments located outside the United States for the personnel attached thereto ..."(1)

(1) Department of Defense Appropriations Act, 1984, P.L. 98-212, § 721A, 97 Stat. 1442, Dec. 8, 1983.

The Berry Amendment allows for some exceptions when:

- *the purchase does not exceed $25,000;*
- *satisfactory quality and sufficient quantity cannot be provided when needed at US market prices;*
- *procurements are outside the US in support of combat operations, or by vessels in foreign waters, or are emergency procurements or procurements of perishables outside the US;*
- *specialty metals or chemical warfare protective clothing are procured outside the US to comply with agreements with foreign governments either requiring the US to make purchases to offset sales, or in which both governments agree to remove barriers to purchases of supplies from each other.*

The National Security Act of 1947 and the Defense Production Act of 1950 *grant authority to the President and the Secretary of Defense to impose restrictions on foreign supplies to preserve the industrial mobilization base and the overall preparedness of the US.*

Congress can also adopt additional Buy America restrictions citing national security interests. Each year, the Department of Defense Appropriations Act sets the Buy American requirements for DoD, but such restrictions may also be attached to other non-related legislation (e.g. the 1990 restriction on procurement of naval circuit breakers was introduced in the Dire Emergencies Supplemental Appropriations Act).

The following procurement restrictions were adopted on "national security" grounds. This is not an exhaustive listing.

- ***Coal and coke for use by the American forces in Europe***
  This restriction is intended to protect the market of US anthracite producers and shippers. It may not be applied if no US supplies are available. There is no exemption for procurement for US installations abroad from local European suppliers.

- ***Supercomputers for the US Army***
  Since 1987 only US supercomputers are to be bought by DoD. The justification given for this restriction is the need to develop US capability in this area for national security purposes. It may be waived if the Secretary of Defense certifies to Congress that foreign supply is necessary to acquire capability, for national security reasons, which cannot be met by domestic sources.

- ***PAN carbon-fibres***
  This restriction, set up by an Appropriation Act of 1987, effectively means that 100% of DoD purchases of polyacrylonitrile carbon fibre should be supplied by US sources by 1992. The objective is to establish and maintain a US industry in advanced composite materials. No waiver or exemptions are provided.

- ***Miniature and instruments (9-30 mm) ball bearings***
  This restriction was designed to protect the only three US firms involved in manufacturing these special bearings against imports from Japan and Singapore, which have achieved an import penetration of 70% of the US apparent consumption.

- ***Naval vessels and coastguard vessels***
  The "Burnes-Tollifson" amendment of 1964 (Section 7309, title 10 USC) requires that US naval vessels and coastguard vessels be built in US shipyards. This restriction is extended to cover small inflatable boats or rafts.

- ***High-carbon ferrochrome***
  This restriction is part of the Stockpile Conversion Program and was the result of a Section 232 study which concluded that the five US firms which produce these chromites were threatened by imports.

- ***Selected forging items***
  This restriction covers anchor chains, propulsion shafts, periscope tubes, rings, cannons, mortars, small calibre weapons, turrets, gears, crankshafts, etc. DoD procurement for these items accounts for 5% of the US forging items consumption.

- ***Speciality metals***
  This restriction is based on the Berry Amendment and it limits procurement exclusively to US suppliers for the following metals: alloyed steel, alloyed metals, titanium and its alloys, zirconium and its alloys. However, it is waived for suppliers from countries which have a bilateral cooperative agreement with the US.

- ***Supply of anchor and mooring chains***
  Since 1987, this restriction applies to all kinds of chains under 4 inches in diameter. It may be waived if US firms cannot supply Dod requirements in a timely fashion.

  In addition, the following items, which are listed for easier reference, have already been described under section VII B:

  - *Valves and machine tools*
  - *Fibres*
  - *Equipment used by the Voice of America*
  - *Hand and measuring tools*
  - *Automotive forging items*
  - *Antifriction bearings*
  - *Telecommunications*

Comments/Estimated Impact

National security may be invoked, under Article VIII of the GATT Procurement Code, to deny national treatment to foreign suppliers.

However, the use of the "national security" justification by the US has led in practice to a substantial reduction of the DoD supplies covered by the GATT Public Procurement Code.

The DoD report to Congress (July 1989) considers that many of the procurement restrictions justified on so called national security grounds "provide protection and guaranteed business to US industries without any requirement or incentives for the industry to modernize and become competitive", and therefore do not even fulfill the domestic objective of an essential US industrial base.

The DoD concludes in its report that in many cases, restrictions should be terminated and Congress should instead support Domestic Action Plan or National Stockpiling Programs. The main arguments against procurement restrictions are, according to the DoD:

- *they increase by 30 to 50% the price of DoD requirements;*
- *they are a disincentive for investment and innovation;*
- *they are costly in terms of paperwork and management;*
- *they have produced increased leadtimes for supply by domestic industries;*
- *they maintain a climate of protectionism;*
- *they create an atmosphere of animosity with allies, particularly when they violate the spirit of the M.O.U.'s.*

The Community would not disagree.

VIII BARRIERS IN THE FINANCIAL SERVICES SECTOR

Community financial institutions generally benefit from national treatment in the US; there are, however, certain aspects in which federal or State laws discriminate against non-US financial institutions. There are also restrictions to the expansion of activities which, while affecting in the same way EC and US financial institutions, may adversely affect the ability of EC financial institutions to compete.

VIII.A Restrictions on geographical expansion(*)

Description

Bank holding companies (either incorporated in or outside the US) are prohibited from establishing or acquiring control of a bank outside their "home State", unless the host State expressly permits (section 5 of the International Banking Act and section 3(d) of the Bank Holding Company Act of 1956). However, a majority of States have now enacted laws allowing out-of-state banks to set up subsidiaries in their territory, although there are still some States which do not permit or impose restrictions on the establishment or takeover by bank holding companies which are not of the same State.

A foreign bank or its subsidiary not incorporated in the US cannot open branches in more than one State (section 5(a) of the International Banking Act) (foreign banks with branches in several States before 27 July 1978 were grandfathered - section 5(B) of IBA); domestic banks are similarly restricted by the McFadden Act.

As regards insurance, the fact that the competence to regulate and supervise insurance activities is left to the States (McCarran-Ferguson Act) has implied that there is a requirement to obtain a separate license to operate in each State.

VIII.B Restrictions to the provision of securities and investment services(*)

Description

Bank subsidiaries incorporated in the US of a non-US bank may not own a securities firm (section 20 of Glass Steagall Act, volume 12 of US Code §377), although in January 1990 some of them have been authorised to own subsidiaries which may engage to a limited extent in underwriting and dealing in corporate debt and equity securities on the same basis as US owned bank holding companies. Similarly, non-US banks with a bank subsidiary in the US may not own a securities firm (section 4(a)(1) of the Bank Holding Company Act); US branches of non-US banks are subject to the same restrictions to engage in securities activities (section 8(a) of International Banking Act). However, banks have been authorised by the Federal Reserve Board to enter a number of securities-related activities.

(*) US banks and insurance companies may also be affected by these provisions

Under section 7 (d) of the Investment Company Act of 1940, a foreign investment company may not sell its securities in the US unless the US Securities and Exchange Commission (SEC) finds that investors would have the same protection as investors in domestic investment companies. Because the SEC recognizes that this standard is hard for foreign companies to meet, it has suggested that foreign money managers organize an investment company in the US that invests in the same type of securities as the foreign investment company and register the "mirror" fund to sell its shares in the US. Foreign money managers are reluctant to incur the additional costs necessary to do this.

With certain exceptions, non-resident firms can only provide investment services, including provision of investment research to non-institutional investors, to US residents through a registered broker-dealer. However, as regards dealing in futures and options, CFTC Part 30 Exemption Order permits the exemption for foreign firms from US registration and regulation to provide services to US residents. While it is appreciated that there are benefits under this exemption, business done for US residents in non-US contracts on a non-US exchange by non-US firms is nevertheless subject to a number of burdensome and extraterritorial regulations, such as:

- *firms need to segregate all US customer money;*
- *firms must acquiesce to US customer rights to refer for arbitration in the US;*
- *foreign firms must provide CFTC with a list of all their US affiliates carrying on related business and procure a consent from those affiliates that CFTC may have access to their books (such requirement is not imposed on local dealers).*

Certain of these requirements may be imposed even in cases of unsolicited business carried out at the initiative of the investor.

Access by US residents to non-US markets may be otherwise hampered by the extraterritorial application of US regulations determining in certain instances, in the case of business carried out in a non-US exchange or market by a US resident, the terms of contracts, the acceptance by the foreign firm of the US jurisdiction, or otherwise imposing US regulation and jurisdiction on non-US exchanges or markets in which US residents participate.

VIII.C Other restrictions operating at the Federal level

Description

Under Federal law, directors of EC banks' subsidiaries incorporated in the US must be US citizens, although under approval of the Comptroller of the Currency up to half of the number of directors may be foreign (cfr. 12 US CODE N° §72).

Taking into consideration concerns expressed in the 1990 Trade Barriers Report and by the international financial community, the Federal Reserve Board raised the uncollateralized Fedwire daylight overdraft ceiling for foreign banks last year. This change represents a positive step, but further progress is needed so that foreign banks no longer have lower uncollateralized overdraft possibilities than US banks.

Federal savings and loan associations are restricted in their ability to make investments in certificates of deposit issued by uninsured offices of foreign banks (section 5(c) of the Home Owners' Loan Act of 1933), or generally to invest in certificates of deposits and other time deposits offered by foreign banks (section 5(c)(1)(M) of the Home Owners' Loan Act of 1933 and section 5 A(b)(1)(B) of Federal Home Loan Bank Act) (most US branches of non-US banks do not engage in retail deposit activities in the US and are not required to obtain FDIC insurance).

VIII.D *Other restrictions operating at the State level*

Description

- ***Banking:***

Banking regulation at the State level is traditionnally important because of the existence of the dual banking system in the US, in which responsibilities are shared or divided between federal and State authorities.

State activities have also become particularly significant because deregulation has often appeared first at the State level before being adopted at the national level. In the 1970's , deregulation of interest rates occurred initially at the State level before being adopted by Congress. Similarly, in recent years many States are attempting to avoid federal interstate banking restrictions or limits on lines of business through changes in State law.

As activity at the State level has become increasingly important, there is concern that many States may have adopted or are introducing measures which discriminate against EC banks :

- *a number of States prohibit foreign banks from establishing branches within their borders, do not allow them to take deposits, or impose on them special deposit requirements;*
- *some States have citizenship requirements for bank incorporators or directors;*
- *certain States still exclude the issuance of stand-by letters of credit for insurance companies for reinsurance purposes by branches and agencies from foreign banks;*
- *certain States exclude from the possibility to expand to other States of a "regional compact" banks established in the "regional compact" whose parent bank is a non-US owned bank, or limit the benefits of such expansion only to bank holding companies which hold a large proportion of their total deposits within the region;*
- *in many States branches and agencies of non-US banks are forced to satisfy burdensome registration requirements to engage in broker-dealer activities, with which US banks need not comply.*
- *several States restrict the ability of branches and agencies of non-US banks to serve as depositories for public funds.*

- *Insurance:*

  Certain States do not allow the operation and establishment of insurers owned or controlled in whole or part by a foreign government or State.

  Certain States impose special capital and deposit requirements for non-US insurers or other specific requirements for the authorisation of non-US insurers. However, some of these requirements are also imposed on out-of-State US insurance companies.

  Some States issue for non-US insurers only renewable licenses limited in time or for shorter periods.

  The Internal Revenue Code of 1986 establishes a special 4% excise tax on casualty insurance or indemnity bonds issued by insurers and a special 1% excise tax on life insurance, sickness and accident policies and annuity contracts issued by foreign insurers; it also establishes a special 1% excise tax on premiums paid for certain reinsurance contracts.

VIII.E Other restrictions

Description

Certain States impose reciprocity requirements for the establishment of branches or agencies of non-US banks, and most States impose similar reciprocity requirements for the establishment of branches of non-US insurance companies(*).

At the Federal level, the Primary Dealers Act (section 3502 (b)(1) of the 1988 Omnibus Trade Act) imposes the prohibition to become or to continue to act as primary dealers of US government bonds on firms from countries which do not satisfy reciprocity requirements, if they have not been authorised before 31 July 1987 (with the exemption of Canadian and Israeli firms).

Non-US banks operating in the US have to calculate their allowable interest expense deduction in a form which disadvantages them, are subject to a 30% "branch profits tax" similar to a withholding tax regardless of whether those earnings have been transmitted outside the US, and are subject to a tax dependent on the amount of the bank's interest expense deduction ("excess interest tax") even if the bank has no taxable income; furthermore, in the application of this tax non-US banks are disadvantaged in the use of certain tax exemptions.

In many instances, the most commonly available visa to executives or managers of non-US banks is temporary (maximum 5-6 years) and renewable only after the employee has left the US for one year.

(*) US banks and insurance companies from other States may also be affected by these provisions.

<u>Comments/Estimated impact of the restrictions in the financial services sector</u>

The separation between banking and securities activities is likely to constitute, in an increasingly globalised international market, a significant competitive disadvantage for EC banks, which cannot compete in the US for certain businesses while US banks can engage in securities activities in most Member States of the Community. However, the US have respected the ability of some EC banks' securities subsidiaries in the US to continue their existing securities operations in the US, and foreign banks now have an opportunity to underwrite and deal, to a limited extent and through a separate subsidiary, in corporate debt and equity on the same basis as that recently granted to US bank holding companies; this ability is however subject to certain conditions (the so-called "firewalls" between the non-US parent bank and its affiliates and its US securities subsidiary) which in some instances encroach upon the authority of the home country bank supervisors. The restrictions on inter-State activities are also a significant obstacle for the conduct of business within the US.

The application of internal US specialisation requirements beyond US borders could also have a substantial and unwelcome impact on the structure of European financial groups, although the Commission acknowledges the flexibility shown by the Federal Reserve Board to limit to the extent possible under current US law these extraterritorial effects. Community banks having a bank subsidiary in the US may become affiliated within the Community with a Community insurance company having an insurance subsidiary in the US, or with a Community securities firm having a subsidiary in the US, or there may also be cases where a Community bank having a branch or subsidiary in a State of the US merges with another Community bank having a branch or subsidiary in the US in a different State. In those cases, it may be necessary either to divest existing bank, securities or insurance operations in the US, or in any case to restrict drastically existing US operations in the securities field.

The United States Government has tabled a proposal for a significant regulatory reform of the US financial services sector. The Commission welcomes the general thrust of these proposals, as they could remove certain obstacles stemming from regulations imposing restrictions to the geographical expansion of banks or to the activities which may be carried out by banking organizations, and hopes for their early adoption. The Commission also expects that these reforms will benefit both US and non-US banks, bank holding companies and other financial firms alike, will respect the present degree of market opportunities which EC financial institutions already enjoy in the US market, and will not result in additional burdens for EC financial firms operating in the US.

The Commission stresses the need for any reform eventually adopted to end the adverse effects on non-US based banking organizations of the present application beyond United States' borders of United States' specialization requirements, geographical restrictions or other operating conditions, such as certain "firewalls" between the US securities operations and the non-US affiliates of the same financial group.

The restrictions and discriminations existing at the State level have a smaller adverse impact on the competitive opportunities available to EC financial institutions, but are nevertheless obstacles to effective market access.

The United States has traditionally carried out a policy of national treatment at Federal level. However, pending legislation in Congress (the "Fair Trade in Financial Services Act") would introduce a reciprocity standard for banking and securities regulation. The Commission has expressed concern about certain features of this bill, some of which are not paralleled in the Community financial services directives, and in particular about:

- *the fact that it could affect the expansion of enterprises already established in the US; there is no certainty that existing operations would be grandfathered;*
- *its automatic application to any third country found as not granting national treatment and effective market access, unless a prior approval is granted;*
- *the broad scope of sanctions, including the geographical expansion of activities, the expansion into new lines of business, and their application both at Federal and State level;*
- *the broad discretionary powers of the Administration to decide on the scope and duration of its application."*

Unlike in the case of the Community financial service directives, the restrictions which could be imposed would not replace current restrictions in the US, but would merely constitute additional barriers unmatched by any increased business opportunities.

IX BARRIERS IN OTHER SERVICES SECTORS

IX.A Maritime Transport

IX.A.1 Non-vessel operating common carriers

Description

The "Federal Maritime Commission Authorisation Act of 1990" - HR 4009 - was signed by President Bush on 16.11.90. Its Section 710, which deals with Non-Vessel Operating Common Carriers (NVOCC's), contains provisions which will put at risk the business of many Community freight forwarders who will be subjected to a range of requirements such as tariff filing, posting of a bond and appointing a resident agent in the US.

Comments/Estimated Impact

The Community considers that the financial and administrative obligations of Section 710 impose an unnecessary and unwarranted burden on the international transportation industry.

IX.A.2 Cargo Preference

Description

Certain types of government owned or financed cargoes are required by statute to be carried on US-flag commercial vessels.

The statutes are:

- ***The Cargo Preference Act of 1904.*** *This requires that all items procured for or owned by the military departments must be carried exclusively on US-flag vessels. Furthermore, the Cargo Preference Act of 1954 specifies that at least 50% of the 100% requirement must be met by the use of privately owned US-flag commercial vessels.*

- ***Public resolution n°17,*** *enacted in 1934, which requires that 100% of any cargoes generated by US Government loans (i.e. commodities financed by Eximbank loans) must be shipped on US-flag vessels, although the US Maritime Administration (MARAD) may grant waivers permitting up to 50% of the cargo generated by an individual loan to be shipped on vessels of the trading partner.*

- ***The Cargo Preference Act of 1954*** *requires that at least 50% of all US government generated cargoes subject to law be carried on privately-owned US flag commercial vessels (when they are available at fair and reasonable rates).*

- ***The Food Security Act of 1985,*** *which increases the minimum agricultural cargoes under certain foreign assistance programmes of the Department of Agriculture and the Agency for International Development (AID) to 75%.*

Comments/Estimated Impact

The impact of these cargo preference measures is hard to assess, but it is very significant. They deny EC and other non-US competitors access to a very sizeable pool of US cargo, while providing US shipowners with guaranteed cargoes at protected, highly remunerative rates. The burden on the US federal budget is clearly considerable. In 1987, revenue from government-impelled cargo preference totalled approximately $570 million for US-flag ship operators.

IX.B Air Transport

IX.B.1 Airline foreign ownership

Description

Until recently the Federal Aviation Act required that the President of an airline registered in the US and two-thirds of its board of directors and other management must be US-citizens and that 75% of the stock must be owned and controlled by US citizens.

Following a request from a number of air carriers established in the US, the Department of Transportation (DoT) recently announced that foreign investors may soon own up to 49% of the shares in an air carrier. However, the other restrictions seem to remain unchanged. In particular 75% of the voting stock in the airline must be owned by US citizens.

Comments/Estimated Impact

These US restrictions place European investment interests at a disadvantage and thus inhibit the free flow of transatlantic investment.

IX.B.2 Antidrug programme

Description

In November 1988, the Federal Aviation Administration (FAA) adopted regulations concerning an anti-drug programme for personnel engaged in specified aviation activities.

The drug testing required that, by 1.1.1991, these rules apply to employees performing sensitive safety and security-related functions, including employees located outside the territory of the US.

In April 1989, the FAA issued an amendment to the anti-drug rules extending for one year (until 2.1.1992) the compliance date specified in the rule for drug testing persons located outside the territory of the US.

Comments/Estimated Impact

The drug testing for personnel located outside the territory of the US is objectionable because of its extraterritorial reach.

IX.C Space Commercial Launch Policy

Description

The National Space Policy Directive of 6 September 1990 establishes that US Government satellites will be launched on US manufactured launch vehicles unless specifically exempted by the President.

From the US viewpoint, the measure is explained as part of a set of coordinated actions which are required to fulfil the long term goal of creating a free and fair market in which the US launch industry can compete.

Comments/Estimated Impact

This US policy is clearly detrimental to European launch service providers and the Commission services are at present examining how best to estimate its impact.

Through this policy, the US intend to promote their commercial space launch industry. As all US launches of government satellites are reserved for domestic launch service suppliers, European launch operators are effectively barred from competing for US government launch contracts, which account for approximately 80% of the US satellite market. The restriction, which is justified by the US for national security reasons as regards the launching of military satellites, is now also imposed on government satellites for civilian use.

IX.D Telecommunications

Description

Foreigners are virtually precluded from offering common carrier (telephone, telex, etc.) services in the US using radio communications by the ownership restrictions imposed on common carriers (see chapter XI C).

Uncertainties about the extent to which federal regulation of major US common carriers may be reduced ('streamlined') and about possible involvement of sub-federal authorities in regulating 'enhanced' or 'value added' services, have led to concerns that foreign enhanced service providers may face new barriers to market entry or predatory behaviour by network operators.

IX.D.1 Common carrier services

These may be provided by foreign-owned businesses if no radio communication is involved. However, these businesses also face discrimination in their regulatory treatment.

The Federal Communications Commission (FCC) establishes a distinction between "dominant" and "non-dominant" carriers. In theory, dominant carriers are those who hold market power and bottleneck facilities. They must comply with stricter regulations than non-dominant carriers. At present the only US carrier so designated is AT&T; and the extent of regulation implied by this designation is under consideration.

In practice, the FCC who classifies as "dominant" all foreign-owned carriers, 15% or more of whose stock is owned by a foreign telecommunications entity, irrespective of their size. These foreign-owned carriers face discriminatory treatment in matters pertaining to the construction of lines, tariffs and traffic and revenue reports, as follows:

- **Section 214 of the Communications Act** requires common carriers to seek FCC authorisation to construct new lines or extend existing lines. The FCC currently forebears regulation for domestic services; but for international services, "dominant" carriers must obtain authorisation for the construction <u>and</u> extension of lines; authorisation is required for each type of service, and each country; "non-dominant" carriers must only get authorisation for the construction of new lines.

- **The Cable Landing Act** requires a common carrier to seek a (marine) cable landing licence from the Secretary of State. This authority has been delegated to the FCC. The Act requires consideration of reciprocity.

All carriers must file <u>tariffs</u> at the FCC for international services; however:

- "dominant" carriers must file most tariffs at the FCC on a 45 days' notice instead of 14 days for "non-dominant" carriers;

- "non-dominant" carriers' tariffs enter automatically into effect at the end of 14 days unless found unlawful, whereas dominant carriers' tariffs must obtain a positive authorisation;

- "dominant" carriers must also submit their costs to justify any tariff changes.

All carriers must file annual international <u>traffic and revenue reports;</u> but only foreign-owned "dominant" carriers must file annual domestic traffic and revenue reports.

IX.D.2 Aeronautical satellite communications services

In 1989, the FCC confirmed its 1987 decision to give American Mobile Satellite Corporation (AMSC) an exclusive licence to provide domestic mobile satellite-based aeronautical services in the US. In its Order concerning AMSC, the FCC ruled that INMARSAT-based services may not be used on the domestic segments of international flights. Thus any aircraft in flight between two US domestic points will be unable to use INMARSAT-based systems, but will instead be obliged to use AMSC's domestic system.

IX.D.3 Enhanced services

Open Network Architecture (ONA): The 1990 California Court of Appeals ruling on the FCC Computer III Inquiry overturned key parts of the FCC's Third Computer Inquiry decision and affected the development of ONA. The Community is concerned that transparency on access to and use of the network by competitive service providers may be impaired unless the large telephone companies' network access policies are, or remain, effectively controlled by Federal authorities responsible for competition policy.

State/Federal jurisdiction: The California Court also overturned the FCC's preemption of state jurisdiction. The Community is concerned that individual State Public Utility Commissions may decide to regulate value-added services.

AT&T has been criticised before the FCC by some US competitors for linking the provision of transmission services with the purchase of AT&T equipment and/or different types of services. FCC decisions on the complaints which have been submitted are pending.

Comments/Estimated Impact

The discriminatory regulatory requirements applied to those foreign-owned carriers which are not excluded by S.310 of the 1934 Communications Act exacerbate the effective barriers to foreign competition in this sector. By regulating European competitors far smaller than many unregulated US companies, the FCC appears to be adopting criteria going beyond competition policy.

Clear legislative guidelines to protect service providers from predatory behaviour by common carriers are required, possibly on the lines set out in the Community's directives on telecommunications services and open network provision in the European markets.

X INTELLECTUAL PROPERTY

X.A Section 337 of the Tariff Act of 1930

Description

Under this Section, as amended by the Omnibus Trade Act of 1988, complainants may choose to petition the International Trade Commission (ITC) for the issuance of an order excluding entry into the US of products which allegedly violate US patents. ITC procedures entail a number of elements which accord less favourable treatment to imported products challenged as infringing US patents than that accorded to products of US origin similarly challenged. The choice of the ITC procedure over normal domestic procedures for complainants with respect to imported products is itself an inconsistency. In addition, the ITC has to take a decision with regard to such a petition within 90 days after the publication of a notice in the Federal Register. Although in complicated cases this period may be extended by 60 days, even this extended period is much shorter than the time it takes for a domestic procedure to be concluded in cases where the infringer is a US company. There are also several other features of the Section 337 procedure which constitute discriminatory treatment of imported products: the limitations on the ability of defendants to counterclaim, the possibility of general exclusion orders and the possibility of double proceedings before the ITC and in federal district courts. Furthermore, Section 337 applies "in addition to any other provisions of law". Suspension of a Section 337 investigation is not automatic when a parallel case is pending before a United States District Court.

Comments/Estimated Impact

The rapid and onerous character of procedures under Section 337 of the Tariff Act of 1930 puts a powerful weapon in the hands of US industry. This weapon is, in the view of European firms, abused for protectionist ends. As a result, European exporters may be led to withdraw from the US market rather than incur the heavy costs of a contestation, particularly if the quantity of exports in question is limited or if new ventures and smaller firms are involved.

In the context of a procedure under its new commercial policy instrument, the Community decided in 1987 to initiate dispute settlement procedures under Article XXIII of the GATT. The Panel established upon the Community's request concluded that Section 337 of the United States Tariff Act of 1930 is inconsistent with Article III:4, since imported products challenged as infringing United States patents are less favourably treated than products of United States origin which are similarly challenged. This discrimination cannot, according to the Panel's findings, be justified under Article XX(d).

The Panel also recommended that the Contracting Parties request the United States to bring the procedures applied to imported products in patent infringement cases into conformity with its obligations under the General Agreement.

Following the adoption of the report by the Contracting Parties at the end of 1989, the US Administration made it clear that it would continue to enforce section 337 without change, pending enactment of amending legislation which, in its view, could most effectively occur through legislation implementing the results of the Uruguay Round negotiations. Given that the timing of the conclusion of the negotiations is now uncertain, it is unclear when this unjustified discrimination against Community exports will be rectified.

X.B *Inadequate protection of geographical designations of European wines and spirits*

Description

Community legislation protects the geographical designations of wines. In 1983, an exchange of letters at high officials' level between the Community and the US provided a measure of protection for EC geographical names to designate wine. The US undertook not to appropriate such names, unless use was traditional. This is the so-called non-erosion clause. The exchange of letters expired in 1986 but the US has maintained its commitment to this clause.

In April 1990 the Bureau of Alcohol, Tobacco and Firearms (BATF) published a list of examples of "Foreign Nongeneric Names of Geographic Significance Used in the Designation of Wines". However, there are many Community geographical designations which do not figure on this list and the Community has indicated to the BATF that the list, as published, is not satisfactory.

In addition, the list did not address the question of wines considered "semi-generic" under US legislation. Here, too, the US continues to provide less strict protection than exists within the Community and this leaves the way open for the improper use of geographical designations of EC wines. Thus the US government allows some EC geographical denominations of great reputation to be used by US wine producers to designate wines of US origin. The most significant examples are Burgundy, Claret, Chablis, Champagne, Chianti, Malaga, Marsala, Madeira, Moselle, Port, Rhine Wine, Sauternes, Haut Sauternes, Sherry.

With regard to spirits, the US regulations basically provide protection against practices misleading the consumer. This limited protection does not prohibit the improper use of geographical designations of spirits or even the development of certain names into generic designations.

Comments/Estimated Impact

The improper use of Community geographic designations for wines and spirits places these products at a disadvantage on the US market.

In the multilateral Uruguay Round negotiations on Intellectual Property the Community has been seeking to establish a high level of protection preventing any use of a geopraphical indication identifying wines and spirits not originating in the place indicated.

X.C Other Intellectual Property Issues

X.C.1 Description

Discriminatory features of patent interference procedures.

In objecting to the granting of a US patent, evidence of prior inventive activity on US territory may be used to defeat an application. However, evidence of earlier inventive activity outside the United States is not taken into consideration. The Community considers the removal of such discrimination to be an important objective of the Uruguay Round.

Berne Convention

Until the United States acceded, in March 1989, to the Berne Convention, copyright relations with Member States were based on the Universal Copyright Convention with the result that, in general, neither party protected works first published in the other country before 1957. As required by Article 18 of the Berne Convention, EC Member States have now extended protection to pre-1957 US works. The US, however, has chosen to interpret Article 18 in a way which is, in the EC view, incorrect and has not extended protection to pre-1957 works of Community origin.

Despite the clear obligation in Article 6 bis of the Berne Convention to provide for "moral rights" of authors, the United States has taken no action to implement this in their national law.

Comments/Estimated Impact

It is difficult to assess the impact of these barriers but there is no doubt that it is substantial.

Trade related aspects of Intellectual Property rights are included in the Uruguay Round negotiations.

XI BARRIERS TO INVESTMENT

Introduction: US policy and attitudes towards foreign direct investment

Foreign groups still own only some 5% of total US assets, a relatively low figure when compared to the position in some European countries. However, foreign direct investment continues to rise steeply on both sides of the Atlantic. In 1989, the last year for which complete statistics exist, foreign investment in the US rose by 22% (21% from the EC), while US investment abroad increased 12% (14.4% in the EC).

The Bush Administration continues to support the longstanding US policy to welcome foreign investment and a Presidential statement reaffirming US international investment policy is said to be in preparation. Nevertheless, an active and sometimes bitter debate is under way not only in the Congress, but among several federal agencies questioning whether this policy should be changed. This is, in large measure, a reaction to US-Japan trade and investment relations, which have deteriorated markedly in recent years. Following Sony's purchase of Columbia, and the Mitsubishi Group's acquisition of the Rockefeller Center, US public and Congressional opinion have been further inflamed by the takeover of MCA by Matsushita, strongly opposed by Interior Secretary Lujan (because MCA owns the concessions at one of the US's most famous national parks, Yosemite).

However, the changed political climate affects <u>all</u> foreign investors. In fact, EC countries account for a much greater percentage of foreign investment in the US than does Japan.

The first significant effect upon legislation of the squeeze on foreign investors was the "Exon-Florio" provisions of the 1988 Trade Act, which required that mergers and acquisitions deemed to affect national security (this concept remains undefined) be reviewed by a Committee; on recommendation from the Committee, the President may order divestiture of assets.

The second was the 1990 Omnibus Budget Reconciliation Act (Foreign Tax Equity provisions), which, inter alia, imposed reporting requirements on foreign companies, applicable retroactively. These are both onerous and extraterritorial in nature.

A number of bills designed to discriminate against foreign investors or having that effect are likely to be revived in 1991. More than 20 were tabled in Congress in 1990.

There are a number of specific sectors where foreign ownership has been restricted, sometimes since the early part of the century. These include shipping, broadcasting, telecommunications and energy. The US Government has taken steps to relax similar restrictions in civil aviation.

XI.A Exon-Florio Amendment

Description

Section 5021 of the 1988 Trade Act, the so-called Exon-Florio amendment (from the names of its sponsors), provides that the President or his nominee may investigate the effects on US national security of any mergers, acquisitions and takeovers which could result in foreign control of persons engaged in interstate commerce in the US. This screening is carried out by the Treasury-chaired Committee on Foreign Investment in the US.

Should the President decide that any such transactions threaten national security, he may take action to suspend or prohibit them. This could include the forced divestment of assets.

The US Department of the Treasury is considering regulations to implement Section 5021. The first draft of these, which was published in July 1989, raised serious concerns among countries and companies with investment interests in the US; the Community made an official démarche on this subject.
A number of bills intended to extend the scope of Exon-Florio provisions, or to widen the concept of national security to purely economic matters, were tabled in Congress in 1990. Some of these are likely to be revived in 1991.

Comments/Estimated Impact

While the European Community understands the wishes of the United States to take all necessary steps to safeguard its national security, there is concern that the scope of application may be carried beyond what is necessary to protect essential security interests. In this context, the Community has highlighted in comments to the US Administration the wide scope of the draft Treasury Regulations, the lack of a definition of national security, and the uncertainty as to which transactions are notifiable. These uncertainties, coupled with the fear of potential forced divestment, have meant in practice that many foreign investors have felt obliged to give prior notification of their proposed investments. Indeed the Treasury itself estimated that, in 1990, 350 of an expected 700 foreign acquisitions of $1 million or more will have been notified in advance. This means in effect that a very significant number of foreign acquisitions in the US will be subject to pre-screening and notification.

If implemented in a restrictive manner, the Exon-Florio provisions could inhibit the efforts of OECD members to improve the free flow of foreign investment and could conflict with the principles of the OECD Code of Liberalisation of Capital Movements. Such an approach would also harm common EC-US efforts to establish multilateral disciplines on trade-related investment measures in the Uruguay Round negotiations.

XI.B Tax Legislation

XI.B.1 *Information reporting requirements*

Description

Information reporting requirements of the US Tax Code with respect to certain foreign-owned corporations treat domestic and foreign companies in a different fashion :

- *The foreign ownership threshold for reporting is expanded to include corporations with at least one 25% foreign shareholder.*
- *The record keeping requirements are extended offshore by requiring foreign corporations to transfer records, in certain circumstances, to their US subsidiary.*
- *US law is further extended offshore by requiring foreign corporations to nominate their US subsidiaries as their agents to receive IRS (Internal Revenue Services) summonses.*
- *Penalties for failure to comply with reporting requirements have been increased considerably (from US$1,000 to US$10,000).*

The Omnibus Budget Reconciliation Act of 1990 further extended the reporting requirements and related provisions :

- *The provisions apply not only to subsidiaries of foreign companies but also to all other "foreign" entities such as branches (this will primarily affect foreign banks).*
- *The requirements apply retroactively to all open tax years and to all records in existence on 20 March 1990.*

Comments/Estimated Impact

These requirements, particularly the retroactive provisions and the extension of the record keeping to the transactions of US branches of multinationals, are both onerous and extraterritorial. They appear to discriminate against foreign companies and could have the effect of discouraging foreign investment in the US.

XI.B.2 *"Earnings stripping" provisions*

Description

The Budget Reconciliation Act of 1989 contained the so-called "earnings stripping" provisions (Internal Revenue Code 163 (j)), which place a limitation on the extent to which interest payments can be deducted from taxable income. The limitation applies when the interest is paid by a *corporation which is subject to tax in the US, to a related party which is exempt from US tax. The majority of such tax exempt related parties will, in practice, be foreign corporations. The new law limiting excess interest is designed to prevent foreign companies artificially loading a US subsidiary with debt, beyond that which would be sustainable on the balance sheet of a dependent corporation. Such artificial loading can, in effect, transfer profits away from the US.*

Comments/Estimated Impact

The objective of limiting excess interest is reasonable and consistent with the OECD model tax treaty. However, the US law uses a formula as part of its determination of excess interest which is inconsistent with the internationally accepted arm's length principle. This could, depending on the way this provision is implemented, be discriminatoryand therefore discourage foreign investment in the US.

The law provides for regulations to ensure that the principle is adhered to. Until those regulations are published, it will be impossible to judge whether or not the US practice is consistent with tax treaties.

XI.B.3 State Unitary Income taxation

Description

Certain individual US States assess State corporate income tax for foreign-owned companies operating within their state borders on the basis of an arbitrarily calculated proportion of the total worldwide turnover of the company[1]*. This proportion of total worldwide earnings is assessed in such a way that a company may have to pay tax on income arising outside the State, thus giving rise to double taxation.*

Comments/Estimated Impact

Quite apart from the added fiscal burden, a state which applies unitary taxation is reaching beyond the borders of its own jurisdiction and taxing income earned outside that jurisdiction. This is in breach of the internationally accepted "water's edge" principle. A company may also face heavy compliance costs in furnishing details of its worldwide operations.

Developments in the State of California, home to numerous foreign-owned companies, continue to be important. In November 1990, the California Appeals Court ruled that California's unitary tax method (which is known as "world wide combined reporting") as applied to foreign-based groups is unconstitutional under the foreign commerce clause of the Federal

(1) According to a 1988 Price Waterhouse report "Doing Business with USA" (p. A-4), the States concerned are Alaska, Arizona, California, Colorado, Connecticut, District of Columbia, Illinois, Indiana, Iowa, Kansas, Massachusetts, New Hampshire, New Jersey, New York, Ohio, Rhode Island and West Virginia.

Constitution. However, because this ruling adressed California practice prior to 1986, it did not invalidate the current state tax law, which was adopted in 1986. Some progress has been made: in September 1986 a tax bill was adopted providing for an alternative solution to unitary taxation, the "water's edge principle" according to which a foreign company may be taxed only on the income arising in the jurisdiction of the host state. Nevertheless, the situation remains inequitable.

In 1988 the Californian law was modified again to further alleviate concerns of foreign-owned companies. Only companies that elect the water's edge approach are now required to file domestic disclosure spread sheets. The other major change was that if it qualifies and elects to do so, a company must bind itself contractually to the water's edge approach for five rather than ten years, as the law originally required.

Although the latest Californian legislation can be considered a step forward, it is still less than satisfactory. Although the length of commitment has been shortened, a company must still bind itself contractually for a five-year period in order to "elect" the water's edge treatment. An annual election fee must be paid by a company that takes the water's edge approach. A more basic objection is that extensive discretionary tax powers continue to be granted to state tax authorities.

No assessment has been made of the effect of unitary tax on EC investment in the United States, but EC-owned companies consider this tax treatment to affect adversely their current or planned operations.

The EC and its Member States will continue to monitor the development of such legislation which are a disincentive for investment in the USA as well as a straightforward breach of bilateral tax treaties between the USA and the Member States of the EC.

XI.C Telecommunications

Description

Section 310 of the Communications Act of 1934 imposes limitations on foreign investment in radio communications: no broadcast (or aeronautical en route or fixed radio station licence) may be held by foreign governments, aliens, corporations in which any officer or director is an alien or of which more than 20% of the capital stock is owned by an alien (25% if the ownership is indirect). As most common carriers need to integrate radio transmission stations, satellite earth stations and in some cases, microwave towers into their networks, foreign-owned US common carriers are unable to compete in much of the market. S.310 also applies to the Communications Satellite Corporation (COMSAT) which as US signatory to the INTELSAT and INMARSAT agreements is sole supplier of INTELSAT space segment services to US users and international service carriers, and of INMARSAT international maritime and aeronautical satellite telecommunications services. The Act provides for waivers but the Federal Communications Commission (FCC) has never used this possibility.

Comments/Estimated Impact

Foreign operators are denied access to ownership in these sectors in contradiction of the principles of the OECD Code of Liberalisation of Capital Movements. As they may not own wireless facilities and networks, and may not take a large stake in US companies providing them, they are effectively prevented from competing in providing most common carrier services. Effectively, S. 310 obliges foreign carriers either to enter into subcontracting arrangements with US carriers, or to use alternative (non-radio) technology.

The ultimate rationale for these restrictions is the argument that US control of communications is essential at all times, for reasons of national security.

XI.D Other restrictions on foreign direct investment in US

XI.D.1 National Security Restrictions

Description

*Apart from the restrictions on foreign ownership of broadcasting and telecommunications facilities (see also chapter IX D) and of airlines (see also chapter IX B 1), the United States has notified a number of additional restrictions on foreign ownership to the OECD, which it has justified "partly or wholly" on grounds of **national security**:*

- *Foreign-owned or controlled firms are not accorded licences to operate nuclear energy installations, under the 1954 Atomic Energy Act.*

- *Foreign investment is restricted in coastal and domestic shipping under the Jones Act and the US Outer Continental Shelf Lands Act; this includes fishing, dredging, salvaging or supply transport from a point in the US to an offshore drilling rig or platform on the Continental Shelf (see chapter III D 2).*

- *Foreign investors must form a US subsidiary for exploitation of:*
  - *ocean thermal energy*
  - *hydroelectric power (e.g. under the Federal Power Act)*
  - *geothermal steam or related resources, on federal lands (Geothermal Steam Act)*
  - *deep water ports*
  - *mining on federal lands, the Outer Continental shelf or the deep seabed (US Outer Continental Shelf Lands Act and US Deep Seabed Hard Mineral Resource Act)*
  - *fishing in the Exclusive Economic Zone (Commercial Fishing Industry Vessel Anti-reflagging Act of 1987),*

  or for acquisition of rights of way for oil pipelines, leases (or interest therein) for mining coal, oil or certain other minerals

- *Licences for cable landings are only granted to applicants in partnership with US entities.*

XI.D.2 Restrictions at State level

Description

The United States has also informed the OECD of a number of restrictions at State level.

A significant number of States have laws directed at the ownership of US land by aliens and business entities. These laws vary greatly from State to State in their degree of severity (e.g. in terms of specification of types of land and of acreage amounts and in terms of exceptions). Twenty-nine States have some type of law restricting alien ownership of land. Nine States require aliens to report their landholdings within the State. Fifteen States restrict business entities from owning land or engaging in the business of farming. Eleven States have laws requiring business entities to report their landholdings within the State. An individual State may be included in more than one of the above categories.

Four States place restrictions on foreign access to mineral rights. One (Rhode Island) will not issue certificates for investments in public utilities. Four states have placed severe restrictions on ownership of real property by non-US citizens. For restrictions in the field of financial services, see chapter VIII.

XI.D.3 Reporting requirements

Description

The United States maintains a number of reporting requirements which apply to foreign-owned businesses. These include:

- Notification of proposed takeovers and acquisitions with a bearing on national security (under "Exon-Florio": see section A of this chapter)

- Those provided for in tax legislation (see section B 1 of this chapter)

- Those provided for by the International Investment and Trade in Services Survey Act. This requires any direct investment which results in single foreign or associated foreign persons owning more than 10% of a US business to be reported to the Bureau of Economic Analysis (BEA) of the Commerce Department. Every five years, foreign-owned business must also contribute information to the BEA's benchmark surveys. This is quite detailed in the case of businesses which have total assets, sales or net incomes of more than $1 million or 200 acres of land.

Quarterly reports for payments flows and annual reports covering US affiliates are also used to update this data. The Commerce Department also conducts annual surveys on major new foreign direct investments; the new investor must, within 45 days of his acquisition, file a report if his investment exceeds the $1 million/200 acre threshold. A number of bills tabled in Congress/Senate in 1990 would have relaxed the confidentiality rules regarding this information, or substantially increased the burden of reporting requirements.

- *Foreign ownership of more than 10 acres of agricultural land must be reported to the Agriculture Department, under the 1978 Agriculture Foreign Investment Disclosure Act. This information is available to the public.*

- *The Federal Reserve Board maintains information on individual foreign-owned US depository institutions. Some of this information is available to the public.*

Comments/Estimated Impact

The US denies national treatment, in the cases referred in sections D 1 and D 2 above, to foreign-owned businesses. Barriers to ownership in certain key sectors also affect procurement of goods and services.

If reporting requirements (section D 3 above) become burdensome, they act as a deterrent to investors, particularly if confidentiality cannot be assured.