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REPORT ON US BARRIERS TO TRADE AND INVESTMENT

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1. INTRODUCTION

The 1993 Report on United States' Trade and Investment Barriers is the ninth annual report in which the services of the Commission of the European Community set out the barriers and impediments with which European business is faced in trading with and investing in the United States. The report has taken into account developments until March 1993.

A. *Development of the economic relationship*

The present report on barriers and impediments to trade with and investment in the US should be seen against the background of an overall positive EC-US economic relationship. The European Community and the US are the world's largest trading actors, together accounting for more than one third of world trade. Bilaterally, the EC and the US have consistently been each other's largest trade partner. Trade flows between them are currently running at about $200 billion a year, constituting some 7.5% of total world trade. The exports of both partners have continually increased since the early 1980s. Although the Community is running a modest trade deficit with the US, a tendency towards a diminishing trade imbalance has emerged most recently. On a sectoral basis, the balance of trade differs substantially, indicating quite clearly that both partners are making full use of their respective competitive advantages.

The substantial growth of foreign direct investment (FDI) flows has greatly increased the economic linkages between the European Community and the United States. In 1991, Community investors owned more than half of the FDI stocks in the US, while over two fifths of American-owned FDI stocks were located in the Community. At historical prices, these investments together are worth more than $420 billion. At current prices their value is certainly much greater.

A very important percentage of the merchandise trade between industrialised countries nowadays takes place between parent companies and their affiliates. This is also true in the case of the growing number of transatlantic companies which increasingly account for a significant share of total employment, value added sales, and research and development expenditure on both sides of the Atlantic. There is thus a common interest of the EC and the US in promoting these economic links. This is even more the case since the Community as of 1 January 1993 has established the Internal Market, by which all remaining intra Community trade barriers have been removed, notably to the benefit of intra Community trade, but also to the advantage of third country exporters doing business within all of the Community.

The growing economic interdependence between the US and the Community can no longer be overlooked. Still, there remains anxiety that this

relationship may become increasingly dominated by US domestic concerns about US competitiveness of its industries. In 1992, the European Community has seen protectionist trade legislation being repeatedly tabled in Congress, ranging from a new and tougher "Super 301" procedure (**Trade Expansion Act**, HR 5100) to proposals which seek to expand the scope of US antitrust law, creating new private causes of action to allow treble damages for those injured by alleged low-price sales of foreign goods in the US (**International Fair Competition Act**, S 2610). Such measures would seriously undermine the multilateral rules laid down in the GATT and the OECD, as well as some of the main principles upon which the open trading system has been constructed, including the principles of most-favoured nation treatment and of national treatment.

Of equal concern to the Community is the US approach to resolve trade problems through the conclusion of bilateral agreements, and its reluctance either to accept GATT Panel rulings (as in the Marine Mammals case, see Chapter 3.C.), or to modify legislation when a GATT Panel report has been adopted (as in the case of discriminatory action in the field of patents under Section 337 - see Chapter 11.A.1.).

And only recently, the imposition by the US of anti-dumping and countervailing duties on steel imports from Community producers has perturbed the transatlantic economic relationship. Not only are the duties unjustified on economic grounds, but they have been determined on doubtful procedural and material grounds, reasons for which the Community has already requested consultations within the GATT.

What is at stake , therefore, is a free and open trading system, which has ensured prosperity in the Community and in the US for the past 40 years, and which has given the opportunity to many countries in the world to improve their living standards. It is therefore to be welcomed that President Clinton's trade policy speech at American University on February 26, 1993 included a basic commitment by the US to an open world trading system and the Uruguay Round. The President's call for cooperation toward world economic growth and his welcome for foreign investment are positive signals against a background of worrying rethoric recently used by the new US administration on issues like telecom, public procurement and Airbus subsidies.

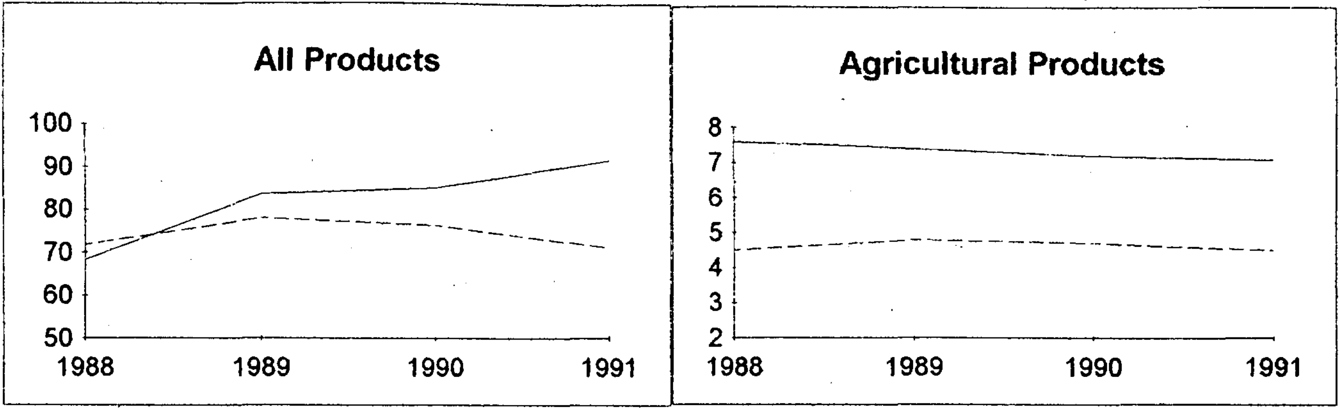
B. *Objectives of the Report*

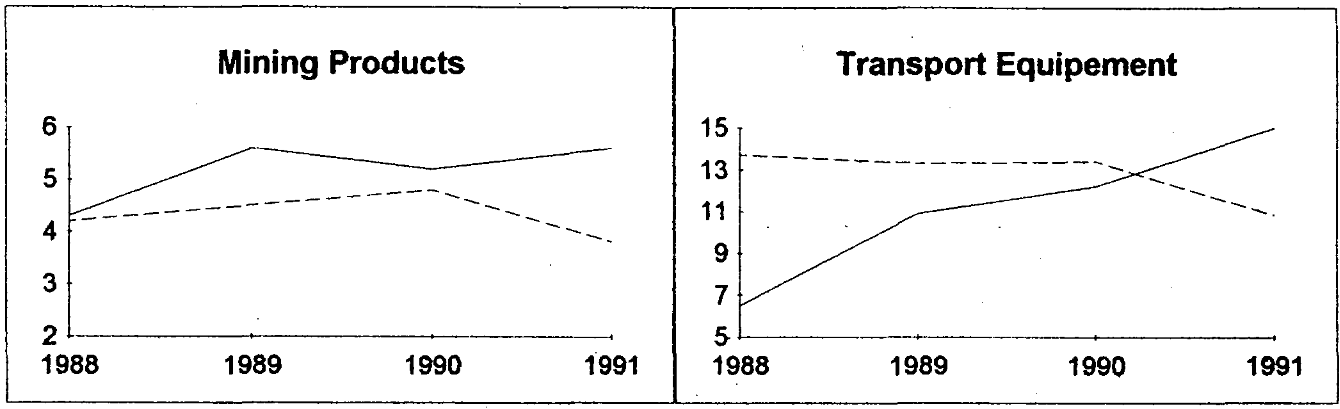
The Commission services' annual report on US Trade and Investment Barriers aims at presenting as comprehensive an inventory as possible. Where approriate, it discusses the measures deemed to be a trade or investment barrier or impediment, points out the Community's legal and political position, and refers to action which has been undertaken in the past or which is envisaged for the future.

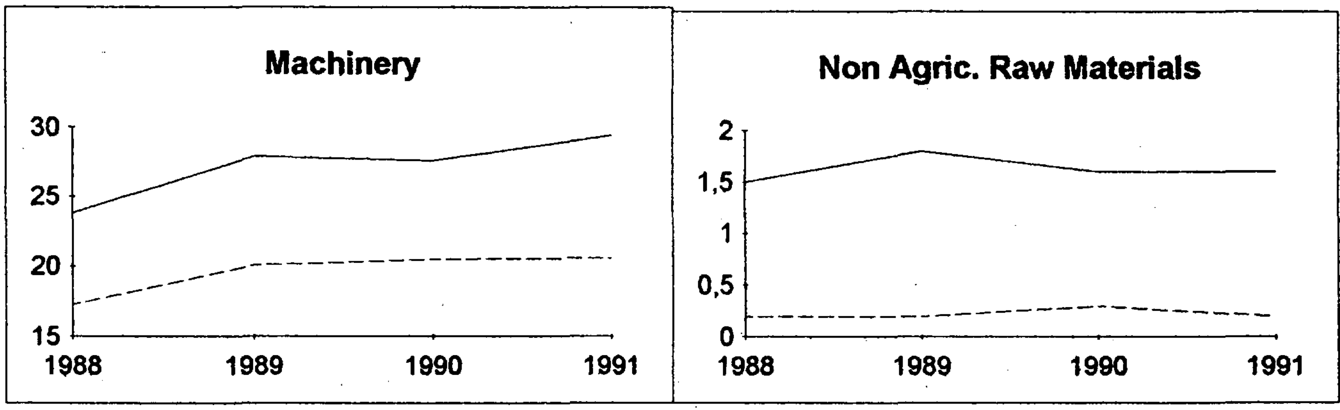
Originally, the reports were compiled in order to redress the impression given by the annual US National Trade Estimate Report that trade barriers are primarily a problem encountered by US business abroad, while the US market is essentially open. However, day-to-day reality shows that European business encounters many serious problems in doing business in the US.

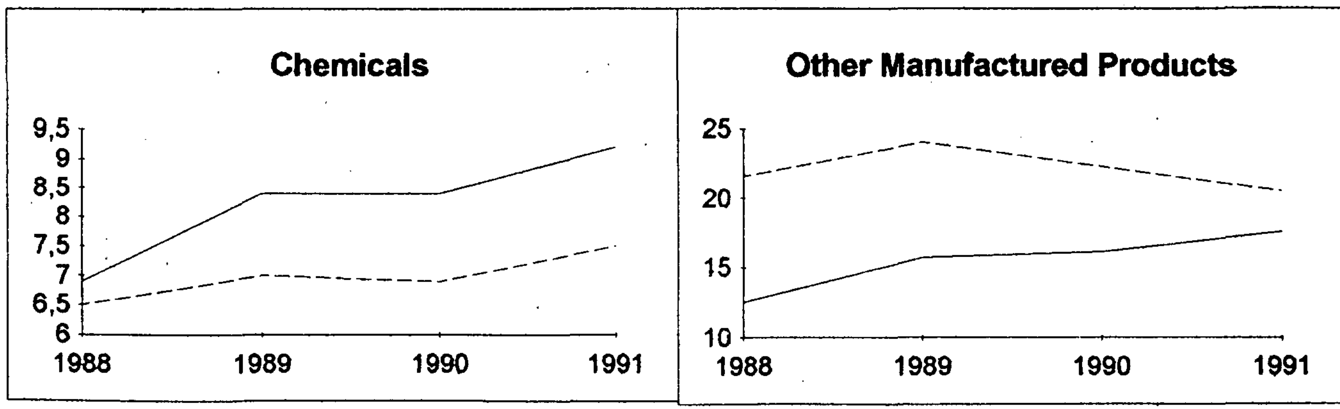
Trade of EC with the US

(in bn ecus)









Imports
Exports

Source: Eurostat

As a means of identifying problems of access to US markets, they have become a useful tool for focusing dialogue and negotiations, both multilateral and bilateral, on the elimination of the obstacles inhibiting the free flow of trade and investment. With this in mind, it is hoped that the present report can play a useful part in the formation of the new US administration's policy on the issues highlighted in the report.

C. *Principal findings of the Report*

As in previous reports, the **unilateral elements in US trade legislation** which are referred to in Chapter 2 rank highest in the Community's concerns. The general objective of achieving freer trade on a multilateral basis is increasingly endangered by unilateral and potentially GATT-illegal US dispute settlement, as in the case of the "section 301" legislation. No other major trading partner of the Community has legislation of this kind. The Community is therefore reinforcing its efforts to strengthen the multilateral dispute-settlement mechanism which is still being negotiated within the Uruguay Round. A comprehensive multilateral dispute settlement mechanism could be expected to restrain GATT Contracting Parties from further resorting to unilateral determinations in trade disputes.

Closely linked to the aspect of unilateralism is that of the **extraterritorial reach of US legislation** which impacts on trade. It may not only conflict with the sovereignty of trading partners, but also may result in conflicting legal demands on economic operators. As a consequence, trade and investment may seriously be hampered. As an example of the resulting effects in cases where one trading partner seeks to impose its own standards and its own policies on others, the **Marine Mammal Protection Act** and the **Cuban Democracy Act** have been taken up in chapter 3. Although there should be no question that there is a need for in-depth reflection notably of the relationship between a free trading system and comprehensive protection of the environment, conflicts should be resolved by a coherent set of multilateral rules. The Community is actively pursuing this objective in different multilateral fora.

The US continues to put forward **national security considerations** to justify growing trade restrictions. As explained in chapter 4, these range from limits on market share to procurement restrictions, and from unilateral export controls to the screening of, or restrictions on, foreign direct investment. The Community does not question the right of every sovereign country to take such measures as are necessary to defend its national security. However, it is concerned that the concept of national security is increasingly interpreted by the US in a way which also embraces **national economic security**. Such a shift of view would inevitably lead to even more protectionist measures on the US side. The Community has repeatedly criticised the US for extensively applying national security considerations in trade issues. It is of the opinion that also in this area multilateral criteria should be developed. There have been Community efforts in this direction within the Uruguay Round negotiations, but which have so far been rejected by the US.

US **public procurement practices**, which have been taken up in chapter 5 have always been a problem of particular importance to European business

seeking access to US markets. The extensive discrimination or even total exclusion of non-US business in and from public procurement at federal and at State level by the so-called "Buy American" legislation continues to be of continued deep concern to the Community. What is more, there exist structural impediments, notably in the telecommunications market, by which market access of European firms becomes extremely difficult, if not completely impossible. The Community has taken up the issue in the Uruguay Round , as well as in bilateral negotiations. It has also successfully employed the GATT dispute settlement procedure in the case of the procurement of a sonar mapping system. It urges the US to finally adopt the relevant GATT panel report.

High tariffs, fees, import quotas and **invoice requirements** , as described in chapter 6, continue to present important barriers for imports into the US, affecting some of the Community's key export items or sectors. The removal of high tariffs which protect the US markets for textiles, clothing, footwear, tableware, glassware and other products - some of them ranging between 30% and 40% - has been a priority for the Community in the Uruguay Round. Other tariff equivalent impediments have been or will be, as far as necessary, addressed within the GATT.

US subsidies, destined to support and enhance US exports of **agricultural products**, as for example in the case of the US Export Enhancement Programme dealt with in chapter 7, are still a source of distortion of trade, as they are targeted on certain markets with a view to expand market shares. In view of the efforts within the Uruguay Round negotiations towards a substantive reduction of agricultural subsidies, the US are also expected to undertake efforts to substantually reduce their respective subsidies.

Tax legislation in the US can constitute an impediment to trade. In chapter 8, this is notably illustrated by the case of European imported cars which in the US are subject to an accumulation of the so-called gas guzzler tax, the luxury tax and the Corporate Average Fuel Efficiency (CAFE) penalty. The Community views this taxation as being discriminatory and contrary to the pertinent GATT provisions. Subsequently, in March 1993 the Community requested a GATT panel to declare this tax legislation incompatible with GATT rules.

The growing economic interdependence between the US and the Community has made apparent that the **multiplicity of standards** and standard-making procedures in the US, their lack of conformity with international norms, and the resulting fragmentation of the US market increasingly take on the character of impediments and even barriers to trade, as set out in chapter 9. The Community would like to pursue the concept of regulatory convergence to resolve the emerging trade problems in this field. The agreement between the US and the Community on the Third Country Meat Directive concerning sanitary standards in slaughterhouses is an excellent example of the resolution of trade hampering divergence in the field of standards.

In the services' sector, there exist a variety of impediments to **access to the US services markets.** Chapter 10 refers notably to sectors such as banking, securities and insurance services and telecommunication and broadcasting services. Many of the trade issues raised in the service

sectors are subject of the negotiations in the Uruguay Round on a General Agreement in Trade in Services (GATS). A successful conclusion of these negotiations would considerably contribute to eliminate major trade impediments in the US in this field.

In the field of **intellectual property rights**, chapter 11 points out that the discriminatory aspects of Section 337 of the 1930 Tariff Act, which allows the US to bar products which allegedly violate US patents, have still remained unchanged, although they have been ruled contrary to GATT rules in 1989 by a GATT Panel requested by the Community. As regards geographical indications of European wines and spirits, their protection in the US remains inadequate. Negotiations between the Community and the US have so far not led to satisfactory results.

Barriers and impediments to investment in the US are mainly characterized in chapter 12 by keylegislation such as the Exon-Florio Amendment and tax concepts such as transfer pricing and unitary income taxation. These measures are counterproductive to efforts undertaken by the Community notably within the OECD to further advance liberalisation measures and instruments.

2. UNILATERALISM IN US TRADE LEGISLATION

A. *General remarks*

Unilateralism is a characteristic element of many US legislative provisions. It generally takes the form of unilateral sanctions or retaliatory measures against "offending" countries or natural or legal persons. These measures are unilateral in the sense that they are taken on the basis of a US judgment of the behaviour or legislation of a third country without reference to, and often in defiance of, agreed multilateral rules.

Such measures are also to be found in US trade legislation. In this way, the main objective of the **Trade Act** of 1974 as amended by the **Omnibus Trade and Competitiveness Act** of 1988 is to open foreign markets to US goods and services and to provide effective unilateral sanctions against nations perceived by the US to be trading unfairly.

B. *Section 301 of the Trade Act of 1974 and related measures*

Section 301 of the 1974 **Trade Act** authorised the US Administration to take action to enforce US rights under international trade agreements and to combat foreign governmental practices which the US government judges to be discriminatory or unreasonable and to burden or restrict US commerce. In GATT covered areas it permits unilateral action to be taken by the US against its trading partners, without the prior authorisation of the Contracting Parties. The 1988 **Omnibus Trade and Competitiveness Act** added strict time limits for completing the Section 301 process. In other cases of alleged trade agreement violations or cases where a foreign nation's policy or practice is judged to be "unjustifiable" and burdens or restricts US commerce, the Act makes retaliation mandatory rather than discretionary. It may thus oblige the US government to take further action contrary to its international obligations.

The US used the Section 301 procedure twice against the Community, in 1989, when retaliatory measures (which are still upheld) were introduced against the EC in the hormones dispute, and when USTR made a determination of unfairness with respect to the EC oilseeds regime. In addition, the US has repeatedly used the threat of Section 301 action, in flagrant violation of the spirit of GATT rules. The disputes concerning canned fruit, shipbuilding and Airbus are cases in point. The Community will continue to defend its GATT rights whenever Section 301 is used to the detriment of its trading rights.

Although the so-called "Super 301" lapsed in 1991, it is worth maintaining a "watch" on this kind of provision. In 1992, the EC has voiced its concern about proposals introduced into the 102nd Congress (**Trade Expansion Act**, HR 5100) which aimed to reinstate this procedure, whereby

the US Trade Representative was required to identify 'priority' unfair trade practices from 'priority' countries, and self-initiate Section 301 cases against them with a view to their modification and eventual elimination, even though such countries were not subject to international obligations with respect to the practices concerned. Early in 1993, similar proposals have been introduced into the Senate, which may eventually develop into a full-scale Trade Act legislation (cf. **Trade Enforcement Act**, S90; **Trade Compliance Act**, S268; **Super 301**, S301).

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

The unique feature of the "301" family of legislation is that they permit unilateral determinations and action, or threats thereof, inconsistent with, and in clear contradiction with, the multilateral trading system. The GATT does not allow for any unilateral interpretation of the rights and obligations of contracting parties, nor for unilateral action by any one contracting party aimed at inducing another contracting party to bring its trade policies into conformity with the General Agreement. Under the GATT dispute settlement procedures, any trade retaliatory measure has to be authorised by the Council. GATT contracting parties therefore have expressed serious concern about the continuing use of unilateral trade measures, or threats thereof, by the United States.

To abandon unilateralism remains an important objective for the EC in the Uruguay Round. The draft Agreement on the new dispute settlement mechanism which will also cover the new areas - services, intellectual property and investment - contains strict commitments to prevent unilateral determinations and measures in the process; it submits all the important stages of a dispute to multilateral provisions. Consequently the contracting parties are entitled to expect that the US will adapt its procedures so as to act in conformity with the future multilateral system; and that its legislation is also adapted accordingly.

C. *Telecommunications Trade Act of 1988*

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

The Community has been and continues to be designated as a priority country under the Act. Nevertheless, in February 1992 the US Trade Representative stated that for the time being sanctions were not felt appropriate as negotiations in the telecommunications sector were continuing.

Pursuant to the 1987 Green Paper on Telecommunications, Community legislation is now in force which liberalises procurement by telecom utilities, introducing a high level of transparency and leading to improved market access, the sale of terminal equipment, and the provision of value-added and data services. Liberalisation in the satellite and mobile telecommunications sectors is also under way, and a review is currently being conducted by the Commission of the entire service sector.

The Community cannot accept that the US unilaterally determines what constitutes a barrier or when "mutually advantageous market opportunities" in telecommunications have been obtained. Nor can the Community accept US efforts to negotiate under threat of unilateral retaliation, which can only hinder the multilateral negotiations. In addition, such sectoral reciprocity is inconsistent with the principles of the multilateral trading system. Consequently, the Community continues to be extremely concerned about barriers to trade in the US market which have been identified in the telecommunications sector (see Chapters 5.B.2.d., 9.E., 10.B.4., 12.D.) which, in many cases, the US is unwilling to see addressed in the GATT.

D. *Title VII of the Trade Act of 1988*

The **Omnibus Trade and Competitiveness 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 publish an annual report on the foreign countries which discriminate against US products or services in their procurement.

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. Action in non-Code covered sectors would run against basic GATT principles.

By a determination of the US President of 27 April 1992, the EC and certain Member States were identified as countries alleged to discriminate in public procurement against US products and services. Reference was made notably to Article 29 of the EC's Utilities Directive (EEC/90/531). The President's determination also set 1 January 1993 as a date for sanctions against the Community in the event the discriminatory provision of the EC's Utilities Directive was applied. On 31 January 1993, the US Trade Representative announced that a prohibition of award of contracts by Federal agencies for products and services not covered by the GATT Government Procurement Code from some or all of the Member States of the European Community would enter into force as of 22 March 1993. In

addition, USTR immediately solicited public comments concerning the impact of other possible actions restricting imports of telecommunications and power generating equipment from the European Communities, and held out a prospect of a study of the desirability and feasibility of the US withdrawing from the GATT Government Procurement Code.

In the context of the multilateral trade negotiations, including the GATT Procurement Code negotiations and on particular telecommunications access, the US played up the allegedly discriminatory nature of Article 29 of the Utilities Directive. Article 29 is now in force for the majority of the Member States. Its impact is in any event under US scrutiny, as the provisions will not apply against third countries with whom the Community has reached an agreement ensuring comparable, effective and lasting access. Since Article 29 applies to areas not covered by the GATT Procurement Code, the community is not obliged to pass on the advantages of the Utilities Directive to parties to the Code or to all corners. The EC is actively negotiating in good faith with the US to achieve an agreement both in the GATT Procurement Code and the telecommunications sector. The threat of retaliation against a provision which will only continue to apply if those negotiations fail is hardly conducive to success. Moreover, these negotiations are taking place against a background of increasing US protection of its own procurement (see Chapter 5.).

3. EXTRATERRITORIAL APPLICATION OF US LEGISLATION

A. *General remarks*

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 unjustified hardships and conflicting requirements. The extraterritorial scope of US legislation affects inter alia importers and exporters based outside the US, who have to comply with US export and re-export control requirements and prohibitions, US owned or controlled businesses in Europe which have to comply with US foreign policy trade legislation, for example the Cuban Democracy Act, as well as manufacturers, who have to keep track of end-users or potential mis-users of sensitive items.

One of the most blatantly and problematical extraterritorial issues is found in the US **Export Administration Regulations** (EAR), the legislative authority for which was the Export Administration Act (EAA) of 1979, as amended. The authority granted under the EAA expired on 30 September 1990 after which the President invoked his authority, including authority under the **International Emergency Economic Powers Act** (IEEPA), to continue the system of controls that had been maintained under the EAA. Although a bill to reauthorise the EAA was introduced into the US Congress in 1991, it was not passed. The EAR, among other things, require companies incorporated in and operating in Member States to comply with US re-export controls. This includes compliance with US prohibitions on re-exports for reasons of US national security and foreign policy subject to US jurisdiction. While the extraterritorial nature of these controls has repeatedly been criticised by the Community and its Member States notably during the Siberian pipeline dispute of 1982, they continue to be applied.

Furthermore, serious 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. The possible sanctions consist of a prohibition on contracting or procurement by US entities and the banning of imports of all products manufactured by the foreign violator. They are thus of such a nature that they must be deemed contrary to the GATT and its Public Procurement Code.

B. *Cuban Democracy Act*

Since 1962, the year in which the US first proclaimed a trade embargo vis-à-vis Cuba, Cuban/US relations have mainly been determined by Section 620 (a) of the **Foreign Assistance Act** (FAA) of 1961, as amended, the **Trading with the Enemy Act** (TWEA) of 1917, as amended, and, the **International Economic Emergency Powers Act** of 1977 (IEEPA).

The FAA and TWEA provide the legal basis for the promulgation of the **Cuban Assets Control Regulations**, which prohibit virtually all commercial and financial transactions with Cuba or Cuban nationals by US companies, US owned or controlled companies and US nationals, unless specifically licenced by the Department of the Treasury. The IEEPA provides the legal authority to control and prohibit US exports to Cuba.

The Cuban Democracy Act of 1992 (CDA) amends the Cuban Assets Control Regulations and further restricts licenced trade with Cuba to only humanitarian actions and food aid operations. Section 1706 of the CDA lays down a number of trade prohibitions. These are:

- a prohibition of all commercial transactions and payments by US owned or controlled foreign firms with Cuba. This will, however, not affect contracts entered into before the date of enactment of the CDA;
- a 180 days landing ban on commercial vessels departing from Cuba, except pursuant a licence issued by the US Secretary of Treasury ;
- a landing ban on vessels carrying goods or passengers to or from Cuba or carrying goods in which Cuba has any interest, except pursuant a licence issued by the US Secretary of the Treasury.
- a prohibition on supplying ships carrying goods or persons to or from Cuba.

According to Senator Graham, the CDA will close a loophole which allowed foreign subsidiaries to make $583 million in Cuban operations. US subsidiaries abroad have requested, in 1991, Treasury licences for $718 million of trade with Cuba. The impact of the CDA upon EC trade and investment with Cuba will probably affect a fraction of that amount.

That part of the CDA which purports to prohibit foreign firms which are owned or controlled by US companies from trading with Cuba is blatantly extraterritorial. Accordingly, the Governments of Canada and the United Kingdom invoked their blocking legislation on 9 and 14 October 1992 respectively to counter the extraterritorial scope of the CDA and to protect the trading interests of their companies.

The opposition of the European Community to the CDA was made clear on many occasions without success and in a final demarche to the Department of State on 7 October 1992, urging the President to veto the CDA. The EC has also noted the threat expressed by the US Government to prohibit, under

the **Food Security Act** and the TWEA, EC imports of certain sugar products into the US, should these products be derived from Cuban sugar.

It is generally recognized that the extraterritorial application of US laws and regulations, where it exposes foreign-incorporated companies to conflicting legal requirements, may have a serious effect on international trade and investment. Moreover, in many instances the extraterritorial application of certain laws implies an intention to replace the laws or fundamental policy of an international entity or another country, such as the European Community and its Member States, within its own territory, by the policy or laws of the US. This is clearly contrary to international law. Accordingly, many close trading partners of the US, such as Canada and certain Member States of the EC, have "blocking statutes" in order to preclude the extraterritorial application of foreign legislation within their own territory.

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

C. *Marine Mammal Protection Act*

The US **Marine Mammal Protection Act** (MMPA) of 1972, as amended, aims at protecting marine mammals, particularly dolphins. The Act progressively reduces the acceptable level of dolphin mortality in US tuna-fishing operations in the Eastern Tropical Pacific Ocean and provides for sanctions to be taken against other countries which fail to apply similar standards for dolphin protection. "Primary" embargoes are currently being applied to imports of certain yellowfin tuna products from Mexico, Venezuela, Colombia and Panama. "Secondary" embargoes on yellowfin tuna products are imposed on imports from "intermediary nations" - countries which have failed to certify that they have not imported from the primary embargoed countries during the preceding six months and which are exporting to the USA.

The **International Dolphin Conservation Act** of 1992 amended the MMPA and authorises the Secretary of State to enter into international agreements which establish a moratorium (from 1 March 1994) on certain "dolphin-hostile" tuna-harvesting practices. Should such a moratorium be agreed but not implemented, the Act provides for a mandatory ban on 40% of US imports of fish products from the country concerned. From 1 June 1994, the US may also impose an import ban on all tuna products considered not to be "dolphin-safe".

Italy and Spain are the only Community countries currently subject to a secondary embargo. The value of frozen yellowfin tuna exports concerned by the embargoes was estimated at some ECU 5.5 million in 1991. These embargoes have had a negative impact on the image of Community products and have contributed towards disturbance of the Community tuna market.

The Community shares the declared aim of the MMPA, but believes that any measures for the conservation of living resources, including dolphins, should be achieved by cooperation at international level as in the context

of other multilateral organisations. Trade measures of a unilateral nature taken for environmental reasons should be avoided in favour of multilaterally agreed measures. The Community is against measures which are both unilateral in nature and have elements of extraterritoriality, such as those seen in the US legislation. It believes that multilateral cooperation leading to internationally agreed rules is the preferable option to follow.

A GATT Panel has reported on the terms of the MMPA at the request of Mexico as a primary-embargoed country. The Panel considered that the US practices were not in conformity with the GATT articles III and XI and that the GATT-illegal and unilateral trade elements of the MMPA should be repealed. The Community fully agrees with this analysis along with most GATT Contracting Parties, however, the report of the Panel has not yet been adopted. Consultations with the US have taken place, but have failed to produce agreement. Therefore, the Community has now requested the establishment of its own Panel in the GATT. Following this request, Panel proceedings are now under way.

D. *Other fisheries related legislation*

The **Magnuson Fishery Conservation and Management Act** (MFCMA) of 1983 was re-authorised in 1990 with a resulting impact on international fisheries matters. The amended Act proposes that the US apply a number of unilateral measures to its partners with which it has **Governing International Fisheries Agreements** (GIFA) on the high seas. The measures include the right for the US authorities to know the whereabouts of driftnet vessels beyond their exclusive economic zone, to board and inspect those vessels and to have on-board observers.

Amendments also require the Department of Commerce to list nations, the nationals of which engage in large-scale driftnet fishing in a manner unacceptable to the US authorities. Such a nation may be certified for the purposes of the so-called "Pelly Amendment" and its marine products may be consequently embargoed.

From 1 July 1991, the US introduced a compulsory system of Certificates of Origin for certain fish caught in the Southern Pacific and from other sources from 1 July 1992. The certificates are applied for a number of types of tuna products as well as other species including shark, salmon, squid and swordfish. Certification rules are also applied for countries using large-scale trawl nets. These rules may be considered to be a serious obstacle for Community exporters.

The **High Seas Driftnet Fisheries Enforcement Act** (HDFEA) of 1992 allows for an exceptional derogation until 1 January 1994 to the list of nations engaged in large-scale driftnet fishing, in particular for Community vessels fishing in the Northeast Atlantic Ocean. This does not preclude the possibility of Member States being faced with an embargo at a later date.

Each year, the US fixes the TALFF (total allowable level of foreign fishing) and accordingly makes allocations to foreign fishing fleets. Squid fishing possibilities for Community vessels off the east coast of

the USA have been gradually phased out under the terms of both the MFCMA and the GIFA in favour of the development of the US domestic fishing industry. Though mackerel migrating off the east coast is the only stock currently identified as being in surplus in the US Exclusive Economic Zone (EEZ), the US authorities have proposed a zero TALFF for both 1993 and 1994 for this stock following pressure from the domestic industry to protect its markets. The Community believes that this line neither corresponds to the provisions and intentions of the MFCMA nor to the provisions of Article 62 of the **UN Convention on the Law of the Sea**. More specifically, it does not correspond to the terms of the GIFA.

The Community acknowledges the entitlement of the US to link access to living resources in its EEZ to certain conditions. The US administration has declared its intention of using some of the new Congressional directives as advisory guidelines for relations with other countries stressing its preference for using international cooperation to achieve the aims set out by Congress. There seems to be a tendency, however, to use US measures (such as the definition of large driftnets) as benchmarks of other countries' policies with the possibility of sanctioning accordingly. No matter how well-founded are the US objectives, their actions should be based upon international cooperation. Otherwise, unilateral measures may be out of proportion with the objective of conservation and destabilising for international trade.

4. IMPEDIMENTS THROUGH NATIONAL SECURITY CONSIDERATIONS

A. *General remarks*

Under existing multilateral instruments (GATT) or bilateral instruments (Friendship, Commerce and Navigation Treaties), sovereign nations have reserved their rights to take any measure to protect their essential national security interests. In the context of OECD's National Treatment Instrument and the Codes of Liberalisation, however, there is a continued interest in the limited and prudent use of such measures.

The US has always been at the forefront of nations in developing national trade laws and regulations to implement and enforce both foreign policy and national security policy objectives. Thus, US trade legislation includes various provisions which refer to national security considerations to justify restrictions on foreign imports, procurement, exports or investment. In his Trade Policy Report to Congress on 3 March 1993, the US Trade Representative reinforced this position, indicating that the US will no longer automatically subordinate its economic interest to foreign policy or defence concerns. Rather, the national security of the US is closely bound up with economic strength at home.

The EC is concerned that such justifications will be employed in areas where there is no significant threat to national security but where employment or industrial policies are implemented to the detriment of free trade objectives.

B. *Import restrictions*

On grounds of national security, the US may restrict imports from third countries. Such restrictions are triggered by US industry petitions under Section 232 of the **Trade Expansion Act** of 1962. Protective measures can be taken for an unlimited period of time.

The Department of Commerce investigates the effects of imports which threaten to impair national security either by quantity or by circumstances. The purpose of Section 232 is supposed to be to safeguard the US national security, not the economic welfare of any company, except when that company's future may indeed affect US national security. The application of Section 232 is not dependent on proof of injury to US industry.

In the past, the EC has voiced its concern that Section 232 gives US manufacturers an opportunity to seek protection on grounds of national security, when in reality the aim is simply to curb foreign competition.

An example of this is the Voluntary Restraint Agreement (VRA) with Japan and Taiwan on machine tools which has been extended through the end of 1993 for "high tech" machine toods. It was announced that if during the phase out period imports from major machine tool supplier countries were capturing an increased US market share as to undermine the integrity of the US machine tool revitalization program, the US Government would consider taking appropriate remedial action.

C. *Procurement restrictions*

Procurement by the Department of Defense (DoD) is considered as one means of addressing the issue of the maintenance of an industrial base capable of meeting national security requirements. According to the 1991 DoD Report to Congress on the Defense Industrial Base, "national security includes economic security and requires that DoD have an assured and reliable source of supply of defense material in peace time, crisis, and war, in an era of declining budgets and increasing of defense markets".

Although the concept of national security may be invoked under Article VIII of the GATT Procurement Code to deny national treatment to foreign suppliers, the use of national security consideration by the US has led in practice to an unjustified substantial reduction in the amount of DoD supplies covered by the GATT Public Procurement Code.

The concept of "national security" was originally used in the 1941 Defense Appropriation Act to restrict procurement by the DoD to US sourcing. It is recalled as the **Berry Amendment** and has been used ever since in DOD Appropriations legislation as a means for restricting to US suppliers DoD procurement of a wide range of products.

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 outside the US are in support of combat operations; or are by vessels in foreign waters, or are emergency procurements or procurements of perishables by establishments outside the US;
- speciality 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.

Further procurement restrictions are based on the **National Security Act** of 1947 and the **Defense Production Act** of 1950 which grant authority to the President and the Secretary of Defense to impose restrictions on foreign supplies to preserve the industrial mobilisation base and the overall

preparedness of the US. Moreover, Congress can also adopt additional Buy American restrictions based on national security considerations. Thus, each year the Department of Defense Authorization and Appropriation Acts sets additional Buy American requirements for the Department of Defense.

Contrary to this, Canada is granted national treatment, since it is considered as part of the North American mobilisation sphere.

US Allies have concluded with the US various cooperative industrial defense agreements or reciprocal procurement agreements (MOUs) including certain EC countries (UK/1975, France/1978, Germany/1978, Italy/1978, Netherlands/1978, Portugal/1978, Belgium/1979, Denmark/1980, Luxembourg/1982, Spain/1982, Greece/1986). These agreements should provide for a blanket waiver of the Buy American Act by the Secretary of Defense with respect to products produced by the Allies, and they should promote more efficient cooperation in research, development and production of defence equipment and achieve greater rationalisation, standardisation, and interoperability. However, the US Administration (DoD and USTR) can determine the standing of an Ally with respect to its discrimination against US products under the bilateral agreements and rescind the blanket waiver of the Buy American Act. In addition, Congress is unilaterally modifying the coverage of MOUs by imposing the Buy American preference as a norm superior to the MOU itself. According to EC industry sources, there are indications that US procuring officers disregard the exemption of Buy American restrictions for MOU countries, eg. in the case of fuel-cells and steel forging items.

The criteria for the Department of Defense procurement of dual-use products which was introduced into the **Department of Defense Authorisation Act** for Fiscal Year 1992-1993 create new additional uncertainties as to which areas the US considers to be covered by the GATT Procurement Code and which are subject to the national security exemptions. Furthermore, under this legislation, Department of Defense procurement of dual-use products will only be opened to "eligible firms", as determined by the Secretary of Commerce on the basis of three criteria, namely a significant level of US - based activities, US majority-ownership, and reciprocity with countries and firms associated in cooperative agreements with the US. This has consequences both for procurement and for the application of national treatment in respect of production of goods which are otherwise sold commercially.

A non exhaustive list of goods for which US procurement restrictions exist on grounds of national security considerations is given below :

* Fibers and synthetic fibers
* Coal and coke for use by the American forces in Europe
* Hand and measuring tools
* Supercomputers for the US Army
* Circuit breakers
* Valves and machine-tools
* Carbon fibres
* Naval vessels and coastguard vessels
* High-carbon ferrochrome
* Forging items
* Stainless steel and speciality metals
* Supply of anchor and mooring chains
* Ball and roller bearings
* Fuel cells for aircraft

A Department of Defense report to Congress in 1989 considered that many of the procurement restrictions "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 fulfil the domestic objective of maintaining an essential US industrial base. The Department of Defense therefore concluded that in many cases, restrictions should be terminated and Congress should instead support a Domestic Action Plan or National Stockpiling Programs.

According to the Department of Defense, the main arguments against procurement restrictions are that

- 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 lead-times 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 MOUs.

In a 1991 report to Congress about the US defence industrial base, the Department of Defense recognises that "*when it is in the national interest, many products used by the Department of Defense are purchased from foreign sources - for example, when foreign goods provide performance, cost, or quality advantages or further the goal of commonality with Allies*". Furthermore, the Department of Defense admits that "*overseas sources are a vital asset to our (US) national defense and help to strengthen the national security; however, there may be occasion when excessive reliance on a single overseas source potentially could lead to unacceptable risks to the continuity of supply ... Findings to date indicate that although foreign vulnerabilities are potentially of great concern to the Department of Defense, they represent an exceedingly small proportion of the items that are foreign-sourced today*". Nevertheless, the Department of Defense notes that the "*US Buy America prevents foreign suppliers from participating in certain aspects of US defense contracts*". Thus, the US enjoy a defence trade surplus with the Community.

The Community agrees with the point of view that the changing defence balance in the West and the deepening of the US/EC relationship should allow for a rethinking of access to Department of Defense procurements or programmes. During the Uruguay Round multilateral negotiations, in the Market Access Group - tariff and non-tariff measures - and in the Procurement Informal Negotiating Group, the EC requested that the US eliminate Buy American restrictions applicable to broad categories of products regardless of their relation with defence issues. The US denied that there was any abuse of the security exemption included in the General Agreement and the Procurement Code. The US recalled that these restrictions had been notified but that they were not tabled for negotiation.

D. *Export restrictions*

The US has established, under the **Export Administration Act** of 1979 (EAA), and continued under the **International Economic Emergency Powers Act** of 1977 a comprehensive system of export controls, with a view to preventing trade to unauthorised destinations. This system is also used to enforce US foreign policy decisions and international agreements on non-proliferation of certain types of goods or know-how.

The Member States of the EC have their own export control systems and cooperate with the US in the COCOM. This makes the extraterritorial characteristics of the EEA mentioned in Chapter 3.A. as well as the **Arms Export Control Act** above all the more inappropriate. Furthermore, the EC has in the past expressed its concern with regard to the unilateral determination made by the US concerning export licences for products made in the EC (Siberian pipeline case of 1982). The Community has in particular protested against the US considering subsidiaries of US companies incorporated in the European Community as US companies and as such subjecting them to US jurisdiction for actions within the Community.

In the context of export controls, the US have shown some interest in a working-level exchange of information with the Commission, since the latter is in the process of launching a common export control regime. Likewise, the US and the Member States of the EC are taking part in "non-proliferation" treaties, such as nuclear non-proliferation, chemical and biological, warfare non-proliferation, and missile technology non-proliferation.

E. *Investment restrictions*

The US restricts foreign investments or foreign ownership in certain economic sectors, deemed to be essential to US national security. An overview of investment restrictions is given in Chapter 12.

5. PUBLIC PROCUREMENT

A. *General Remarks*

Discriminatory government procurement provisions known as "Buy American" are implemented in the US at Federal, State and lower levels. Under the US doctrine of international trade law, the domestic law, such as the Buy American Act of 1933, overrides US international obligations. The practical application of this principle means that Buy American provisions apply unless waived in response to specific international obligations of the US, such as the Government Procurement Agreement. The net result of the continuing amendments to the Buy American Act is a lack of transparency and predictability in the implementation of US obligations under the GATT.

Buy American restrictions may take several forms. Some straightforwardly prohibit public sector bodies from purchasing goods from foreign suppliers. Others establish local content requirements ranging from 50% to 65%, while others still extend preferential terms to domestic suppliers, the price preference ranging anywhere from 6% to 50%.

As is usual every year, the US Congress enacted in 1992 a number of ad hoc Buy American provisions when adopting the budget of the different Federal departments and agencies. These provisions extend the scope of the Buy American Act of 1933 as amended and affect primarely products/sectors not covered by the GATT Procurement Code - such as transportation and defence. In the case of defence, they represent unilateral changes to the Memoranda of Understanding signed in the defence cooperation field (MOU) between foreign governments and the US Administration (see Chapter 4.C.).

In 1992, two demarches were presented to the US Department of State and the Department of Defense on Buy American provisions related to the procurement of ball bearings and fuel cells by the Department of Defense. Of these two provisions, the one relating to ball bearings was kept in the Department of Defense Authorization Act. Although the other relating to fuel cells was dropped, the House-Senate Conference on the Department of Defense Authorization Bill for FY 1993 directed the DoD to procure US-manufactured synthetic fabric fuel cells.

The European Community has repeatedly expressed its deep concern about the continuation of and the increase in Buy American provisions. The opportunity provided by the Uruguay Round multilateral trade negotiations ought to lead to an elimination of the US discriminatory procurement practices at federal and state level. The European Community will continue, on a case by case basis, its analysis of Buy American provisions and pursue these matters in the framework of the GATT through consultations and panels, in order to achieve a narrow interpretation of article VIII of the GATT Government Procurement Code. Moreover, the

European Community will also continue to urge the US Government to adopt the GATT panel report on the procurement of a sonar mapping system by the National Science Foundation. This case showed that the US Government had violated its GATT obligations by applying a Buy American provision to its procurement. All parties, except the United States, have agreed to the conclusion of the panel report.

B. Buy American legislation at Federal level

1. Basic legislation

The **Buy American Act** (BAA) of 1933 as amended, sets up the basic principles of a general buy national policy. It applies to government supply and construction contracts and requires that Federal agencies procure only domestically unmanufactured supplies for public use which have been mined or produced in the US and only manufactured goods with a substantial local content of a minimum of 50% as defined by the **Executive Order 10582 of 1954**. In the construction, alteration, and repair of public buildings and public works only domestic materials shall be used.

The **Executive Order** 10582 of 1954, as amended, expands the scope of the Buy American Act in order to allow procuring entities to set aside procurement for small business and firms in labour surplus areas, and to reject foreign bids either for national interest reasons or national security reasons.

Exemption from the Buy American Act is provided for public interest reasons. Furthermore, the Buy American obligations do not apply to the procurement of goods to be used outside the US territory, to goods which are not available on the domestic market and to goods whose cost is determined to be unreasonable. Whereas the Executive Order of 1954 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.

Beside the Buy American Act, Buy American restrictions are also contained in:

- the **National Security Act of 1947** and the Defense Production Act of 1950, which grant authority to the President and the Secretary of Defense to impose restrictions on foreign supplies to preserve the domestic mobilisation base and the overall preparedness posture of the US. These restrictions are "justified" on the grounds of national security, although in most cases the issue is not the achievement of defense objectives but the protection of US industry (see chapter 4.C.);

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

- the **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 mobilisation objectives.

Furthermore, each year the US Congress adopts some ad hoc Buy America provisions as part of the **Budget Authorizations and/or Appropriations legislation**. By this, price preferences can rise from a standard 6% up to 10-25%, notably in the following utilities sectors: water, transport (mass transit, airport and highway construction), energy, and telecommunications.

The application of the Buy American legislation may be waived in order to give a preferential or less favourable treatment for certain countries, for example on the basis of the **Trade Agreements Act** of 1979 in the case of Free Trade Agreements signed by the United States with Canada, Israël and Mexico. Moreover, until recently, it was generally assumed that the Memorandum of Understanding signed between the US Department of Defense and the Department of Defense of a third country in defence cooperation constituted a waiver from the application of the Buy American legislation. However, ad hoc legislation adopted by Congress under the Department of Defense Appropriation Acts for FY 1992 and 1993 apparently override the preferential provisions of MOUs (see already Chapter 4.C.).

2. Indicative list of Buy American provisions at Federal level

a. Defence Sector

In 1992, the following Buy American provisions were adopted for the defence sector. Title IX of the **Defense Appropriation Act for Fiscal Year 1993** contains a series of restrictive provisions:

- The Berry Amendment is made permanent. It implements a Buy America clause on food, tents, clothing, certain textiles, stainless metals, including stainless steel flatware and handtools;
- for 120 mm mortars or ammunitions manufactured outside the US;
- for anchors, mooring chains 4 inches or less in diameter;
- for multibeam sonar mapping systems;
- for carbon, alloy or armour steel plate;
- for shipboard components for sealift ships;
- for 4 ton dolly jack;
- for high purity quartz yarn or fibre and finished products;
- for coals for use at US defense facilites in Europe when US coal is available;
- for 75% of US requirement of coal and petroleum pitch carbon fiber to be procured from US sources by 1994;
- for carbonyl iron powders contained in any system or item.

The Department of Defense **Authorization Act for Fiscal Year 1993** contains three Buy American provisions:

- for ball bearings and roller bearings: this limitation extends the current Buy American requirement for another three years until fiscal year 1995;
- for sonobuoys: a waiver can be granted considering national security interests;
- for shipboard components for sealift ships and major ship propulsion systems and components. There is already a Buy American provision on the procurement of systems as a whole;
- although the final text of the Act has not maintained a Buy American provision on fuel cells, the House- Senate conference nevertheless "directed the Department of Defense to abide by the Berry amendment in its purchases of synthetic fabric fuel cells".

b. Transport Sector

The **Airport and Airway Safety, Capacity, Noise Improvement and Intermodal Transportation Act** of 1992 extends for the fiscal year 1993 the authorizations for the Federal Aviation Administration (FAA) and the attendant Buy American provisions, notably a 25% price preference for US steel and manufactured products with respect to funds for FAA operations, FAA equipments and facilities, and with respect to grants to airports.

c. Utilities and public works sector

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.

According to the **Surface Transportation Assistance Act** of 1978 (STAA) US States must meet several requirements to receive federal funds from the Urban Mass Transport Administration. Firstly, the State must certify that its laws, regulations and directives are adequate to accomplish the objectives of Section 165 of STAA. Secondly, standard specifications in contracts must favour US supplies. Finally, steel must have been manufactured in the US. Non-compliance of States with the provisions of Section 165 of the STAA is sanctioned by an obligation to repay any federal appropriation used in a violating contract (**Federal Claims Collection Act of 1986**).

The STAA is applied to mass transit equipment (rolling stock and other). It requires that for all contracts, the local transit authorities give a 25% preference to bidders supplying US equipment, which for contracts entered into on or after 1 October 1991 must have a local content of 60%. In addition, final assembly of the vehicles must have been carried out in the US.

The domestic content requirement was in 1987 also extended to subcomponents. Waivers for products or subcomponents may be granted by the Urban Mass Transportation Administration, when the use of domestic suppliers will prove uneconomical and will result in unreasonable costs.

These Buy American provisions also apply to federally assisted programmes and contracts awarded by the Federal Aviation Administration and the Federal Highway Administration.

The **Amtrak Improvement Act** of 1978 and successive 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 United States within a reasonable time.

The **Intermodal Surface Transportation Efficiency Act** of 1991 (ISTEA) defines the US national policy for intermodal transport, which includes a national highway system and arterial roads essential for international interstate and regional commerce, travel, national defence, intermodal transfer facilities, etc. The ISTEA extends to iron products the existing Buy American restriction on steel (see above). Furthermore, it reserves not less than 10% of the total appropriations to US small business and disadvantaged business. Under Section 1048, it also provides for trade sanctions against a foreign country, which has violated, as determined by the Secretary for Transport (in consultation with the USTR), either an agreement in respect of transport activities or one in respect of products covered by ISTEA, or which is considered to have discriminated against US suppliers.

d. Telecommunications sector

Telecommunications equipment is at present excluded from the GATT Procurement Code - apart from the inclusion of NTT of Japan - but examination of a possible extention to this sector has been taking place for a number of years. Negotiations on telecommunications have been held up because of the difficulty in coming to an agreement on which particular utilities should be included. In the view of the Community, the criteria for inclusion of entities should be based not on the distinction between public and private companies, but on the identification of underlying conditions which lead entities in the telecommunications sector to pursue procurement policies that tend to favour particular national suppliers. These conditions include, firstly, insulation from market forces through the possession of a monopoly or a dominant position over a network, or through the possession of special rights relating to the management of the network; and, secondly, the means which government may use to influence the operations of an entity, such as regulation of tariffs and financing, or authorisation to operate. Thus the Community view is that both publicly-owned and private-status utilities operating under monopoly or dominant conditions should be covered under GATT procurement procedures. This will introduce a high level of transparency and will lead to improved market access. Currently European manufacturing companies, which are competitive on the world market, face great difficulties in the US market where operating companies have historically bought equipment from local suppliers, and where AT&T buys network equipment almost exclusively from itself.

Community companies' access to the US network equipment market is impeded by a variety of factors, such as the lack of 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 ability of the Federal Communications Commission (FCC) and of State Public Utility Commissions (PUCs) to influence the procurement practices of these utilities, and the effect of a US standardisation policy which is not closely linked to international standards.

AT&T (the dominant long-distance carrier) and GTE (a provider of local services) also manufacture equipment (although GTE is leaving the market by way of a joint venture with AT&T), and, as vertically integrated companies, have little incentive to buy competitively. These companies are far better placed than outside companies to supply their own networks; in practice they buy most of their equipment from themselves. AT&T also benefits from advantages, including 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, 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 non-discriminatory in the sense of not favouring AT&T above other suppliers. However, these procedures fall short of those set out in the EC directive on procurement. Notably, the procurement process followed by the 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.

In addition, 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.

The RBOCs enjoy monopolies on provision of basic services in their areas of operation, and they are subject to regulation in a number of different ways. Under S.214 of the 1934 **Communications Act**, the FCC must authorise the construction of new lines for all carriers, including RBOCs. It also regulates inter-state tariffs through price caps. Intra-state communications are regulated by the local State Public Utility Commissions (PUCs) whose administration of price-setting involves them in all aspects of the 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 significant 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 could apply to their procurement also.

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).

Draft legislation tabled in Congress in 1990, 1991 and 1992 would explicitly impose local content requirements on BOC procurement. Any such legislation is being closely monitored by the Community.

C. *Set aside for small business*

The Small Business Act of 1953, as amended, requires executive agencies to place a fair proportion of their purchases with small business concerns, defined as business located in the United States which makes a significant contribution to the US economy and is not dominant. Currently, the concept of fair proportion means that the Government-wide goal for participation by small business shall be established at no less than 20% of the total value of all prime contract awards for each fiscal year. Moreover, each executive agency shall have an annual goal, which is currently 10% for the Department of Defense, and 5% for other agencies. Under the normal bid procedures, there is a 12% preference for small business in bid evaluation for civilian agencies (instead of the standard 6%). In the case of the Department of Defense, the standard 50% preference applies to all US businesses offering a US product.

The GATT Code contains a US reservation indicating that it does not apply to small and minority businesses set asides.

D. *Buy American provisions at state level*

The Buy American legislation specifies that any purchase funded in whole or in part with federal money is subject to the requirements of the Buy American Act of 1933. Thus, purchases carried out by state or local government bodies using or including federal funds are thereby subject to Buy American requirements. For example, the multi annual Appropriation Act of the Federal Department of Transport (Surface Transportation Act of 1978 and successive legislation) contains Buy American requirements for State highway and urban mass transportation projects (see Chapter 5.B.2.c.).

Legislation in at least 40 States provides for Buy American restrictions on their procurement. Many of the States' requirements concern purchases of steel used for construction and infrastructure work and are applicable not only to the public purchaser, but also to private contractors and subcontractors, in accordance with the basic principles of the Buy American Act of 1933. For example, Buy American restrictions on steel are implemented by the states of Illinois, Maryland, New York, Pensylvania, Rhode Island and West Virginia. In public work projects New Jersey legislation requires that only domestic materials such as US cement may be used.

E. *Economic impact of Buy American legislation*

US procurement at Federal level totals approximately $210 billion annually. The value of US procurement covered by the GATT Code as reported by the US has declined from $18.8 billion of SDR in 1985 to $13.1 billion of SDR in 1990, whereas the contracts below the thresholds

and falling outside the Code have increased over the same period. It is clear that the potential US market for Community exports is significantly affected by the Buy American restrictions. 60% of Federal government procurement in the United States is by the Department of Defense and is largely outside the GATT Code. On the other hand, the important states and municipalities have procurement potential in tradeable products. US statistics show that State spending represents more than 70% of total US public procurements.

According to figures of the Federal Procurement Data Centre, small and disadvantaged businesses are currently obtaining approximately 20% of total Federal procurement. (For FY 1991 these percentages include direct contracts and subcontracting.)

6. TARIFFS AND EQUIVALENT MEASURES

A. *Tariff problems*

1. High tariffs and tariff peaks

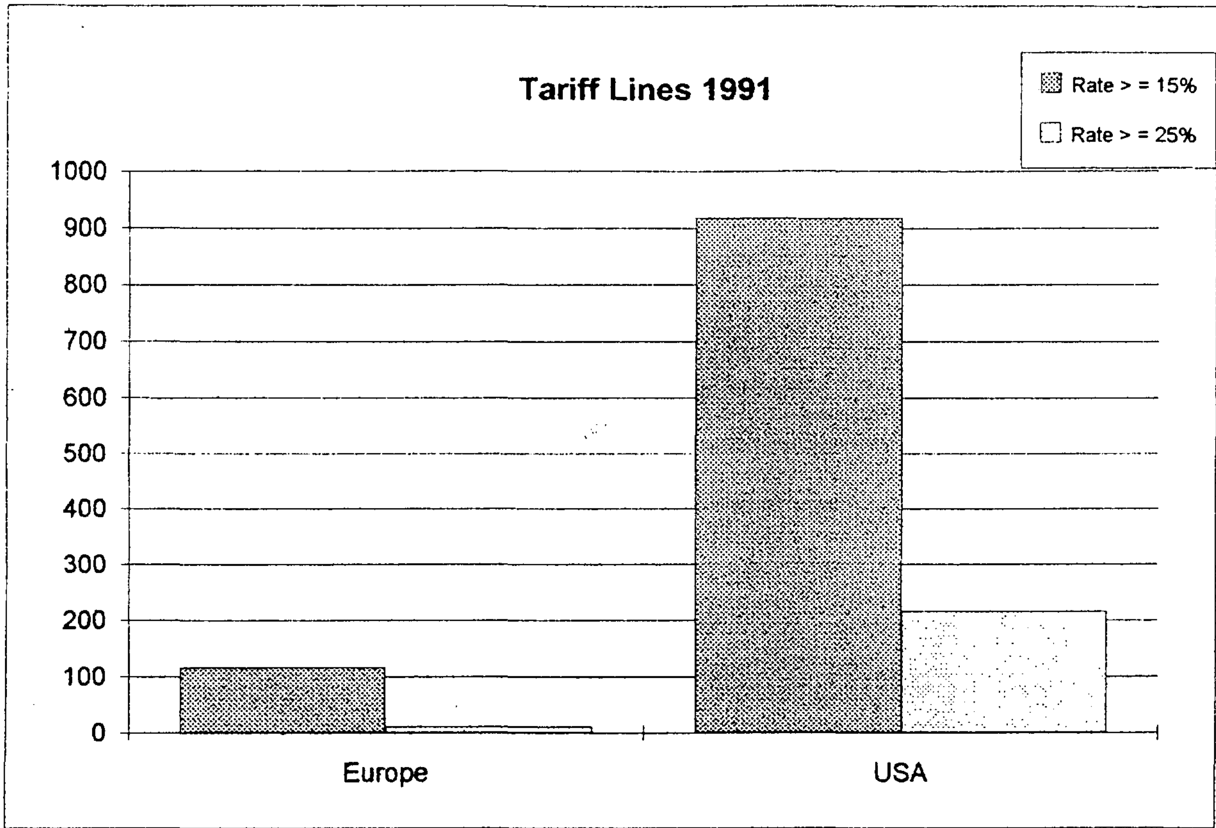
Numerous products exported from the EC are subject to high US tariffs. Certain textile articles, ceramics, tableware, glassware, vegetables and footwear are all subject to tariffs of 20% or more. The following examples illustrate high US tariffs which reduce market access possibilities for EC products *(the corresponding EC tariff rates are in brackets; the numbers in square brackets refer to US tariff codes included in the table on page 38) :*

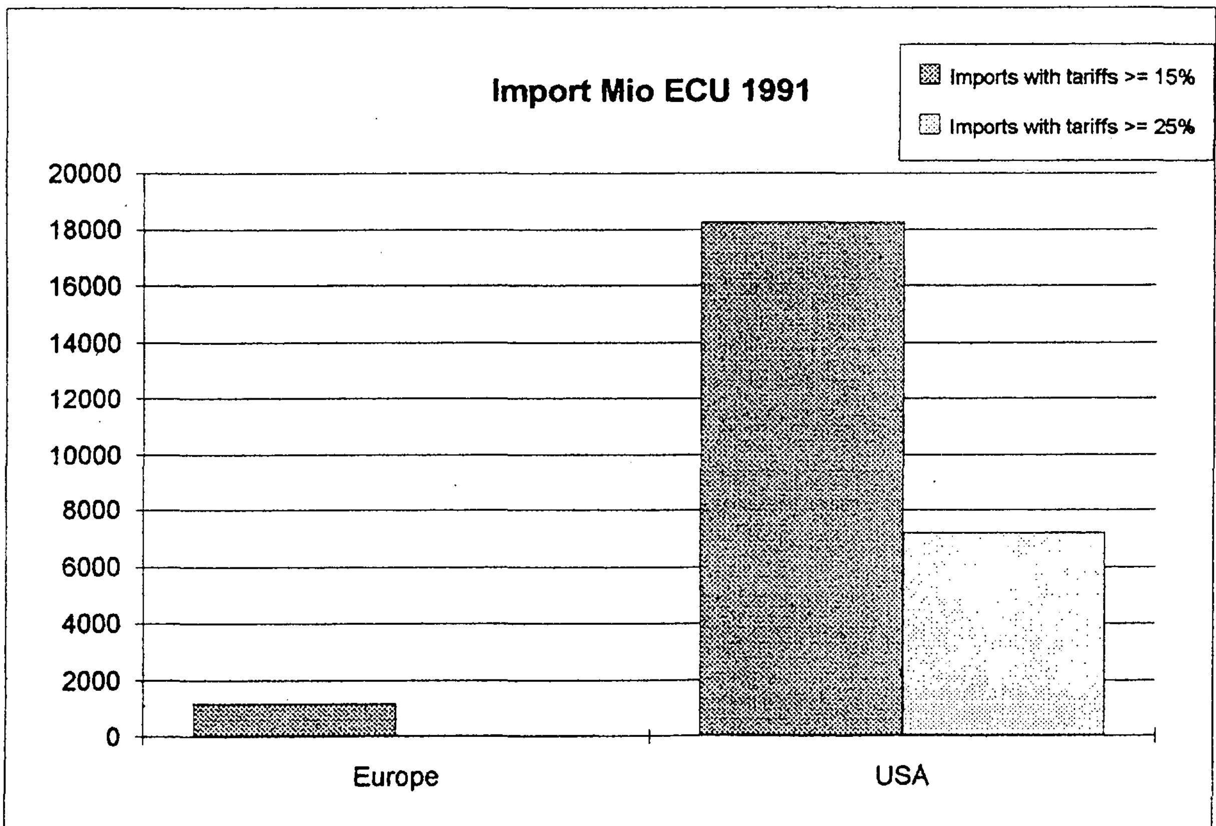
Certain clothing (1)	*20-34.6% (13-14%)*
including soccer uniform and warm ups	*35%*
Silk and MMF/woollen-blended fabrics (2)	*38% + 48.5 cents/kg (3-7.5% and 11%)*
Ceramic tiles, etc. (3)	*20% (8-9%)*
Certain tableware (4)	*26-35% (5.1-13.5%)*
including hotel porcelain dinnerware	*35%*
Certain glassware (5)	*20-38% (12%)*
Certain footwear (6)	*37.5-48% (4.6, 5.8, 20%)*
Garlic and dried or dehydrated onions(7)	*35% (16%)*
Zinc alloys (8)	*19% + 48.5 cents/kg (3.5%)*
Certain synthetic organic colouring matter(9)	*20% (10 %)*

Tariff reductions on these products would significantly increase the competitiveness of EC firms in 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.

2. Tariff Reclassifications

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.


Tariff Lines 1991
Rate > = 15%
Rate > = 25%
1000
900
800
700
600
500
400
300
200
100
0
Europe
USA


Import Mio ECU 1991
Imports with tariffs >= 15%
Imports with tariffs >= 25%
20000
18000
16000
14000
12000
10000
8000
6000
4000
2000
0
Europe
USA

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 (10) 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 from classification by chief value to classification by chief weight of fabric. In addition, US tariffs for certain wool-blended tapestry (11) 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% (12).

Duties on some **marbles**, in particular on "ivory cream marbles" (13) have increased from 2.8% to 6%. The type of Spanish marble known as "Crema marfil" marble, was formerly classified under the TSUSA tariff classification as "marble; slabs; rubbed; or polished in whole or in part" (item 514.65), subject to an ad valorem tariff of 2.8%. In the new harmonized classification (HTSUS, Harmonized Tariff Schedule of the United Sates), the US customs authorities have classified this marble under item 68.02.92.00, "other calcareous stones", with a tariff of 6%.

The new classifications of **gaskets** and gaskets material (14) and red dye (15) 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% (16).

According to a Treasury Department ruling of 1989, **multi-purpose vehicles** remain to be classified under heading 87.03 of the Harmonised System, that is "motor vehicles designed for the transport of persons", provided that they contain four doors. Thus, effectively two-door multi-purpose vehicles are classified as trucks under HTS heading 87.04, which are subject to a tariff of 25%, while four-door vehicles are treated as cars, subject to a tariff of 2.5%.

With the Miscellaneous Tariff Act of 1992, also four-door multi-purpose vehicles would have been reclassified as trucks, subject to a 25% duty. However, the Act has not passed Congress. Nevertheless, in the beginning of 1993, there have anew been activities to bring about a reclassification of four-door multi-purpose vehicles.

The criterion of the number of side-doors is inadequate for the classification of multipurpose vehicles. With the exception of the US, this is recognised by all members of the Customs Cooperate Council (CCC), whose Harmonised System Committee has on several occasions expressed the view that the classification cannot be made on the basis of criteria related to the number of doors.

A unilateral change of classification of multipurpose vehicles from category 87.03 to 87.04 of the Harmonized System would consitute a violation of the United States obligations under Article II of the GATT, since it would have the effect of raising the bound tariff for the affected category of vehicles from 2.5% to 25%. Under GATT rules, if the EC were adversely affected, the United States would be subject to demands for compensation, which it would be obliged to grant. In addition, a

unilateral change of classification of multipurpose vehicles would also be an infringement of the United States' obligations under Articles 3 and 8 of the International Convention on the Harmonized Commodity Description and Coding System.

Since August 1992 US customs services have been reclassifying certain empty glass **perfume bottles** made for spray under HTS headings 7013.99.50 and 7013.39.20.00 thus submitting imports to a tariff rate of 30% rather than 3.7% due under the old classification.

SELECTED US TARIFF CODES BASED ON THE HARMONIZED SYSTEM (HS)				
(1)	*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*		
	55.15.1305			
	2205			
(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)	*32.04.1150*	*32.04.1425*	*32.04.1650*	
	1250	*1450*	*1750*	
	1325	*1530*	*1919*	
	1350	*1550*	*1950*	
(10)	*51.11.1160*	*51.12.1100*	*54.07.9105*	
	1960	*1960*	*54.08.3205*	
	2060	*2000*	*3305*	
	3060	*3000*		
	9060	*9060*		
(11)	*51.11.2060*	*51.11.9060*		
	3060	*51.12.1960*		
(12)	*59.05.0090*			
(13)	*68.02.9200*			
(14)	*45.04.90.20*	*45.04.10.50*		
(15)	*32.05.00.10*			
(16)	*17.04.90.40*			

Such duty increases are not justified and as in the case of the new tariff reclassifications contravene the agreed GATT guidelines for transposition to the HS. 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 : as extra duties on wool-woven fabrics and wool/silk blends, mainly supplied by the EC, amounted to approximately US$ 1.02 million in 1991.

3. **Tariff Suspensions**

On 31 December 1992 most of the provisions contained in Chapter 99, Subchapter II of the US Harmonized Tariff Schedule expired, thereby reverting the duty rates for a substantial number of agricultural and industrial products to the applicable most favoured nation rates.

A proposal for the extension of the duty suspensions was included in the **Miscellaneous Tariff Bill**, which was introduced in 1992, but was not passed by the 102nd Congress. There currently appear to be no plans to introduce legislation to renew the duty suspensions during the 103rd Congress. The EC has requested a renewal. While recognising that the US is under no obligation to provide one, such a move would assist companies both in the EC and US in that it offers a permanent system which would remove uncertainty in the trade.

The estimated total volume of imports from the EC of products covered by Chapter 99, Subchapter II amounts to US $1.27 billion. With some of the currently applicable duties being as high as 38%, the economic impact of the expiry is considerable.

B. Fees

1. **General remarks**

As a result of laws enacted in 1985 and 1986, the Unites 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 1990 and the **Omnibus Budget Reconciliation Act** of 1990 extend and modify these provisions, among other things, by considerably increasing the level of the fees. This legislation demonstrates a 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.

2. **Customs User Fee**

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 Recovery Act and the Andean Trade Preference Act, or from United States insular possessions. It is also levied on merchandise entered under Schedule 8, Special Classifications, of the Tariff Schedules

of the United States. In addition, Article 310 of the North American Free Trade Agreement (NAFTA) provides for a removal of the fees for goods originating in the US, Canada or Mexico.

The merchandise processing fee was fixed at 0.17% of the value of the imported goods for 1988 and 1989. The Customs and Trade Act of 1990, effective 1 October 1990, provided a number of modifications to the previous law for one year. The Omnibus Budget Reconciliation Act of October 1990 extended it for five more years, to 30 September 1995. It also provided for the discretionary adjustment of fees. As of 1 October 1992, the Merchandise Processing Fee is 0.19% ad valorem.

The main provisions of the current law as opposed to the pre 1990 situation are:

Current law	Previous law
0.19 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 not Customs prepared, $8 for manual Customs prepared informal entries	no charge on informal entries

It is estimated on the basis of the approximate total value of about $91 billion of US imports from the Community in 1992 that the Merchandise Processing Fee cost the EC approximately $156 million (fees for informal entries not included).

At the request of Canada and 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. 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 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.

3. US Cotton Import Fee

The **Cotton Research and Promotion Act** Amendments of 1990, enacted under the 1990 **Farm Bill** provide, inter alia, for a levy of $1 per bale on imports of cotton and cotton-containing products, in addition to a supplemental assessment of six tenths of one percent of the historical value of the cotton (based on the average price received by US producers of upland cotton).

This import fee does not appear to discriminate, in principle, against foreign producers exporting to the US, as a similar fee is imposed on domestic US producers of raw cotton. However, it may prove discriminatory in practice for two reasons, which were explained to the US Administration.

Firstly, the fee is levied domestically on the production of raw cotton. The administration of this system is relatively straightforward and the administrative costs for companies are likely to be low. However, with regard to imports, the fee is also assessed on cotton content in a large range of cotton-containing products. The **assessment of the fee** for imports is consequently more onerous than for the domestic product and the administrative costs much higher. The reimbursement mechanism for products containing US-produced cotton is also cumbersome and tends to place the cost of administration disproportionately on imports. These high administrative costs, besides being burdensome in themselves, may also have the effect of a non-tariff barrier in discouraging foreign producers from exporting to the US. The European Community is also concerned that the list of imported products upon which this fee is to be levied appears to include a range of products which are classified as containing blends of a high percentage of other textile fibres, for example, many wool garments, sales of which would in no way benefit from measures destined to increase cotton consumption.

Secondly, it is understood that this fee is to be used to fund the **US Cotton Board**. To the extent that the activities of this organisation benefit domestic and foreign cotton equally, there would not appear to be discrimination. However, the European Community is concerned that foreign cotton may not, in fact, receive equitable treatment, especially as one of the express purposes of the Cotton Board, as set out in the Federal Register notice, is "to maintain and expand domestic and foreign markets and uses for US cotton".

The final rule became effective on 10 November 1992. This was unchanged except for the reduction of the rate from 0.6% to 0.5% of the value of

cotton bales or bale equivalent. The EC's concerns were not met. The US Department of Agriculture proposes to raise the rates again in 1995/6.

In summary, the European Community is concerned that the two aspects of the proposed legislation referred to above may amount to de facto discrimination against imports into the US and a non-tariff barrier for foreign exporters of cotton-containing products. The Community has accordingly reserved its GATT rights on this issue.

C. *Quantitative restrictions and import surveillance*

1. Agricultural and Food Import Quotas

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, 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, they restrict EC exports to the US and have a considerable negative effect on world markets. The EC exports potentially most heavily affected by United States quotas are dairy products, cheese and sugar-containing articles. In 1991, for example, total US imports of certain cheeses reached $112 million and US imports of certain sugar-containing products (including certain chocolates) reached $124 million.

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 to interfere with, any United States agricultural programme. Such restrictions are contrary to 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 the annual examination of the waiver in the GATT, the Community together with other Contracting Parties has always insisted that the conditions under which the waiver was granted should be fully respected and that the application of the waiver should be brought to an end. The Community therefore welcomes that the US have accepted in the Uruguay Round negotiations on agriculture to subject the restrictions maintained in the waiver to tariffication.

In this context, attention has to be drawn to the fact that unilateral decisions of the US administration on the application of the cheese import quota in 1988, 1989 and 1991 resulted in a globalisation of certain EC allocations in favour of other third countries. Such decisions are incompatible with the provisions of the 1979 **cheese arrangement** between the EC and US.

2. Excessive Invoicing requirements

Invoice requirements for exporting certain products to the US can be excessive. This is particularly the case for textiles/clothing where

customs formalities include the provision of particularly detailed and voluminous information. Much of this information would appear to be irrelevant for customs or statistical purposes. For example, for garments with an outer shell of more than one construction or material, it is necessary to give the relative weight, percentage values and surface area of each component; for outer shell 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). Furthermore, 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 September 1992, the US Customs Service proposed amendments to the **Customs Regulations**. The proposed amendments are intended to ensure that Customs has sufficient information to determine the tariff classification and admissibility of the merchandise with reference to the numerical scheme and product description contained in the Harmonized Tariff Schedule of the United States.

The new legislation limits the specific and very detailed invoice description requirements in 19 CFR 141.89 (a) Customs Regulations to three groups of merchandise:

- Textile and apparel products which are subject to quotas and visa requirements under the US textile import program;
- Steel and steel products which until 31 March 1992, were subject to voluntary restraint arrangements; and
- Machine tools which until 31 December 1991, were subject to voluntary restraint arrangements.

The information requirements in their amended form are unnecessary and constitute a considerable additional burden on the trade community. They are unnecessary because customs are entitled to ask all supplementary documents and information necessary during clearance (standard 15 of Annex B1 of the **Kyoto Convention**). There should be no systematic demand for this kind of information.

Moreover, as regards textile and apparel products, there is already a system in place, in the context of the MFA, which implies giving very specific information to the administration who hands out these licenses.

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. These formalities are burdensome and costly; they thus also 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.

D. *Measures affecting vessels*

1. General Remarks

The US maintains a variety of measures designed to support its ailing shipping and shipbuilding industry. Apart from the measures identified in the sections which follow, new measures continued throughout last year to be tabled in Congress, such as the **Shipbuilding Trade Reform Act** (HR 2056), the **"Breaux Bill" (S 3192) and the Maritime Reform Act** (HR 5627). These proposals were aimed at eliminating foreign shipyard subsidies and boosting the US merchant marine by enhancing the **US Merchant Marine Act**. However, Congress ended its 1992 session without acting on this shipbuilding legislation.

2. Tax on maritime equipment and repair of ships abroad

The United States applies a 50% ad valorem tax on non-emergency repairs of US owned ships outside the USA and on 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 latter amendment the tax would not apply, under certain conditions, to foreign repairs of "LASH" (Lighter Aboard Ship) barges and spare vessel repair parts or materials.

The direct revenue from the tax on repairs outside the US is estimated at $15-20 million annually, but its effect in terms of loss of activity for European shipyards is much greater. This is evidenced by the fact that the amount of repair work performed outside the US is estimated to be of the order of only $30-40 million.

3. Buy American requirements for certain categories of vessels

The use of certain categories of foreign-built vessels is restricted in the US. This is the case for fishing vessels, vessels used in coastwise trade and special work vessels.

A US flag vessel when foreign-built, cannot be documented for **fisheries** in the US's 200 mile exclusive economic zone. 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.

Foreign-built (or rebuilt) vessels are prohibited from engaging 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 Marine Act** of 1920 -

Jones Act). Moreover, the definition of vessels 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).

No foreign-built vessel can be documented and registered for **dredging, towing** or **salvaging** in the US.

The analysis of EC exports to the US of certain categories of vessels shows the negative impact of US restrictions on EC imports (average for the years 1984 to 1991):

category CN code	average EC exports in 1000 ECUs	
	to the world extra 12	US share %
fishing boats *8902.00.11 + 8902.00.19*	*238,811*	*2.38*
vessels for *towing or pushing* *89.04*	*70,090*	*0.45*
dredgers *8905.10.10 +90*	*54,494*	*0.15*
vessels for the transport *of goods and passengers* *8901.90.10*	*871,949*	*8.57*

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.

4. Subsidies and tax policies

The **Merchant Marine Act** of 1936, as amended, provides for various subsidies schemes or tax deferment measures in the shipbuilding sector which contain domestic build requirements.

Title V of the Merchant Marine Act, provides for a **Construction differential subsidy (CDS)**, a direct Federal grant, for the construction of US-flag merchant ships in US ship yards under Buy American requirements. However, no public source funding seems to have been provided by the Government since 1981.

Section 607 of the Merchant Marine Act, enables US shipowners to defer certain taxable income via the **Capital Constructions Fund (CCF) + Construction Reserve Fund (CRF)** to buy or transform vessels, on condition that they use American material or goods (Buy American) except for fisheries vessels (under the CCF program). Approximately $1.2 billion in funds had accumulated in the CCF as of the end of 1991 and there are 103 fundholders. The CRF fund was $2.5 million in Fiscal Year 1992. This programme has a more limited use as currently there are only 4 fundholders.

Section 601 of the Merchant Marine Act 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 1992, the US authorities distributed in excess of $216 million in funds on old ODS contracts.

Title XI of the Merchant Marine Act, authorizes the US Government to provide direct **Federal Ship Financing 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. As of 30 September 1992, Title XI guarantees in force amounted to just over $2 billion. The guarantees covered 2500 vessels (including 750 barges). In the 1991 fiscal year, 6 applications amounting to $84.76 million were approved. At the beginning of 1993, there were 7 Title XI applications pending.

The Buy American requirements imposed in these different types of subsidies clearly favour US shipbuilders and equipment manufacturers and act as a restriction on 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, unless they can be eliminated through the conclusion of the draft agreement on normal competitive conditions in the shipbuilding and repair sector, on which negotiations in the OECD might restart later this year.

7. EXPORT AND OTHER SUBSIDIES

A. *Export Enhancement Programme (EEP)*

The **Food Security Act** of 1985 required the United States Department of Agriculture (USDA) to use Commodity Credit Corporation stocks to subsidise exports of US wheat 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, barley malt, sorghum, vegetable oils, frozen poultry, pork, eggs, rice, dairy cattle and canned peaches) and for exports to over 40 food-importing countries.

The **1988 Trade Act** extended the programme to 1990 and increased it from $1.5 billion to $2.5 billion. The 1990 **Farm Bill** reinforced the tough US attitude, providing for the continuation of the EEP without specified programme limits. It maintained a minimum of $500 million per year, for five years. The expenditure for FY 1992 was $1.12 billion. The estimated expenditure for FY 1993 is $1.2 billion.

From FY 1985 to 1992, about 194.1 million tons of grains and products in grain equivalent, 2.8 million tons of vegetable oil and substantial quantities of eggs, dairy cattle, frozen poultry, pork and canned peaches were targeted for export subsidies within the programme. In financial terms, subsidies already granted are valued at approximately $5,306 million. According to the US Department of Agriculture the 1992 EEP measure of $1 million on exports of 9,000 tons of canned peaches to Japan, Korea and Mexico has been taken as a retaliation against the EC because of the EC refusal to apply retroactively a modification of the EC processing aid for canned fruit which had become necessary under the EC-US agreement on canned fruit.

Under the **Dairy Export Incentive Program** (DEIP), instituted in September 1989, over half the countries targeted were EC markets. The Dairy Export Incentive Program as of January 1992, had attained sales of 33,430 tons of butter oil, 5,772 tons of cheese, 40,817 tons of milk powder and 43,602 tons of non-fat dry milk. Initial allocations for FY 1993 are set at 204,020 tons of milk powder, 48,415 tons of butterfat and 5,800 tons of cheese.

Both programmes, the EEP and the DEIP are clearly targeted against EC agricultural exports to third countries. The programmes aim at the US gaining higher world Market Shares to the detriment of other countries' exports and make explicit use of the possibility of undercutting prevailing world market prices. Both programmes are therefore clearly in conflict with GATT obligations. Furthermore, they also 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". This needs to be viewed in the context of the Community's willingness to reduce agricultural support, as shown in the recent CAP reform.

B. Other subsidies

1. Marketing Loans

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. These triggers are scheduled to come into effect in Fall 1993. The **1990 Farm Bill** provided for the continuation of mandatory marketing loans for upland cotton and rice and for extension of the scope of same to include soyabeans and other oilseeds.

2. Market Promotion Program (Targeted Export Assistance)

The **Food Security Act** of 1985 established a new programme, entitled Targeted Export Assistance (TEA). Under this programme, for fiscal years 1989 and 1990 figures of $200 million and $220 million were approved. 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. The allocation for FY 1992 was $200 million and for FY 1993 is $147.7 million.

3. Deficiency Payments

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.

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. Deficiency payments allow the US to have lower internal prices than within the Community and to start with direct export subsidies from lower levels.

If implemented a bilateral agreement between the EC and the US reached within the context of the Uruguay Round negotiations would have the effect of exempting certain deficiency payments from the requirement of reduction, provided they satisfy certain criteria, such as a direct link to set-aside. However, as long as the Uruguay Round remains unconcluded, the Community will retain its position regarding these payments.

4. **Credit guarantee and food aid programmes**

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. A total of $3.6 billion of guaranteed credit was announced for FY 1993 under GSM-102 and GSM-103. In FY 1992, $5 billion in US agricultural products were sold with the aid of these programmes.

Public law 480 (P.L.480) has amongst its other (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 40 years (as and from FY Spring 92). Donations for emergency food relief are provided under Title II. Title III authorises "food for development" projects. The programme level for P.L.480 for FY1993 is about $1.7 billion. Up until now, the US have not accepted to start negotiations in the framework of the OECD on international rules and disciplines on export credits for agricultural exports.

5. **Californian subsidies on water**

There is a wide-ranging debate going on in California over the state's future water policy triggered by one of President Bush's last actions: the signing into law of the Omnibus Water Bill of 1992, officially called the **Reclamation Projects Authorization and Adjustment Act** of 1992. The provisions of this bill regarding the federally funded Central Valley Project drastically reduce water deliveries to Central Valley farmers to the benefit of fish and wild life as well as urban users. As a result, the Central Valley project has decided to cut its 1993 deliveries to urban users to 75% of normal deliveries, but farmers in the Central Valley will only receive an average of 25% of their normal deliveries.

The Community, though generally pleased with the direction of the changes, will continue to closely monitor these developments.

C. ***Double Price System: Rock Phosphate/Fertilizer***

US 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 US fertilizer manufacturers who have privileged access to the rock phosphate raw materials.

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 reports of the US Bureau of Mines, average prices for rock phosphate were the following :

	US price for US market $/metric tonne	US price for exports $/metric tonne	Difference in $/metric tonne	%
1988	18.36	25.58	7.22	39
1989	20.40	28.98	8.58	42
1990	21.91	30.66	8.71	40
1991	21.15	32.00	10.05	46

According to some estimates, the additional cost for EC fertilizers producers was $26 million in 1989, $21 million in 1990 and $19 million in 1991 (based on EC import figures from the US of 3 million tonnes in 1989, 2.4 million tonnes in 1990 and 1.9 million tonnes in 1991). Indirect losses were higher because of lost sales by EC producers.

8. TAX LEGISLATION

A. *General remarks*

Much attention has been devoted in recent years to macroeconomic imbalances among the world's major trading partners. In particular, it is widely considered 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. There is, however, 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 examples illustrate this tendency.

B. *Automobiles*

US legislation imposes certain taxes which discriminate against imported automobiles. The three major taxes in question are the Corporate Average Fuel Economy payment (CAFE), the luxury excise tax as applied to cars, and the so-called "gas guzzler" tax.

The Corporate Average Fuel Economy Law (CAFE) penalises car makers for failure to achieve minimum fuel efficiency standards, based on averages of the fuel economy of their entire US sales. This penalty is levied on the manufacturers/importers. Enacted in 1975, CAFE is intended to increase fuel efficiency and thereby reduce the US's dependence on foreign sources of petroleum.

Although the CAFE tax applies theoretically to virtually all car makers doing business in the US, 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. 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. The fact is that the price of certain European cars includes this CAFE penalty, whereas the price of a comparable US car with the same fuel consumption does not.

In addition to its discriminatory impact, this measure unduly favours 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 Environmental Protection Agency (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 US or to "Buy American" for car parts to the detriment of Community exports.

The **luxury excise tax**, as applied to cars, was introduced as of 1 January 1991 by the **Omnibus Budget Reconciliation Act** of 1990. The tax is levied as a 10% excise tax on automobiles above $30,000.

The tax is applicable only to newly manufactured items (which are not exported) and is to be collected by the retailer who then remits it to the Internal Revenue Service (IRS). Passenger vehicles used exclusively by the federal government or a state or local government for public works purposes are exempt. All items subject to the tax are liable upon their importation into the US, regardless of whether the item was used outside the US prior to importation. According to US Treasury Department estimates, the total luxury tax collected on automobiles for calendar year 1991 will be $226 million.

For automobiles, the $30,000 threshold seems to be set at a level so as to exempt or cause minimum pain to the domestic automobile industry, whereas it has a large impact particularly in terms of competitivity on foreign, notably EC, automobiles. More than 50% of the cars exported from the European Community to the US are subject to the luxury tax, compared to only 12% of total sales of US cars.

The arbitrarily designated threshold of $30,000 means that imported cars are treated less favourably than domestic automobiles, even though they compete in the same market. Although this tax is not discriminatory in its face, its practical impact is far heavier on imports than on domestic products.

In 1991, an independent study financed by the Federation Against Inequitable and Regressive Taxation (FAIRTAX) concluded that the impact of the tax on imported European cars was devastating. Further, because of the deleterious effect of this tax upon trade, less customs duties are paid, the result actually being a net loss to the Federal Treasury.

Against the background of decreasing sales of the affected luxury products and therefore decreasing tax revenue, bills were introduced to Congress in 1992 which would have repealed the luxury tax for all covered items. The House Ways and Means Committee and the Senate Finance Committee, however, supported the repeal of the tax on all products except cars. Although the legislation finally passed Congress, it was vetoed by President Bush in October 1992.

The **"gas guzzler" tax** as specified by Section 4064 of the **Internal Revenue Code**, is levied 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, the EPA set the threshold fuel economy standard at 22.5 miles per gallon (MPG). As of 1 January 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 increasing 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).

The fuel economy cut-off point of 22.5 mpg is not founded on any reasonable or objective criterion and leads to discrimination against imported cars, on which falls overwhelmingly the incidence of the tax. Even though the Omnibus Reconciliation Act of 1990 has repealed previous exemptions from payment of the tax for stretch limousines as well as the special rules permitting the Department of the Treasury to set the rate of tax for small manufacturers, off-road and sport utility vehicles are still exempt from the gas guzzler tax. This further weakens the credibility notably with respect to its alleged environmental policy objectives.

The total revenue of the three taxes levied in 1991 was US $558 million, of which $494 million were levied on European cars. Thus, around 88 % (100% of CAFE, 80% of the luxury tax and 80% of the "gas guzzler" tax) fall on European cars, versus a market share of only 4%.

These figures show the direct and serious effect of these tax measures on European car makers' business in the US. The combined application of the three taxes impose additional costs on European car imports. These costs represent a considerable proportion of the retail price of a car and thus directly impact on the competitive position of Community suppliers in the US market. As US domestic producers are able to escape these costs, the tax system simply discriminates against imported models and cannot be brought in line with the reduced GATT rules of non-discrimination.

At the Community's request, there have been two rounds of consultations with the US under GATT Article XXIII, 1 on these car taxes. Neither the discussions during the consultations nor the data received from the US

have, however, led to an elimination of the Community's concerns. Therefore, the Community has requested the establishment of a GATT panel.

C. *Beer and Wine Excise Taxes*

The **Omnibus Budget Reconciliation Act** 1990 created a new tax credit for domestic wine producers of 90 cents/wine gallon and augmented the credit provided to domestic beer producers by between $9 and $11 per barrel. 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. Many of the individual states also maintain such discriminatory tax exemptions or credits.

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 practice, this measure would provide a maximum total benefit of $660,000 per eligible brewery (of which, it has been estimated there are more than 200 in the US) and of $90,000 per winery (of which, there are 1,400 estimated beneficiaries).

In September 1991, the Community made a submission to the GATT panel which was requested by Canada on, inter alia, this issue. In March 1992, the panel reported that the Federal and State tax exemptions and credits were inconsistent with Article III.2, first sentence. The panel report was adopted at the GATT Council meeting on 19 June 1992. Implementation is not yet complete; apparently hindered by constraints imposed by US constitutional law on Federal Government involvement in State regulation of alcohol. The Community noted its dissatisfaction that implementation was incomplete at the GATT Council on 9-10 February 1993.

9. STANDARDS, TESTING, LABELLING AND CERTIFICATION

A. *General remarks*

In the US products are increasingly being required to conform to technical regulations regarding consumer protection (including health and safety) and environmental protection. Even if, in general, not intentionally discriminatory, the complexity of US regulatory systems in this domain can represent a very important structural impediment to market access. This situation is aggravated by the lack of a clear distinction between essential safety regulation and optional requirements as to quality, which is due in part to the role of some private organisations as providers of assessment/certification in both areas.

A particular problem in the US is the relatively low level of usage of, or even awareness of, standards set in international standardising bodies. All parties to the GATT Code on Technical Barriers to Trade are committed to the wider use of these standards; but although a significant number of US standards are claimed to be "technically equivalent" to international ones, very few indeed are directly adopted. Some are in direct contradiction. One example of the problems this can cause is the case of food labelling, detailed below under C.

There are more than 2,700 State and municipal authorities in the US which require particular safety certifications for products sold or installed within their jurisdictions. These requirements are not always uniform or consistent with each other, or even transparent; in some cases a national standard may not exist. In this case, product safety requirements are not set out by mandatory technical regulations, but are determined in the market place through product liability insurance. Individual States may set environmental standards going far beyond what is provided for at federal level, as has occurred in California (see the cases of lead levels and glass recycling under 9.D. and F.). Then again, the Labour Department may require certification for equipment used in the workplace; the county authorities for electrical equipment; large municipalities for virtually any equipment they choose to regulate; insurance companies for other product safety aspects, depending on the company.

Acquiring the necessary information and satisfying the necessary procedures is a major undertaking for a foreign enterprise, especially a small or medium sized one, as at present there is no central source of information on standards and conformity assessment. One company has estimated the volume of lost sales in the US due to these factors at 15% of the total. Hidden costs could be much greater - if only because the time and cost involved can be greatly reduced simply by using US components which have already been individually tested and certified. In

addition, the private organisations providing quality assurance may impose the use of certain specific product components, under their own programmes which are not in conformity with international quality assurance standards (ISO 9000).

In some cases (e.g. that of telecommunications network equipment, see E. below), the buyers require an expensive evaluation procedure which does not lead to certification and does not take account of any additional requirements by individual buyers.

It is hoped that some of these problems can be tackled if new rules, currently under negotiation in the Uruguay Round, can be adopted. Also, EC/US negotiations should begin in 1993 for the conclusion of mutual recognition agreements covering the industrial products for which mandatory conformity assessment procedures apply.

B. Sanitary and phytosanitary requirements

Barriers often arise from divergences in the legal sanitary and phytosanitary requirements implemented on each side of the Atlantic. In addition, there have been cases where US customs follow a sampling and inspection procedure which fails to define adequately which goods require urgent processing by customs if detioration is to be avoided. EC exports of fruit (apples, pears, citrus), ornamental plants, cut flowers and smoked salmon to the US have encountered problems due to delays, resulting in damage to the goods and subsequent commercial losses for the exporters. In particular, the Food and Drug Administration's time-consuming scrutinising controls on the detection of pit fragments in imports of canned peaches from the EC has lead to detentions and subsequent destruction or obligatory re-export of this product, hampering the flow of trade and negatively affecting the volume of exports. The EC does not dispute the right of the US authorities to inspect imported goods but considers that adequate steps should be taken to deal expeditiously with perishable goods.

In the **phytosanitary field** the following main difficulties persist in spite of some progress within the framework of bilateral discussions between the European Commission and the US Department of Agriculture in 1992.

Prior to the introduction of administrative instructions governing the entry of **apples and pears** from certain countries in Europe. (Fed. Reg. of 1987, title VII, ch.3, par. 319-56-2r), a pre-clearance programme was applied in agreement between the French and US authorities with the objective of guaranteeing the absence of an insect pest known as the pear leaf blister moth. The new administrative rules extended the inspections to other Member States and to "other pests that do not exist in the US or that are not widespread in the US", the result being that US inspection was operated on the basis of an open list of prohibited pests.

Operating on the basis of an open list is not a scientific approach and is contrary to the spirit of transparency as provided for in the international Plant Protection Convention. Notwithstanding the continued operation of the pre-clearance programme, the rate of rejection of

consignments has increased significantly. The extended and more stringent inspection as well as the ensuing increased costs have had an evident negative impact on EC exports of apples and pears to the US. Negotiations between the EC and the US have so far failed to solve the issue.

The prohibition of import of **fruit and vegetables** from pathogen-free regions of an EC Member State adjacent to regions in which a given pathogen is known to occur (Fed. Reg. of 1987, title VII, ch.3, par. 319-56-2r) creates undue obstacles to export from pathogen-free regions within the EC. An example is the prohibition of import of tomatoes from Brittany because of the presence of the Mediterranean Fruit Fly in the Mediterranean regions of France. Although Brittany is ecologically isolated from the infested regions of France, and the French authorities carry out the necessary surveillance to avoid dissemination, imports into the US of ripe tomatoes from Brittany are not permitted by the US authorities. The EC considers these measures to be excessive and not justifiable on phytosanitary grounds.

The revised provisions regarding standards and certification of **plants** established in growing media (Fed. Reg. of title VII, par. 319-37-8) have reduced the obstacles encountered so far for EC exports of potted plants to the US. However, the certification of plant genera involves a very long procedure which may considerably delay the approval of EC plant genera. The EC considers the decision to reevaluate the previous risk analyses done on EC plant genera unnecessary and an undue obstacle to trade in this area.

The US insists on zero **pesticide residue** levels for substances which have not been approved for use in the US or for which no import tolerance has been established even where these substances are manufactured in the United States and exported to foreign countries (i.e. Mercabam). In some cases, time-consuming or unduly delayed approval procedures have led to trade disruption.

In February 1990, the Food and Drug Administration (FDA) 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 (EPA) 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 interim solution of the trade dispute, in April 1991, 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.

The recent provision of required data by the manufacturer of procymidone should enable the EPA to establish an import tolerance which should allow shortly the access of Community wines to the US market (insofar as procymidone residues are concerned).

In July 1992, the Californian Court of Appeals effectively ruled the EPA's negligible risk policy as illegal. This ruling would have the effect of rejecting food products (fresh or processed) containing

residues of more than 35 frequently used pesticides. The new Administration is awaiting the result of an appeal to the Supreme Court before taking a final decision on the matter.

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

In the **sanitary field** the following difficulties persist :

The US rules on importation of **animal products** and by-products from countries where Bovine Spongiform Encephalopathy (BSE) exists (docket number 90-252, Fed. Reg. 56 : 19794, April 30, 1991, amending 9 CFR parts 94 and 95) contain three requirements concerning ruminant animals:

- that the meat does not originate from any animal which has been in a country in which BSE exists during a time when the country was permitting the use of ruminant meat and bone meal for the feeding of ruminants ;
- all meat has to be deboned and all visually identifiable lymphatic and nerve tissue have to be removed ;
- each animal has to be inspected prior to slaughter by a veterinarian and found free of neurological disorders.

The EC has taken restrictive veterinary measures, which have been approved by the International Office for Epizooties (IOE), in order to protect animal health and public health in the EC. However the US measures go beyond these measure on important points such as:

- US does not make any distinction between countries with low or high incidence of BSE, while the EC in accordance with IOE requirements takes restrictive measures only in countries with a high incidence of BSE (UK). Furthermore, there was no justification for the temporary addition of Denmark to the US list of countries where BSE exists on the basis of one imported infected cow;
- all meat from all countries with BSE (FR, IRL and UK) must be deboned, while EC requirements for deboning only concern UK ;
- double requirements of deboning together with ban on meat from animals present prior to the ban on feeding on ruminant meat and bone meal.

The EC considers that the US measures constitute an unjustified restriction on trade. There is no justification for going beyond the recommendations of the authoritative international institution (IOE) especially when the US has not taken measures to protect its cattle population from the internal threat of scrapie in the US. In particular, the application of the severe measures (as applied to the UK) to countries with only a few cases of BSE cannot be justified.

Some restrictions on live animals relate to the non-recognition by the US of **freedom from certain diseases**, e.g. contagious equine metritis.

While accepting the **principle of regionalization** as an effective means of controlling animal disease, US import legislation concerning Foot and Mouth Disease, Rinderpest and other relevant diseases does not reflect this. The legislative and administrative amendments required are delayed on the pretext of the US awaiting IOE recommendations.

Non-comminglement means that establishments exporting animals, meat or meat products to the US do not handle at the same time, animals, meat or meat products from countries which are not recognized as free from relevant diseases and that there is no mixing of meat or meat products destined for the US with meat or meat products from such countries. These requirements are unnecessary in view of the EC policy of regionalized control of animal diseases.

Imports into the US of **uncooked meat products** (sausage, ham and bacon) have been subject to a long-standing prohibition, only part of which may be justified on health grounds. 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, e.g. San Daniele ham, German sausage, ham and bacon and cured hams from Spain.

C. *Labelling*

US legislation requires certain products to be labelled as to their content and origin.

The implementation of the **Nutrition Labeling and Education Act** 1990 requires the US Food and Drug Administration (FDA) to follow an accelerated timetable in their extensive programme of changes to US food labels. In this context, the FDA published a series of proposed rules (amounting to over 600 pages) in the Federal Register of 27 November 1991, with a comment-period deadline of 25 February 1992. The US Department of Agriculture has also been working along the same timetable with regard to the labelling requirements for fresh meat and poultry. Final rules have now been published with respect to both the FDA and USDA nutrition labelling with effective dates in May 1994.

The Community is concerned that the proposed rules differ from international standards on labelling established by Codex Alimentarius (upon which the corresponding EC legislation is based) and, furthermore, that this legislative action would have serious negative consequences on EC/US trade in foodstuffs. As it stands, the proposed implementing

legislation would result in significant commercial obstacles to EC food products marketed in the US and vice-versa.

With respect to wine labelling, there exist procedures, both at Federal and State level, for the approval of labels on the front and rear sides of wine bottles. In general, an average of three months is required to obtain label approval at the Federal level and, at the State level, the approval period varies from State to State but may be as long as six weeks. This renders the approval procedure time-consuming, confusing to exporters (who have to comply with different regimes from State to State) and costly.

Section 355 of the **Transportation Appropriations Act** of 1992 has introduced as of 1 January 1994 an obligation for automakers and car dealers to place labels on new cars detailing among others things the percentage of US/Canadian parts that went into the car as well as indicating the final assembly point by city, state and country.

It has been suggested that transparency is the aim of the proposed language. Providing consumers with accurate, useful information is certainly in everyone's best interest. The obligatory labelling system, as set out by Section 355 of the Transportation Appropriations Act of 1992, would, however, not provide any useful information to consumers about the product as such and its characteristics. The only information contained in the label would be whether and to what extent the parts of the product or the product itself are of domestic origin.

Such information can only be intended to influence consumers to buy cars of US/Canadian origin. This is clear from the language used, and from the speech made by Senator Mikulski in sponsoring her amendment. References to "stand up for America", "help provide jobs" and "practice pocketbook patriotism" cannot be interpreted in any other way. Legislation with such intent is clearly incompatible with the object and the purpose of GATT.

D. Lead levels

EC exporters of **ceramicware** must comply both with Federal regulations setting tolerance levels on the amount of lead in ceramicware, and with those enacted by State legislatures such as California. At the end of 1991, the Food and Drug Administration (FDA) unilaterally set tolerance levels for lead in **wine** and introduced new action levels for lead release from ceramicware. These action levels represent significant tightening of the standards and are used to determine the need for enforcement action against specific lots of shipments. The sampling and testing methods used to assess levels of leachable lead from cups and mugs are not satisfactory. As it stands, the FDA can take action on the basis of a single sample. EC exporters believe that if the FDA insists on new action levels, they ought to be introduced in such a way to at least prevent individual states from enacting more stringent standards and unnecessary labelling requirements.

In this respect, California's **Safe Drinking and Water Toxic Enforcement Act** (Proposition 65) is of concern to the Community. The Act requires a

warning label on all products containing substances known to the State of California to cause birth defects or reproductive harm, including lead. In addition, enforcement of Proposition 65 by the Attorney General of California has meant that European manufacturers of ceramicware are having to finance a $1 million lead safety information campaign for consumers. Most recently, a court settlement in California will have the effect of repealing a paragraph of Proposition 65 pertaining to an exemption for food, drug, cosmetic and medical device products, and will as from July 1993 impose stricter Californian standards in place of federal standards.

E. Telecommunications

While recognising the problems in standardisation arising from the speed of innovation and the difficulty for standards-setting to keep up with this, the EC continues to be concerned about certain developments taking place in the United States and the fact that these developments are not transparent.

With regard to **telecommunications services**, for example, the ONA (Open Network Architecture) plans of the BOCs (Bell Operating Companies), which continue to be monitored by the Federal Communications Commission (FCC) 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 and intelligent network 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" requirements (according to Part 68 of the FCC rules), manufacturers, in practice, have to comply with a number of voluntary standards, such as those required by individual Bell Operating Companies, to ensure end-to-end compatibility, or those set by industrial organisations, such as Underwriters Laboratories (UL). The latter produces standards in order to ensure safety concerning connection to the electrical supply system covered by the National Electrical Code and covering risks of fire, electrical shock and personal casualty, and as they are in practice universally regarded as a necessary addition to FCC requirements under the FCC rules, they may be termed "de facto mandatory". Indeed, due to changes in the National Electrical Code, manufacturers of terminal equipment to be connected to the network now have to submit their products to a nationally recognised laboratory in order to assess

conformity with UL standards, and in many states this has been made mandatory.

In addition, in practice today about two thirds of products which have to comply with the "no harm to the network" requirements of Part 68 of the FCC rules also have to comply with Part 15 of those rules, relating to frequency requirements. The technical standards developed by the FCC for radio frequency equipment are 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 of the other requirements will apply in a given jurisdiction.

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.

F. Recycled glass content in new glass containers

The **Public Resources Code of California**, requires that glass containers to be used for or containing food and beverages have a minimum percentage of recovered glass in their composition. The minimum percentage is progressive from 15% in 1992 up to 55% in 2002. Glass container manufacturers are requested to give a monthly report on the percentage of postfilled glass used, i.e. the glass containers found in bottle banks which have been previously filled with a beverage or food. In-house cullet (broken scrap glass resulting from the manufacturing process) is not considered to be recycled glass.

This legislation applies to all glass containers produced or sold in California, and thus also hits EC exports to California. The only element of flexibility in the legislation is the possibility of a reduction or a waiver of the percentage requirement if its achievement is technologically infeasible. At the Federal level too, there have been proposals in both houses, to require a minimum percentage of recycled glass in glass containers.

In 1991, sales of European food and beverage glass containers to the US totalled US $10 million. Although the share being exported to California is not known, it can be assumed that it is a high percentage, as California is the main wine producing state. If the Californian legislation were to be introduced at the federal level and extended to food and beverages sold in such receptacles, the economic impact would of course be tremendous.

While the Community shares the environmental objective of recycling glass containers in order to save landfill spaces, to reduce energy consumption and to preserve natural resources, it questions the Californian approach to this objective. It is worth noting that any environmental damage caused in California by the import of glass containers is in no way

related to the amount of recycled glass used when the product was manufactured in a third country. Therefore the application of such a domestic environmental requirement to imported products is not in conformity with GATT rules. Furthermore, the reporting requirements are unnecessarily burdensome.

G. *Electrical Products and Components*

Federal, State and local jurisdictions require product testing and certification of the safety of numerous electrical products and parts thereof. At 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.

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.

The testing and certification 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), as this is done in the European Community in the respective directives.

10. SERVICES

A. *Barriers in the financial services sector*

1. General remarks

An attempt by the US Government to reform the US banking system, in particular through allowing banks' groups to enter the securities and insurance markets eliminating current restrictions on the geographical expansion of their activities failed to pass Congress in 1991. A banking reform bill tabled by the Administration in February 1992 was not adopted.

While the Commission welcomes the outcome of the recently released roll-up/subsidiary study of the FED and Treasury which upheld the investor's choice as to the establishment of subsidiary or branches, generally speaking, the atmosphere for banking in the US has become more restrictive in the last few years. The implementing regulations to the Federal Deposit Insurance Corporation Improvement Act of 1991 are creating uncertainties and delays for establishment. FED must now approve all foreign bank applications for branches, agencies and representative offices, including those seeking or holding state charters. In doing so, FED must determine whether the foreign bank is subject to comprehensive supervision on a consolidated basis by its home country authorities, and must also check whether the bank's top management and local office managers have been associated with any criminal activity. While it is recognized that the new procedures have arisen out of prudential concerns, it should be possible to address those concerns while avoiding the creation of barriers to doing business in the US market.

Community financial institutions do not always benefit from national treatment in the US. There are 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. This applies, for example, to Section 214(a) of the **Federal Deposite Insurance Corporation Improvement Act** of 1991, concerning foreign bank operations in the US. As there has yet been no implementary rule making as required, the present status quo of foreign banks in the US is in no way secured.

2. Restrictions on geographical expansion

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 this (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 of 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 7 July 1978 were grandfathered - section 5(B) of BA); 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 meant that there is a requirement to obtain a separate licence to operate in each State.

3. Restrictions to the provision of securities, futures, options, and investment services

Bank subsidiaries incorporated in the US of a non-US bank may not own a securities firm (section 20 of **Glass Steagall Act**), although in January 1990 some of them were 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 on 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.

Under section 7(d) of the **Investment Company Act** of 1940, a foreign investment company may not sell its securities in the US unles 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. The CFTC issued ar order in October 1992 which had the effect of relaxing previously imposed restrictions on the marketing activities of those firms, granted part 30 relief, while in the US. While granting of the order was appreciated, 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.

The SEC have proposed large trader reporting rules which appear to require reporting of large trades in US-listed securities even when they take place outside the US and are not carried out through US brokers/dealers. The EC is concerned that, if implemented in the way apparently envisaged by the SEC, this proposal would have unwelcome extraterritorial effects.

4. Other restrictions

a. Restrictions operating at the Federal level

Under Federal law, directors of EC banks' subsidiaries incorporated in the US must be US citizens, although on approval by the Comptroller of the Currency, up to half of the number of directors may be foreign.

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 in 1991. 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 A(b)(1)() 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.

b. Restrictions operating at the State level

Banking regulation at the State level is traditionally 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 increasigly 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 the possibility of expanding to other States for "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 required 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.

As regards **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, whereas other 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. Finally, some States issue for non-US insurers only renewable licences 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.

c. Miscellaneous restrictions

At Federal level, the **Primary Dealers Act** (section 3502 (b)(1) of the 1988 Omnibus Trade Act) prohibits firms from countries which do not satisfy reciprocity requirements becoming or continuing to act as primary dealers of US governent bonds, if they were not authorised before 31 July 1987 (with the exception 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.

In an increasingly globalised international market, the separation between **banking and securities activities** continues to be at odds with developments, elsewhere, and is likely to constitute 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 (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 supervisor. 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 so far shown by the Federal Reserve Board to limit to the extent possible under current US law these extraterritorial effects. It is now necessary to work towards a permanent solution rather than the temporary exemption from US Law used until now. 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, unless exempted from the prohibitions of the Bank Holding Company Act, 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. It is thought that up to 200 EC banking groups might be affected by this problem.

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.

As regards **State level** 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. US banks and insurance companies from other States may also be affected by these provisions. The restrictions and discriminations thus 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.

Towards the end of 1991, the **Interstate Commerce Commission** introduced a requirement that **truck operators** involved in interstate commerce should only be allowed to insure with domestically admitted insurers. This in effect bars European insurers from writing business in a sector where they have been active for many years. This is a restraint on trade which is against the interests not only of European insurers, but also of US consumers. It is against the spirit of the OECD Capital Movements and Invisible Transactions Code and also contrary to the desire to improve market access underlying the current proposals in the GATT services negotiations. The decision is currently being challenged in the US Courts.

B. *Other Services Sectors*

1. Maritime Transport

a. Non-vessel operating common carriers

Section 710 of the **Federal Maritime Commission Authorisation Act** of 1990 dealing with Non-Vessel Operating Common Carriers (NVOCC's), contained provisions which put at risk the business of many Community freight forwarders by subjecting them to a range of requirements such as posting of a bond and appointing a resident agent in the US, aimed at reinforcing the provisions of the 1984 **Shipping Act** which requires NVOCCs to file tariffs. In 1991, the **Non-Vessel Operating Common Carriers Act** amended the 1990 Act allowing the Federal Maritime Commission to accept - in addition to bonds - insurance and other surety as proof of a NVOCC's financial responsibility. The $50,000 minimum amount for a bond was deleted.

A final rule published in the Federal Register on 22 January 1993, amended the FMC regulations on NVOCC's in order to implement the 1991 Act. Although through this new rule the Federal Maritime Commission gives

NVOCC's considerable flexibility regarding their financial responsibility requirements, no amendment has been introduced on the tariff filing obligation which is considered to be a great administrative burden and a disadvantage in competition, particularly for small Community freight forwarders.

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

b. Cargo Preference

According to provisions included in the following statutes, certain types of government owned or financed cargoes are required to be carried on US-flag commercial vessels.

The Cargo Preference Act of 1904 requires that all items procured for or owned by the military departments must be carried exclusively on US-flag vessels. **Public Resolution N°17,** enacted in 1934, 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, subject to the condition that they are available at fair and reasonable rates. Finally, **the Food Security Act** of 1985 increases the minimum agricultural cargoes under certain foreign assistance programmes of the Department of Agriculture and the Agency for International Development (AID) to be shipped on US-flag vessels to 75%.

The impact of these cargo preference measures 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.

c. Maritime Shipping Services and Ship Classification Services

Based on the **Merchant Marine Act** 1920, the Coast Guard Administration grants an effective monopoly for ship classification and inspection services to the American Bureau of Shipping. Community classification companies are therefore excluded from the respective market.

2. Air Transport

a. Airline foreign ownership

Current US legislation allows foreign investors to own up to 49% of the shares in an air carrier, but only 25% of the voting stock. These US restrictions place European investment interests at a disadvantage and

thus inhibit the free flow of transatlantic investment in this services sector.

b. Antidrug programme

In November 1988, the Federal Aviation Administration (FAA) adopted regulations concerning an anti-drug programme for personnel engaged in specified aviation activities. According to these regulations, employees performing sensitive safety and security-related functions -including employees located outside the territory of the US- would have to undergo a drug test. The rule is already applicable within the US, but in so far as it relates to testing outside US territory, the compliance date was extended several times, first until January 1992, then until January 1993, and once again until January 1995. However, drug testing for personnel located outside the territory of the US is objectionable because of its extraterritorial reach.

c. Computer Reservation System Displays

Revised rules on Computerised Reservation Systems (CRS) issued by the US Department of Transportation, became effective on 7 December 1992 and will terminate on 31 December 1997. These rules maintain the approach of their predecessors, allowing US Computer Reservation Systems in the principal CRS displays to give preference to "on-line" services (connections with the same carrier) over "interline" services (connections with other carriers). This implicitly disadvantages all the non-US airlines which, unlike the US carriers, have to rely on interline connections for traffic to and from US points other than their own gateway points.

This method of display amounts in effect to a disguised restriction of international trade in services. As a result, airline bookings are distorted. The consumer (the passenger) is only given the selection of US on-line services on the first screens (some 80% of all bookings are made through the first screen), and this despite of the fact that the quickest connections may be ensured through interline services. Therefore the present restrictions work against EC airlines' interests as well as against US and non-US consumer interests.

d. Certification of foreign aircraft repair and maintenance stations

In 1988, the Federal Aviation Regulation (FAR 145) was amended in order to allow routine repair and maintenance of US registered aircraft to be performed anywhere in the world.

In order to perform maintenance or repair work on US registered aircraft, a foreign repair station needs to be approved (certified) and annually inspected by the US Federal Aviation Administration (FAA). Until such approval is given, the station cannot be used by US registered aircraft. Due to the length of the process, it is virtually impossible for an EC firm providing maintenance and/or repair for aircraft to be certified by the FAA, because the FAA does not carry out the necessary inspections/certifications across the Community. Although there are over

100 EC firms operating with FAA approval, there is a 2-year backlog of requests affecting in particular equipment manufacturers and airlines.

It is thus an incorrect implementation of the Federal Aviation Regulation which in fact acts as a barrier to trade in services in this particular sector. The impact in commercial terms is very damaging, since an EC manufacturer may not be able to repair or to sell maintenance equipment to US customers.

3. Space Commercial Launch Policy

The National Space Policy Directive of 6 September 1990 establishes that US Government satellites will be launched on US manufactured launch vehicles unless a specific exemption has been granted by the President. The measure is explained as part of a set of coordinated actions which are required to reach the long term goal of creating a free and fair market in which the US launch industry can compete.

The promotion of the US commercial space launch industry, by reserving all US launches of government satellites exclusively to domestic launch service suppliers, is clearly detrimental to European launch service providers. 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.

4. Telecommunications and Broadcasting

Foreign firms face obstacles in the provision of common carrier services as a result of the FCC licensing process under Section 214 of the **Communications Act** of 1934 and/or the implementation by the FCC of the restrictions on foreign investment under section 310 of the same Act. The latter provision also affects broadcasting services. In addition, foreign firms operating in the US face discrimination in their regulatory treatment.

Furthermore, uncertainties about the extent to which federal regulation of major US common carriers may be reduced ("streamlined") and about possible involvement of subfederal 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.

a. Common Carrier telecommunications services

These may be provided without restriction by foreign-owned business (for long-distance service only - services at the local level are for the most part regarded as a natural monopoly) only if no radio communication is involved (see Chapter B.4.b). However, non-radio 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 which hold market power and bottle-neck facilities. They must comply with stricter regulations than non-dominant carriers. At present the only US carrier so designated is AT&T and COMSAT for certain services; and the extent of regulation implied by this designation is under consideration.

Until recently, the FCC classified as "dominant" all foreign-owned carriers, 15% or more of whose stock is owned by a foreign telecommunications entity, irrespective of their size, and irrespective of the route being operated. On 24 November 1992 the FCC adopted a rule modifying this policy so that carriers will be regulated as dominant only on those routes where their foreign affiliates have the ability to discriminate against unaffiliated US international carriers through control of bottle-neck services and facilities in the foriegn market. Under the new framework, carriers affiliated with a foreign carrier that is a monopoly in the destination market will presumptively be considered dominant for that route, while carriers affiliated with a foreign carrier that is not a monopoly on the destination route will receive closer scrutiny by the FCC. However, the modified policy deals only with the manner in which US international carriers will be regulated once they obtain authority to operate, and does not address the standards the FCC will apply in determining whether to authorise entry.

Classification is a crucial issue because dominant carriers face heavier regulation with respect to the construction of lines, tariffs and traffic and revenue reports. Thus, Section 214 of the Communications Act requires common carriers to seek FCC authorisation to construct new lines, extend existing lines acquire or operate new lines. For international services, "dominant" carriers must obtain authorisation of the construction and extension of lines; prior authorisation is required for each type of service, and each country; "non-dominant" carriers must only get authorisation for the construction of new lines.

All carriers must file tariffs 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, and they must also submit their costs to justify any tariff changes. Moreover, in 1989 the FCC allowed AT&T to file tariffs on a 14-day notice for certain IMTS (international services) filings. AT&T generally does not need to provide cost support data for its IMTS (international service) filings.

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

Regarding Section 214 authorisation, this requires that common carriers may not construct, extend or acquire a communications line unless the FCC determines it would be in the public interest, and it provides that the FCC may attach such conditions to the issuing of the certificate as it thinks are in the public interest. The legislative intent behind this section of the Act was to regulate monopoly providers of communication services, and to make sure that they did not duplicate facilities, which would lead to the monopoly's "captive" customers paying higher charges

than they should for surplus facilities. However, there is no definition of what is in the public interest, nor are there any set criteria used by the FCC in order to judge whether it is in the present or future public convenience that carriers provide services, and there is some concern that the FCC, through its application of Section 214, has moved away from the original intent of the section and independently makes decisions affecting international trade policy.

Finally, the **Cable Landing Act** requires a common carrier to seek a (marine) cable landing licence. Section 2 of the Act provides that the FCC, through power delegated by the President, may withhold or revoke a submarine cable landing licence in order to assist in securing or maintaining rights or interests of the US, or may grant landing licenses on terms which will assure just and reasonable rates and services. The act is intended to achieve reciprocal treatment of US interests. It permits, among other things, the revocation of an existing authorisation if a country fails to grant US nationals reciprocal rights.

b. Radio based services

Section 308(c) of the **Communications Act** of 1934 permits the FCC, in certain circumstances, to "impose any terms, conditions or restrictions" on the granting of a radio station licence, including for basic telecoms for commercial communications between the US and a foreign country. Such conditions or restrictions, including withholding or revoking a licence, may be imposed to assist in securing or maintaining rights or interests of US providers in foreign countries, or to assure just and reasonable rates and services.

Section 310 of the **Communications Act** of 1934 significantly inhibits the operation of mobile and satellite facilities and the provision of telecom and broadcast services by imposing limitations on foreign investment (see section on investment in telecommunications). As a result, FCC does not grant licences to operators owned by foreign governments or their representatives (e.g. state-owned telecom operators and broadcasters), nor to suppliers of broadcast, common carrier or aeronautical services in cases where the foreign ownership exceeds 20% (or 25% indirectly). (See section 12D for description).

The provision of "private" services by satellite is subject to great regulatory uncertainty. In principle, foreign companies have unrestricted access to the provision of "non-common carrier" or "private" services. However, the question of whether a proposed satellite service may comprise a licensable common carrier service or a private service is not clear in US regulatory terms, for reasons related to the US treaty obligations to INTELSAT regarding interconnection with the public network. Each application is subject to a lengthy case-by-case consideration, so a non-US owned licence applicant's commercial viability may remain very uncertain pending the outcome of individual FCC licence proceedings.

The use of satellite news gathering terminals in the US by foreign organisations is hampered by Section 310(a) which prevents the FCC from granting a licence to foreign governments or their representatives.

Regarding **mobile satellite services** (MSS), the FCC decision to give American Mobile Satellite Corporation (AMSC) the exclusive monopoly rights to serve the domestic US market for these services means that any foreign competition, either at space segment level or at service level is excluded. The US Court of Appeals reversed the FCC's decision to require several mobile satellite service applicants to join a consortium under a single license. However, in January 1992 the FCC launched the process for a final decision granting the US monopoly mobile satellite service licence to AMSC.

The FCC has stated that the reason for imposing this consortium is related to the scarcity of MSS spectrum and the limited market for MSS services. However, a number of companies have in the past been licensed to provide mobile satellite services, albeit in different frequency bands, namely in the Ku and RDSS bands respectively. In addition, COMSAT has recently been allowed to provide international land-based mobile satellite services outside of North-America, and thus COMSAT can now compete in Europe for the provision of MSS services if it obtains the necessary European licenses, while domestically the US retains the AMSC monopoly.

As far as **aeronautical mobile satellite services** is concerned, in 1989, the FCC confirmed its 1987 decision on the exclusivity of the AMSC licence and ruled that Inmarsat-based aeronautical satellite services may not be used on the domestic segments of international flights, thereby preventing effective market entry by Inmarsat-based systems, since any aircraft in flight between two domestic US points would be obliged to use AMSC space segment.

While the FCC, in a recent Order, has decided to permit certain parties (those already authorised to provide Inmarsat aeronautical MSS services to aircraft in international flight) to provide interim services to aircraft in domestic flight, it deferred consideration of a permanent waiver to allow use of Inmarsat for AMSS to aircraft in flight on domestic legs of scheduled international flights.

The discriminatory regulatory requirements relating to "dominance" applied to those foreign-owned carriers which are not excluded by Section 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. Simularly, the FCC should not use this authorisation procedure as a tool to address broader policy issues beyond the regulatory concerns regarding the service for which the authorisation is sought.

The US policy to retain a domestic monopoly for MSS while at the same time launching additional US-based consortia into global MSS ventures via an effective control over spectrum allocations is detrimental to efforts of non-US based organisations to provide both global or US MSS services. First of all, the arguments for the domestic monopoly of AMSC no longer hold. Despite the so-called scarcity of spectrum and the so-called limited market, additional service providers have been and continue to be licenced by the FCC. There remains therefore no justifiable argument to retain the monopoly. Furthermore, early licencing of MSS providers, the early availability of additional spectrum in the US only, and an applied

ownership filter to bar non-US competitors seem an indication that the US is trying to seek effective control of global MSS ventures, while closing the domestic market from foreign competitors.

5. Professional services

The major difficulty for professional services suppliers in terms of market access in the United States relates to the fact that most do not have regulations providing for the access of foreign suppliers. Hence, in a large number of States there is no access at all for foreign professional service suppliers.

As for foreign **legal consultants**, access is provided for in 10 states only. Thus there is no supply of services of foreign legal consultants possible in the other 40 States. These States are: Alabama, Arizona, Arkansas, Colorado, Delaware, Louisiana, Georgia, Idaho, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Minnesota, Mississippi, Missouri, Nebraska, Nevada, New Hampshire, New Mexico, North Carolina, North Dakota, Oklahoma, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, Wyoming. Access restrictions for foreign legal consultants are for example in-State residence in New York, US residence in Michigan, and in Texas there is even a reciprocity provision.

As regards **accounting services**, 35 States have no provisions for temporary practice. Foreign accountants can only practise when they have obtained a state licence as a Certified Public Accountant. Wherever the provision of accounting and auditing services is opened up to foreigners, nevertheless a state qualification is required. Such a qualification is difficult to obtain since there is no recognition of qualifications foreseen. Furthermore, for **accountants and auditors** the possession of US citizenship is necessary in North Carolina and Alabama. Local residency is required in the following States : Arizona, Arkansas, Connecticut, District of Columbia, Idaho, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Michigan, Minnesota, Mississippi, Missouri, Nebraska, New Hampshire, New Mexico, North Carolina, North Dakota, Ohio, Oklahoma, Rhode Island, South Carolina, Tennessee, and West Virginia.

For **architectural services** an in-State residence is required in the following States : Arkansas, Idaho, Illinois, Kansas, Kentucky, Mississippi, New Hampshire, Oklahoma, Pennsylvania, Rhode Island, South Dakota, Tennessee, and Wyoming.

For **engineering services**, the possession of US citizenship is required in the District of Columbia and Rhode Island, in-State residency in Idaho, Iowa, Kansas, Maine, Mississippi, Nevada, Oklahoma, South Carolina, South Dakota, Tennessee, Texas, and West Virginia.

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

A review of the US market for professional services demonstrates that, firstly, access is not provided for at all in a large number of States; secondly, in the States where access is possible, requirements such as US citizenship, US or in-State residence and/or local establishment have to be complied with; and thirdly, there is a lack of procedures for recognition of qualifications. The US, therefore, is not granting effective market access in the field of professional services.

11. INTELLECTUAL PROPERTY

A. *Patents and related areas*

1. Section 337 of the Tariff Act of 1930

Section 337 of the Tariff Act of 1930 provides remedies for holders of US patents with a view to keeping imported goods which are infringing such patents out of the US (exclusion order) or to have them removed from the US market once they have come into the country (cease and desist order). These procedures are carried out by the US International Trade Commission (ITC) and are not available against domestic products infringing US patents.

In July 1987 the European Community requested the establishment of a panel to consider the compatibility of Sec. 337 of the US Tariff Act with the US' obligations under the GATT notably with its Article III. The Panel Report which was adopted by the Contracting Parties on 7 November 1989 came to the following conclusions :

Section 337, inconsistently with Article III:4 of the General Agreement, accords to imported products alleged to infringe United States patent rules treatment less favourable than that accorded under federal district court procedures to like products of United States origin as a result of the following factors :

- the availability to complainants of a choice of forum in which to challenge imported products, whereas no corresponding choice is available to challenge products of United States origin;
- the potential disadvantage to producers or importers of challenged products of foreign origin resulting from the tight and fixed time-limits in proceedings under Section 337, when no comparable time-limits apply to producers of challenged products of United States origin;
- the non-availability of opportunities in Section 337 proceedings to raise counterclaims, as is possible in federal district court;
- the possibility that general exclusion orders may result from proceedings brought before the USITC under Section 337, given that no comparable remedy is available against infringing products of United States origin except where this might be justified under GATT Article XX (d)
- the possibility that producers or importers of challenged products of foreign origin may have to defend their products both before the ISITC and in the federal district court, whereas no corresponding exposure exists with respect to products of United States origin.

Under the **Omnibus Trade and Competitiveness Act** of 1988, several modifications have been introduced to Section 337 such as the availability of remedies in relation to imported goods which infringe a US process patent.

Despite the GATT Panel finding of 1989 the US have to date not taken any measure to bring Section 337 in line with its international obligations under the GATT. The serious effects of Section 337 on European companies' activities were highlighted in 1992 by several cases. The discriminatory character became particularly apparent in one case where the federal district court had stayed the procedure before it on the ground of an arbitration clause, which did not prevent the ITC (which was subsequently petitioned) from taking action. In 1992 Senator Rockefeller introduced a bill into the US Senate which was intended to bring Section 337 in line with the GATT panel findings. While the bill indeed addresses some of the issued raised in the panel findings, it clearly falls short of remedying the GATT inconsistencies in a meaningful manner. In February 1993 the bill was reintroduced in the Senate with minor modifications.

2. Section 104 of US Patent Law

US patent law is based on the "first to invent" system, with almost the rest of the world following the "first to file" system. Section 104 of the **US Patent Law** provides that it is not possible to establish a date of invention by reference to any activity in a foreign country. A non-US inventor who typically carries out research and development activities outside the US cannot therefore establish a date earlier than that in which he or she applied for the patent.

This treatment clearly discriminates vis-à-vis foreign inventive activities in comparison to US domestic inventive activities and thus has the effect of forcing foreign companies to carry out research and development in the US rather than abroad. The elimination of this discrimination is therefore one of the objectives of the current TRIPs negotiations in the Uruguay Round.

3. Government use

US law allows government use of intellectual property rights without even having to notify the right holder. This practice is particularly frequent in the activities of the Department of Defence.

For obvious reasons this practice is particularly detrimental for foreign right holders because they will generally not be able to detect such government use and are thus very likely to miss the opportunity to initiate an administrative claims procedure. This issue is also addressed in the Uruguay Round negotiations on TRIPs.

B. *Inadequate protection of geographical indications of European wines and spirits*

Community legislation protects the geographical indications of wines. US legislation does not afford the same level of protection against misuse of EC denominations. In 1983, an exchange of letters between the Community and the US provided a measure of protection for EC geographical names that designate wine. The US undertook not to appropriate such names, if known by the US consumer and unless this use by US producers was traditional. The exchange of letters expired in 1986 but the US has maintained its commitment to this undertaking.

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, many Community geographical designations do not figure on this list and the EC indicated to BATF that the list, as published, is not satisfactory, since it does not improve protection of EC wine denominations in the US. A petition to complete the list of EC protected distinctive indications has recently been denied on the grounds of "lack of evidence".

Moreover, no progress has been achieved to date with respect to wine names defined as "semi-generic" under US legislation. The US government allows some EC geographical denominations of great reputation to be used by American wine producers to designate wines of US origin. The most significant examples are Burugundy, Claret, Champagne, Chablis, Chianti, Malaga, Marsala, Madeira, Moselle, Port, Rhine Wine, Sauternes, Haut Sauternes and Sherry. This issue is clearly a major one in the ongoing EC/US discussions on a new and better "wine accord".

American producers also use some of the most prestigious European geographical indications as names of grape varieties. This abuse could often mislead consumers as to the true origin of the wines. Furthermore, the improper use of Community geographical designations for wines and spirits places the respective EC products at a disadvantage on the US market.

With regard to spirits, the US regulations basically provide protection against practices misleading to the consumer. Furthermore, they explicitly protect five EC denominations. This limited protection does not prohibit the improper use of geographical designations of spirits or even the development of certain names into generic designations. A draft agreement has been presented by the Commission to the Council for the reciprocal protection of two US and six EC designations.

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 geographical indication identifying wines and spirits not originating in the place indicated. The most recent draft text resulting from the Uruguay Round negotiations partially addresses this question. It aims to secure a "standstill" on the usurpation of geographical indications. The EC's goal, however, remains to eliminate the illicit use of its appellations.

C. *Copyright and related areas*

1. **Moral rights**

Despite the unequivocal obligation contained in Art. 6 bis of the **Berne Convention** to which the US acceded in 1989 to make "moral rights" available for authors, the US have never introduced such rights and have repeatedly announced that they have no intention to do so in the future.

It is clear that while US authors fully benefit from moral rights in the EC, EC right holders do not enjoy such rights in the US, which leads to a lack of balance of benefits from Berne Convention Membership for the European side.

2. **Protection of existing works**

Art. 18 of the **Berne Convention** stipulates that works which have not fallen into the public domain by the entry into force of the Convention shall benefit from its protection. Furthermore, protection under the Berne Convention is not dependent on the fulfilment of formalities (Art. 5). Contrary to these provisions the US do not grant copyright protection to third country works created before 1989 in the absence of the completion of the formalities under US copyright law.

Thus, films which at the time have not appropriately been registered in the US are not granted any copyright protection. To the financial detriment of legitimate Community right holders, this situation has apparently led to widespread copying and rental of such films in the US.

12. BARRIERS TO INVESTMENT

A. *General Remarks*

The United States has been a net exporter of capital for direct investment since the end of World War II and up to the 1980s. Together with transfers of technology and skills, US investment contributed significantly in rebuilding the economies of many individual European countries. The pattern of foreign direct investment (FDI) flows changed in the last decade, with the US becoming a net recipient of foreign investment. Between 1982 and 1991, the FDI position in the US more than trebled, from $125 billion to $408 billion, while the US FDI position abroad increased twofold, from $208 billion to $450 billion. In 1988/1989 it was thought that the position would be reversed but the US recession that followed broke this trend.

US legislative concerns have switched from protection of interests abroad to those typical for a host country. Public perceptions and attitudes towards inward FDI also changed, due to some spectacular acquisitions, especially by Japanese interests. The change in the political climate affects all 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.

There are also 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.

The Community and its Member States have repeatedly stressed the need for open and liberal investment policies and for a strengthening of international disciplines in this area, in negotiations and discussions.

B. *Exon-Florio Amendment*

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 merger, acquisition or takeover which could result in foreign control of legal persons engaged in interstate commerce in the US. This screening is carried out by the Treasury-chaired Committee on Foreign Investment in the US (CFIUS). 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. There are no provisions for judicial review or for compensation in the case of divestment.

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, have been tabled in Congress. The Fiscal Year 1993 Defense Authorisation Act has strengthened Exon-Florio procedures, by requiring a report by the President to the Congress on the results of each CFIUS investigation and by including among other factors to be considered "the potential effect of the proposed or pending transaction on US's international technological leadership in areas affecting US national security". This economic criterion is new.

Moreover, there are three new provisions concerning entities controlled by foreign governments. The first requires that, if they engage in any merger, acquisition or take-over which could result in a control that could affect the national security of the US, an Exon-Florio investigation be made. The other two, although not substantially burdensome, constitute a declaration of policy aimed at discouraging acquisitions by (and certain contract awards to) such entities.

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 statute, the lack of a definition of national security and the uncertainty as to which transactions are notifiable. Although the US Treasury's implementing regulations, which were published in November 1991, do provide some additional guidance on certain issues, these uncertainties remain. Coupled with the fear of potential forced divestment, they have meant in practice that many, if not most, foreign investors have felt obliged to give prior notification of their proposed investments. In effect, a very significant number of EC firms' acquisitions in the US will be subject to pre-screening.

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 and improve multilateral disciplines on trade-related investment measures in the Uruguay Round negotiations and to enhance liberalisation measures and instruments in the OECD.

C. *Tax Legislation*

1. General remarks

The US taxation policy is at a turning point. Both the commitments of the new President and the Democratic leadership in Congress express the sense that the US tax policy needs substantial reform. Indications were given that it would result in tax revenues raised out of multinational or foreign companies. President Clinton's clarification in the State of the Union Address that the Administration will put the emphasis on the enforcement of existing rules and not new "anti-foreigner" legislation is welcome, though it is noted that such legislation is not definitively rules out.

In 1992, the House of Representatives considered the **Foreign Tax Simplification Bill** (HR 5270) with the aim of reducing tax anomalies by US companies having domestic and foreign activities. **Transfer pricing** was approached with a formula apportionment for large foreign owned business unless there was a transfer pricing agreement between the company and the Internal Revenue Service (IRS). **Capital gains** on substantial holdings of US corporate stocks were taxed at the source country (the US), and an **increase of excise tax** of reinsurance premiums paid abroad foreseen.

This Bill illustrates the perception in Congress that foreign companies are a legitimate target for IRS action on transfer pricing. According to the IRS itself, such tax avoidance is US-wide estimated at $3 billion, which could be eliminated by improved law enforcement. A similar approach can also be found at subfederal level, where state legislatures have maintained in different forms rules of unitary taxation which might be considered contrary to bilateral tax treaties, and the principles of "arms length" and non-discrimination.

Although the Foreign Tax Simplification Bill did not pass Congress in 1992, it may be tabled again by the Democratic leadership in the new Congress. The EC would then, as it did in 1992, make appropriate representations to the US Government.

Early in 1992 detailed draft **Transfer Pricing Regulations** (S482) were put forward by the US, which if introduced as drafted, were perceived as being likely to result in economic double taxation. Following representations from many quarters, including comments from a task force established by OECD to review proposed regulations, revised regulations were released for comment in January 1993.

2. Information reporting requirements

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 Service) 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 not only to subsidiaries of foreign companies, but also to all other "foreign" entities such as branches, which will primarily affect foreign banks. Furthermore, the requirements apply retroactively to all open tax years and to all records in existence on 20 March 1990.

The extended 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. Although the purpose of the legislation is reasonable - to ensure that IRS can obtain relevant information about transactions between a US operation and a foreign affiliate where foreign ownership might otherwise be used as a shield - meeting the requirements is onerous and adds to the complexity of doing business in the US for foreign owned corporations. Accordingly, they could have the effect of discouraging foreign investment in the US and run counter to national treatment.

3. "Earnings stripping" provisions

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 an independent corporation. Such artificial loading can, in effect, transfer profits away from the US.

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. Depending on the

way this provision is implemented, this could be discriminatory and therefore discourage foreign investment in the US.

The law provides for regulations to ensure that the principle is adhered to. Those regulations have now been published in draft form for comment. So far, regulations on the most controversial aspects have not been published which reflects the difficulty of finding equitable yet effective solutions.

4. State Unitary income taxation

Some 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. 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. The basic objective of such a method is to overcome transfer pricing problems and so raise additional revenue.

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 bilateral tax treaties concluded by the US with foreign countries. A company may also face heavy compliance costs in furnishing details of its worldwide operations.

In response to multinational corporations' protests and foreign governments' demarches, the State of California enacted in 1986 "the water's-edge" legislation. In 1988 the Californian law was modified again to alleviate further the 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. However, companies have to pay a substantial non-returnable fee to make this election.

Long-running cases have been brought in the US Courts by foreign corporations, challenging the constitutionality of the worldwide combined reporting method, and these are nearing their conclusion. However, whilst it is hoped that litigation will provide a satisfactory solution to the problems faced by multinationals operating in "unitary" States, if this proves not to be the case the EC would look to the US Federal Government to take appropriate action.

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 is 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.

D. *Telecommunications and broadcasting*

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 long-distance market, and only through a minority shareholding in the mobile market. Foreign news organisations are also hampered in their activities in the US. Section 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 to be made by the FCC in the specific case of indirect ownership, if it finds that this would be in the public interest, but the Federal Communications Commission (FCC) has rarely used this possibility.

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 many 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.

E. *Restrictions on foreign investments in energy and power production, exploitation of energy ressources and the puchase of public lands*

Apart from the restrictions on foreign ownership of broadcasting and telecommunications facilities, US legislation at federal and state level contains restrictions on foreign investment in the energy sector at large. Although foreign participation in business activities in this sector in principle is feasible through incorporation in the United States - a requirement which is understood to be intended to ensure equal application of US law to foreign and domestic investors -, there are nonetheless a series of obstacles - ranging from licencing requirements to a complete prohibition on foreign-controlled investment - which limit access of foreign investment to the respective US markets.

1. Investments in energy and power production

Under the **Federal Power Act**, any construction, operation or maintenance of facilities for the development, transmission and utilization of power

on land and water over which the Federal Government has control is to be licensed by the Federal Energy Regulatory Commission. Such licenses can only be granted to US citizens and to corporations organized under the laws of the United States. The same applies under the **Geothermal Steam Act** to leases for the development of geothermal steam and associated resources on lands administered by the Secretary of the Interior or the Department of Agriculture.

As regards the operation, transfer, receipt, manufacture, production, acquisition and import or export of facilities which produce or use nuclear materials, the **Nuclear Energy Act** requires the issue of a licence which may not be granted to a foreign individual or a foreign-controlled corporation, even if there is incorporation under US law. Under the Geothermal Steam Act, leases for the development of geothermal steam and associated resources on lands administered by the Secretary of the Interior may be issued only to US citizens, associations of US citizens, and corporations organized under US state or federal law.

Foreign individuals and corporations not organized under the laws of the United States may not obtain leases for the development of geothermal steam or related resources on lands administered by the Secretary of the Interior.

2. Exploitation of energy resources

The conveyance to or use of public lands by foreign investors for the exploitation of energy resources which include oil and gas, coal, and certain other minerals, is limited to corporations organized under US federal or state laws, provided that the country of the foreign investor provides like or similar priviledges to US citizens or corporations (Reciprocal Investment Privileges Requirement; **Mineral Leasing Act of 1920, Mineral Leasing Act for Acquired Lands of 1947, Geothermal Steam Act of 1970**). This applies also to the acquisition of rights-of-way for oil or gas pipelines across onshore federal lands. However, the Reciprocal Investment Privileges Requirement appears to be interpreted by the Department of the Interior and the US courts in a flexible manner, so that at present, no country is considered to deny reciprocal investment privileges.

According to the **Naval Petroleum Reserves Act** the leasing of mineral rights may be denied to foreign nationals or corporations in which such citizens are stockholders, if the foreign country denies the privilege of leasing public lands to citizens or corporations of the US. Leases for minerals in the Outer Continental Shelf may be held by aliens lawfully admitted for permanent residence in the US or by associations of such resident aliens (**Outer Continental Shelf Lands Act**).

3. Government grants and loans

Certain government grants and cooperative research and development programmes in the energy and power production sector are not (or only under certain conditions) available to foreign citizens and foreign controlled companies. This applies notably to financial assistance under

the **Advanced Technology Program** (ATP) of the National Institute of Standards and Technology of the Department of Commerce, which is only available to companies that either have majority ownership or control by citizens, or have a parent company which is incorporated in a country which affords US-owned companies opportunities comparable to those in the US. Furthermore, preferential treatment is given under the **Technology Transfer Act** and the **Bayh-Dole Act** to business units located in the US which manufacture products embodying subsidized technical inventions substantially in the US.

As regards US government insurance and loan programmes, there are restrictions to be noted for foreign investors in the energy sector as far as the insurance and loan guarantee program operated by the Overseas Private Investment Corporation (OPIC) is concerned. Benefits from this programme are not available to certain aliens, foreign enterprises, and foreign-controlled domestic enterprises.

F. Other restrictions on foreign direct investment in the US

1. Restrictions applicable to the purchase and transfer of public lands

There are several **US federal laws** which limit the purchase and assignement of certain public lands to US citizens. However, such restrictions on the transfer of public lands from the US government to private individuals apply only to the initial sale, whereas subsequent sales may be made to non-US citizens. Furthermore, with the exception of reclamation and desert land, companies incorporated under US laws may purchase public lands regardless of the nationality of their shareholders (**Federal Land Policy and Management Act, Irrigation and Reclamations Act, Desert Land Act, Homestead Act**).

A significant number of **State laws** are also 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.

2. Restrictions based on National Security considerations

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 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 also chapter 6.D.3.). Foreign investors must form a US subsidiary for exploitation of deep water ports

and for fishing in the Exclusive Economic Zone (**Commercial Fishing Industry Vessel Anti-reflagging Act of 1987**). Licences for cable landings are only granted to applicants in partnership with US entities.

3. **Reporting requirements for foreign investment**

According to the provisions of the **International Investment and Trade in Services Act (IITSSA)** and the **Foreign Investment in Real Property Tax Act of 1980 (FIRPTA)**, all foreign investments in US business enterprises in which a foreign person owns a 10% or more voting interest (or the equivalent) are subject to reporting, including all ownership of real estate, improved and unimproved, other than for personal use.

Many States impose reporting requirements for investments by foreign individuals, foreign-controlled and foreign-incorporated corporations. Some States distinguish between reporting requirements imposed on foreign individuals and those imposed on foreign business entities. Also, some states treat differently aliens, aliens who have not declared their intention to become a US citizen and alien corporations. Most states with reporting requirements impose penalties for noncompliance with the reporting requirements.