EUROPEAN UNION

The European Union (EU) and the United States share the largest two-way trade and investment relationship in the world. In 1998, the U.S. trade deficit with the EU was $26.9 billion, an increase of $10.2 billion from the U.S. trade deficit of $16.7 billion in 1997. U.S. merchandise exports to the 15 member states of the EU were just under $150 billion, an increase of 6.2 percent from the level of U.S. exports to the EU in 1997. U.S. imports from the EU were more than $176 billion, an increase of almost 12 percent from the level of imports in 1997. The stock of U.S. foreign direct investment in the EU amounted to almost $370 billion in 1997, a greater than 9 percent rise from 1996.

IMPORT POLICIES

Import and Distribution of Bananas

Since the late 1980's Latin American countries and the United States have urged the EU to implement the "Single Market" for bananas in a manner consistent with their international obligations under the GATT (General Agreement on Tariffs and Trade) and the subsequent international agreements under the WTO (World Trade Organization). A group of Latin American countries -- Colombia, Costa Rica, Guatemala, Nicaragua and Venezuela -- tried twice in the GATT to convince the EU to reform its discriminatory and burdensome banana rules; twice GATT panels found that EU banana rules were GATT-inconsistent (1993, 1994); twice the EU ignored those GATT panels and proceeded to extend and compound unfair and discriminatory trade barriers.

On July 1, 1993, the EU implemented a new banana import regime to replace individual Member State rules for banana imports. Elements of the new regime have caused significant adverse effects on U.S. distribution companies in the EU banana market. As a result of the EU's failure to reform its discriminatory system, a case was filed by the five complaining parties (Ecuador, Guatemala, Honduras, Mexico, and the United States) with the WTO in February 1996, and a dispute settlement panel was established to review the EU banana regime on May 8, 1996. The panel's May 22 report listed violations of fundamental WTO provisions in goods and services. The Appellate Body report, released on September 9, confirmed the panel's major findings of WTO-inconsistency of the EU regime and reversed two panel findings that had been favorable to the EU. The EU agreed to implement the WTO reports' recommendations and rulings within a "reasonable period of time," which was determined in arbitration to be the period from September 25, 1997 to January 1, 1999.

On January 14, 1999, a revised EU banana regime went into effect. The revised regime maintains WTO-inconsistent elements both in the structure of the market (goods) and licensing (services) regimes. The U.S. Government continues to press the EU to implement a new regime that is WTO-consistent, and sought agreement to return to the original WTO panel for a judgement on the EU regime within the "reasonable period of time" provided for compliance. The EU refused efforts to address both goods and services aspects of the case with the original panel that would have permitted completion of the process before the end of the implementation period. As no consistent regime was in place by the end of the reasonable period, the United States has requested the right to withdraw concessions under Article 22 of the Dispute Settlement Understanding (DSU). The EC has exercised its WTO right to ask for arbitration on the amount of

concessions to be withdrawn. This arbitration, under DSU rules, is scheduled to conclude by March 2, at which time the United States may withdraw concessions.

EU Implementation of Uruguay Round Grain Tariff Commitments

During the Uruguay Round, the United States obtained a tariff concession from the EU establishing a ceiling on the duty that could be charged on grain. The ceiling is based on the duty-paid import price of grains into the EU. However, the EU subsequently established a reference price system for grain imports. The reference price system deprived U.S. exporters of the significant duty reductions that they expected to receive on high-value grains, such as malting barley and packaged rice. The United States held unproductive consultations with the EU under WTO dispute settlement procedures in September 1995 and requested a WTO Panel later that month. The United States and the EU subsequently reached an agreement under which the EU committed to establish a cumulative recovery system (CRS) for duty underpayments and overpayments on brown rice, and a side commitment to establish a system that would permit imports of a limited amount of malting barley at 50 percent or less of the duty that would otherwise be charged. After the threat of further WTO action, the EU implemented these concessions in mid-1997.

The EU reauthorized the regulations regarding 1997 and 1998 imports of malting barley, and is in the process of reauthorizing imports of one hundred thousand metric tons of malting barley for 1999 and 2000. On the CRS, the United States and the EU signed a letter of understanding on duty treatment for husked rice in December 1998 for one year. However, consultations on the subject are still ongoing.

Implementation of EU Import Quotas for U.S. Rice

As part of the concessions made to the United States as compensation for the accession of Finland, Austria, and Sweden to the EU, the EU agreed to implement tariff rate quotas (TRQ) for imports from the United States of 38,721 metric tons of milled rice at zero duty and 7,642 metric tons of brown rice at an ECU 88/MT duty effective January 1, 1996. In late 1997, the EU, with the consent of the United States, implemented a one year quota. In 1998, the U.S. allocation system, named AARQ (Association for the Allocation of Rice Quotas, Inc.) came into operation. EU Commission Regulation (EC) No. 648/98 of March 23, 1998 outlines the quantities of milled and husked rice originating in the United States which can be imported through the AARQ under the TRQ in 1998, 1999, and 2000. Quantities for these 3 years exceed 38,721 MT and 7,642 MT for milled and brown rice, respectively, since they contain the 1996 TRQ volumes, spread out over 1998, 1999 and 2000.

Customs Classification of Information Technology Products

Increased tariff rates resulting from the reclassification by the European Commission and EU Member State customs administrations of certain local area network equipment and multimedia personal computers have raised concern with information technology equipment manufacturers. On February 25, 1997, the WTO Dispute Settlement Body established a WTO Dispute Settlement Panel to examine whether the following measures were inconsistent with the EU's obligations under Article II of the GATT 1994: (1) Regulation No. (EC) 1165/95, which reclassifies certain LAN adapter cards from category 8471, "automatic data processing machines and units thereof," to category 8517, "telecommunications apparatus"; (2) the actions of customs authorities in Member States in reclassifying and increasing tariffs on imports of all types of LAN equipment - including hubs, in-line repeaters, converters, concentrators, bridges and routers; and (3) the actions of customs authorities in Member States in reclassifying and increasing tariffs on imports of PCs with

multimedia capacity. On March 20, 1997, the dispute settlement body modified the terms of reference of the Panel to include U.S. complaints against Ireland and the UK.

The Panel's final report, released on February 5, 1998, found that the tariff concessions on "automatic data processing machines" (category 8471) in the EU Uruguay Round tariff schedule apply to computer networking equipment. Since the EU had been applying higher tariffs to computer networking equipment than the tariffs provided for in category 8471, the EU was found in violation of its tariff obligations.

On the EU tariff treatment of multimedia PCs, the Panel found that (1) PCs that incorporate a TV tuner can be regarded either as PCs capable of receiving TV or televisions that can also function as computers, and (2) it could not make a decision in the United States' favor on the basis of the evidence before it. However, the United States raised this issue due to concerns that the EU might treat any PC with multimedia capabilities as a television for tariff purposes.

The EU appealed the Panel's ruling. On June 5, 1998, the WTO Appellate Body overturned the original findings of the panel by finding in the EU's favor on most points. However, the commercial results the United States wanted to achieve have substantially been met in the Information Technology Agreement (ITA). There, the EU has agreed to lower tariffs on LAN equipment by the year 2000 (see below).

Tariffs on Information Technology Products

The EU is one of the signatories of the Information Technology Agreement of 1997, which eliminates tariffs on over $600 billion worth of world trade in computers, telecommunications equipment, semiconductors, and other information technology products. The EU will eliminate tariffs on all ITA products by the year 2000. The United States and EU are working together with other countries in the WTO to expand product coverage through the conclusion of an additional tariff and nontariff liberalization package on a broader range of related information technology products (ITA II) by early 1999.

Restrictions Affecting U.S. Wine Exports to the EU

The United States and EU have an active two-way trade in wine, although EU exports to the United States are roughly ten times the size of U.S. exports to the EU. Since the mid-1980's, U.S. wines have been permitted entry to EU markets by means of a series of annual extensions to temporary exemptions from EU wine making regulations. These regulations require imported wines to be produced with only those oenological practices (i.e. wine making practices) which are authorized for the production of EU wines. Without these "derogations," the majority of U.S. wines would be immediately barred from entering the EU. This leaves in doubt both the foothold U.S. exporters have secured in the EU market and the prospects for export expansion in the future. The United States seeks assurance of long-term access and growth potential for U.S. wine exports to EU markets.

Recently, as a result of bilateral discussions, the EU derogations have been renewed until 2003, with a Commission review in 2000. The EU has granted derogations for certain wine-making practices to other third countries that it has not granted to the United States The United States believes these derogations for additional practices should also be granted to U.S. producers on a most-favored-nation basis. However, a range of other barriers exists. The United States also is concerned about the EU's regulation 881/98 adopted to protect certain "traditional expressions" associated with wine and liqueur production. Traditional expressions are,

for the most part, adjectives used with certain other expressions (often geographical indications) to identify descriptive attributes of wine or liqueur. These terms are granted trademark protection in the EU, although 1) third country industry does not have a means to apply directly for such protection and 2) in many cases the terms are highly generic (e.g. “ruby” and “tawny” are protected “traditional terms”). The United States does not recognize the concept of traditional terms, nor is this subject covered under TRIPs. EU tariffs on wine are also of concern.

The United States has held a series of consultations with the EU on these and other wine-related issues. The main U.S. objective in the consultations is to ensure that the EU market remains open to U.S. wine and that U.S wine exports can compete fairly on the EU market. In late 1997, the United States proposed broad-ranging discussions on wine, potentially to include such issues as U.S. and EU oenological practices, the use of semi-generic designations in the United States, and tariffs. After consultation with industry, the United States held preliminary discussions with the EU in July and September 1998 to establish a basis for negotiation of a new Wine Agreement. The United States hopes negotiations can begin in early 1999.

Market Access Restrictions for U.S. Pharmaceuticals

U.S. pharmaceutical companies have difficulty with consistent market access throughout the EU because of price, volume and access controls placed on medicines by national governments. The pharmaceutical industry sees these controls as undermining the value of patents, distorting competition among medicines and across national markets, limiting access by patients to innovative products, and diminishing the contribution of Europeans to research and development.

While the EU's single market ensures that pharmaceuticals, like other goods, can move freely across borders among EU countries, member state public health authorities impose strict price controls on pharmaceuticals. As a result, since controlled prices vary greatly from one country to another, middlemen engage in parallel trading, profiting at pharmaceutical companies' expense by buying drugs in countries where the price is lower and selling in member states where the price is set at a higher level. This undermines the need of pharmaceutical companies to recoup the expense of their research and development.

Austria: Some U.S. pharmaceutical companies have complained about restricted access to the Austrian market. A U.S. firm seeking to market a product in Austria must first obtain the approval by the Austrian Social Insurance Holding Organization (Hauptverband der Sozialversicherungsträger). According to critics, the non-transparent procedures by which the Hauptverband approves drugs for reimbursement under Austrian health insurance regulations has perpetuated a closed market system favoring established suppliers. Pharmaceuticals not approved by the Hauptverband have higher out-of-pocket costs for Austrian patients and therefore suffer a competitive disadvantage vis-a-vis approved products. One U.S. pharmaceutical firm has raised Austria’s practices with the European Commission as a possible violation of the EU transparency directive.

The European Transparency Directive which will become effective in Austria in 1999, further complicates the issue. Allegedly to fulfill its obligations under the Transparency Directive, the Hauptverband has designed a contract which sets out its approval procedures in general terms. By signing the contract, a firm agrees to be bound by the decisions of the Hauptverband, effectively waiving its rights of appeal under the provisions of the Transparency Directive. About 65 percent of the pharmaceutical suppliers in Austria have signed the contract, though a number of major U.S. firms have not. Non-signatories are concerned that they

may be the subject of harassment on the part of the government but this has not materialized. Other U.S. pharmaceutical firms signed the contract in its present form, and approve its content.

Belgium: In Belgium, there are significant delays in providing market authorization and approval of pricing and reimbursement for new pharmaceutical products. According to industry sources, the current average duration for these processes is more than 1000 days, in contrast to EU requirements of a maximum 390 days for the entire process. (Directives 65/65, 93/39 for Marketing Authorization, Directive 89/105 for Transparency/Pricing and Reimbursement). One industry survey shows that the mean delay for Price and Reimbursement exceeds 500 days, well in excess of the 180 days required by the EU. The lengthy process to obtain marketing approval in Belgium shortens considerably the period of patent protection. Under the centralized European procedure, mandatory for new products, the supplementary protection certificate period depends on the date of first approval. U.S. companies are disproportionately affected by procedural delays as they are among the most active in developing and bringing to market innovative new products. The Belgian Government reportedly is considering new legislation to bring the reimbursement period into line with the EU Directive, but it is not clear when it will be implemented.

Pharmaceuticals in Belgium are also under strict price controls. There is a price freeze on reimbursable products and a required price reduction on drugs on the market for fifteen years. A four percent turnover tax is charged on all sales of pharmaceutical products. Control of prices for reimbursed and non-reimbursed products affect not only in-country sales, but exports sales to third markets for which the Belgian price is the reference price.

Spain: Pharmaceuticals and drugs still must go through an approval and registration process with the Ministry of Health requiring several years unless previously registered in another EU Member State or with the equivalent EU body, in which case the process is shortened to a few months. Vitamins are covered under this procedure; however, imports of other nutritional supplements are restricted, and they are dispensed only at pharmacies. This has an impact on U.S. nutritional supplements exporter's efforts to develop the Spanish market.

Ban on Fur from Animals Caught in Leg-hold Traps

In November 1991, the EU adopted a regulation banning the use of leg-hold traps in the EU. The regulation also requires a ban on imports of fur and fur products of certain species from countries which either do not ban leg-hold traps or do not conform their trapping practices to internationally agreed humane trapping standards. After over eight years of discussions on this topic, the United States and the EU signed an agreed minute on humane trapping standards on December 18, 1997, in parallel with an EU agreement with Canada and Russia. Together, these instruments involve the countries accounting for the vast majority of international trade in fur. The EU/Canada/Russia agreement is still undergoing domestic approval procedures. The EU completed its approval of the U.S.-EU agreed minute on July 15, 1998. In the United States, the agreed minute does not require formal treaty ratification procedures - competent authorities in the United States have already begun to undertake activities described in the agreed minute. The agreed minute should permit continuing access of U.S.-sourced fur and fur-products to the European market. Nevertheless, some problems could still emerge as the EU has not yet ended its requirement for certification of all fur imports. USTR will continue to monitor closely developments on this issue.

STANDARDS, TESTING, LABELING AND CERTIFICATION

EU Member States still have widely differing standards, testing and certification procedures in place for some products. These differences may serve as barriers to the free movement of these products within the EU and can cause lengthy delays in sales due to the need to have products tested and certified to account for differing national requirements. Nonetheless, the advent of the "new approach," which streamlines technical harmonization and the development of standards for certain product groups, based on minimum health and safety requirements, generally still points toward the harmonization of laws, regulations, standards, testing, quality and certification procedures in the EU. The European standardization process is still closed to U.S. firms' direct participation, although European standards bodies can be sympathetic to U.S. concerns when approached. There is also an increasing trend in the EU to adopt industry or environment standards before international standards-making initiatives have been completed (see 3rd generation wireless, wine and aircraft certification discussions below).

Standardization

Standardization continues to play an increasingly significant role in U.S.-EU trade relations, as evidenced by the Transatlantic Business Dialogue (TABD) adopted goal of "approved once accepted everywhere in the Transatlantic Marketplace." The United States Department of Commerce anticipates that EU legislation covering regulated products will eventually be applicable to 50 percent of U.S. exports to Europe. Given the enormity of this trade, EU legislation and standardization work in the regulated areas is of considerable importance. Although there has been some progress in implementation, a number of problems related to this evolving EU-wide legislative environment have caused concerns to U.S. exporters. These include lags in the development of EU standards; lags in the drafting of harmonized legislation for regulated areas; inconsistent application and interpretation by Member States of the legislation that is in place; overlap among directives dealing with specific product areas; grey areas between the scope of various directives, and unclear marking and labeling requirements for regulated products before they can be placed on the market. While many such problems may not constitute deliberate "trade barriers," their existence can impede U.S. exports to the EU.

Mutual Recognition Agreements

The EU is implementing a harmonized approach to testing and certification as well as providing for the mutual recognition within the EU of national laboratories designated by Member States to test and certify a substantial number of "regulated" products. The EU encourages mutual recognition agreements between private sector parties for the testing and certification of non-regulated products. One difficulty for U.S. exporters is that only "notified bodies" located in Europe are empowered to grant final product approvals of regulated products. While there are some laboratories in the United States which can test regulated products under subcontract to a notified body, the limited number of such labs means that such subcontracting procedures are unlikely to provide sufficient access for U.S. exporters. Moreover, these labs cannot issue the final product approval but must send test reports to their European affiliate for final review and approval, which delays the process and adds costs for U.S. exporters.

The United States and the EU have negotiated a Mutual Recognition Agreement (MRA) for several important sectors as a means of addressing this issue. MRAs will permit U.S. exporters to test and certify their products to the requirements of the EU in the United States, and vice versa. The U.S.-EU MRA entered into force on 1 December 1998. The MRA provides for a transition phase ranging from 18 months to 3 years, depending

on the specific sector. Under the recently agreed Trans-Atlantic Economic Partnership (TEP), the United States and EU plan to negotiate MRAs in additional sectors in 1999.

GMOs Product Approval

Despite EU Commission approval in 1998 of several products of modern biotechnology, the lengthy and highly unpredictable approval process for genetically modified organisms (GMO) has affected U.S. exports of corn and soybeans and threatens to affect an even broader range of products in 1999. Biotechnology continues to be a political issue in several member states which retain an active role in the EU approval process, with scientific and objective attitudes pushed to the side by emotional and extremist positions. Prospects for improvement appear dim at this time.

Approval of "viable" GMO's --including seeds and grains-- for environmental release and commercialization is governed by directive 90/220, the subject of internal EU executive and parliamentary debate as it undergoes revision, a process that may take several years. In the meantime, the approval process is slow and unpredictable, and several member states have defied final EU approvals, banning GMO's or suspending approvals without presenting any scientific justification. The Commission has shown great reluctance to prosecute these violations of EU law. Several products have been under review for over three years, as compared to an average six to nine month process in Canada, Japan and the United States. U.S. exports of corn to Spain and Portugal in 1997 were reduced to a fraction of historical levels due to tardy approvals. Exports in 1998 may even fall to zero.

A new directive that would cover use of GMO's in livestock feed, "Novel Feeds," is circulating in the Commission but has not yet been published. Another directive on seeds for planting has passed the Council but has not yet been published. The United States recognizes the right of the European Union to ensure products introduced into the market are safe and do not harm the environment. However, the EU process has become highly politicized and the addition of procedural steps and new, additional scientific reviews at the conclusion of an already intensive scientific review process places in question the EU impartiality in these matters. Even when products are approved, market access for products of modern biotechnology is not guaranteed. France, Austria and Luxembourg have imposed marketing bans on GMO products, which run counter to EU regulations.

Labeling

In addition to directive 90/220, in May 1997, the EU adopted the “Novel Foods Regulation”, which governs food safety assessments and labeling for genetically-modified foods. The regulation requires labeling of all new processed foods and food ingredients, including those made from GMOs. Neither the novel foods regulation, nor directive 90/220 makes clear which products processed from GMOs must be labeled.

In September 1998, an EU law provided for labeling of foods processed from Bt-corn and herbicide-tolerant soybeans became effective. First proposed a year earlier, the law fails to specify any threshold for incidental contamination, testing method or list of exempted products. Indeed, one of the issues at present in some member states is the determination of the threshold level that would trigger the labeling requirement. Austria has taken a leading position in advocating a threshold level (0.5-1.0 percent GMO content) lower than what the United States considers economically feasible. An ad hoc committee was supposed to have completed such details by the time of implementation in September 1998, but has made little progress. It is expected that whatever is eventually adopted for corn and soybeans will provide the basis for labeling of other GMO foods. Some European food processors have switched to non-U.S. soybeans to avoid confusing labeling regulations for GMO's.

In the United States, companies are not required to label products simply because they are produced through biotechnology. The United States believes that such labeling is unnecessary, in the absence of an identified and documented risk to safety or health. However, most European officials, including those that are pro-biotechnology, have come to believe that labeling of all GMOs, regardless of risk, is necessary to ensure consumer acceptance.

Ban on Growth Promoting Hormones in Meat Production

For almost 10 years, the EU has banned imports of beef produced with growth promoters. The United States launched a formal WTO dispute settlement procedure in May 1996 challenging the EU ban. The WTO Appellate Body (AB) upheld the original WTO Panel finding that this ban is inconsistent with WTO Agreement on Sanitary and Phytosanitary (SPS) measures and calls for the EU to comply with its WTO/SPS obligations. The AB clearly confirms the earlier Panel finding that the EU ban was imposed and maintained without evidence of health risks posed by eating beef from cattle treated with growth promoters, and despite scientific evidence showing such meat to be safe.

The EU announced in March 1998 that it would implement the AB finding. A WTO arbitrator consequently decided that the EU needed 15 months to bring its measures into conformity with its WTO obligations, instead of the four years it argued for, and that it was not necessary to conduct another risk assessment. The 15 months started in February 1998, with the adoption of the Appellate Body report. The reasonable period will expire on May 13, 1999. The EU currently is undertaking additional studies on hormone usage in beef production. These studies are not expected to be completed before the end of the "reasonable period of time" provided for WTO compliance. The United States is seeking early discussion with the EU regarding how the EU will meet its WTO obligations.

Poultry Regulations

The EU continues to refuse considering the use of anti-microbial treatments in poultry production. As a result, U.S. poultry exports to the EU have been blocked since April 1, 1997, representing a loss of $50 million annually to U.S. poultry exporters. In October 1998, the EU published an opinion on anti-microbial treatments, which, although more tolerant of some forms of treatment, does not recommend the use of chlorinated water, the primary means employed in the United States to assure safety of poultry products from microbial contamination.

Besides this issue of anti-microbial treatment, there is another issue at stake in France regarding poultry production: the United States continues to oppose the French ban on U.S. poultry, which has been in effect since the early 1960's. The French prohibition on U.S. poultry is based on U.S. poultry feed practices, practices which the United States believes to be entirely safe.

Specified Risk Materials Ban

On July 30, 1997, the European Union adopted a ban on the use of Specified Risk Materials (SRMs) for use in food and feed and medical, pharmaceutical, cosmetics and other industrial products. Specified risk material is defined as (a) the skull, including the brains, eyes, tonsils and spinal cord of cattle, sheep, and goats aged over 12 months, and (b) the spleens of sheep and goats. This measure results from EU concerns over the transmission of BSE, or bovine spongiform encephalopathy, commonly known as "mad cow" disease. The ban, originally

scheduled to go into effect on January 1, 1998, was subsequently deferred several times, most recently to January 1, 2000. The decision also prohibits the use of the vertebral column of cattle, sheep, and goats for the production of mechanically covered meat, and allows for a derogation for the feeding of fur animals. Industry sources estimate that the potential trade effect of the ban could exceed $20 billion if all products currently covered are ultimately covered by the ban.

Beyond the direct trade impact of the ban which is potentially significant, the SRM ban raises a number of concerns with respect to WTO requirements, including those set out in the Sanitary and Phytosanitary Agreement. It fails to recognize regional disease differences in animal disease status; and it fails to account for available scientific information and advice relating to the control of bovine spongiform encephalopathy (BSE) and other transmissible spongiform encephalopathies (TSE) in products of animal origin. As a result, the ban is unnecessarily restrictive. For example, products of the United States and other trading partners, which have no evidence of BSE, are currently affected.

In November 1998, the EU Commission developed a proposal to address the overall, long term problem of TSEs, and proposed measures which would be implemented pending the formal adoption of the TSE proposal under co-decision with the EU Council of Ministers and the EU Parliament. Both would apply only to the production and placing on the market of live animals and products of animal origin which are destined for use in human food, animal feed or fertilizers, and explicitly exclude cosmetics and pharmaceuticals. Provisions of the two measures are based on recommendations of the International Office of Epizootics (OIE) for BSE. The TSE proposal could take up to two years to be adopted. On December 15, EU Agriculture Ministers rejected the interim measures proposal, but agreed to postpone the SRM ban until January 1, 2000.

EU Approval of Third Country Establishments Exporting Animal Products

The implementation of a 1992 EU directive, requiring that practically all animal products imported in the EU have to be sourced from third country establishments approved by the European Commission, has effectively resulted in trade losses for U.S. companies. The approval process entails that competent third country authorities compile for each product category a list of establishments and guarantee that these establishments meet EU animal and public health requirements. This list is submitted to the Commission services for approval. All amendments to the existing list, including additions, deletions, name changes also have to be submitted to the Commission. The Commission, however, has not devoted the necessary resources to process submitted lists in a timely manner.

As a result, companies with export opportunities have had to wait for months before being added to an approved list and have thus been cut off from the European market. This problem has been especially acute in the dairy sector, but as the directive is further implemented to also cover important U.S. export products such as animal casings and pet food, similar trade disruptions in these sectors are likely in the near future.

Veterinary Equivalency

The United States and the European Commission concluded negotiations on a veterinary equivalency agreement in April 1997 after over four years of often contentious discussions. This agreement translates the principles of the World Trade Organization Agreement on the Application of Sanitary and Phytosanitary Measures into practical and workable terms. The agreement establishes a framework for the exporting country to make an objective demonstration to the importing country that its sanitary measures achieve the importing country's appropriate level of protection when such measures differ. By establishing clear criteria for reaching a determination of equivalence,

this agreement will facilitate trade in live animals and animal products. When implemented, the agreement will establish the terms of trade for nearly all animal products, including dairy products, pet food, fishery and egg products, between the United States and the EU, representing over $3 billion annually.

The EU Council of Agriculture Ministers approved the Agreement in principle on March 16, 1998 contingent on U.S. publication of a proposed final rule in the U.S. Federal Register on the EU animal disease status. The final rule on recognition of freedom from Newcastle disease, foot and mouth disease and rinderpest in the EU was published in November 1998. The proposed rule on the EU status for classical swine fever is expected to be published in late spring of 1999.

Proposals on Aflatoxin Limits

In July 1998, the EU adopted a regulation harmonizing maximum levels of aflatoxin in peanuts, tree nuts and dried fruits, cereals and milk, effective January 1, 1999. At the same time, a directive specifying sampling methods to be used after 31 December 2000, was adopted. The United States considers the maximum limits unjustifiably low in relation to consumer exposure and risk and believes that these levels will lead to trade disruptions without a corollary increase in consumer protection. Also, the sampling procedure will increase handling costs with no appreciable reduction of aflatoxin contamination in consumer products.

Market Access for Gas Connector Hoses in Europe

A U.S. producer of gas connector hoses has experienced difficulties in obtaining market access in some Member States for its products due to design-restrictive standards that arguably have no bearing on the safety and performance of the product. The problem has been extended to European markets generally with the establishment of a CEN (European Committee for Standardization) technical committee to begin work on a harmonized standard for Europe. Reports of initial technical discussions within the committee indicate consideration is being given to standards containing design-restrictive requirements. The initiation of work on a European regional standard results in a "standstill" on standards work in individual Member States and thus can delay or, if it results in unnecessarily restrictive standards, prevent improved access to EU markets. The U.S. Government has been actively pursuing a resolution to this problem and in cooperation with industry will be closely examining the committee's progress. There has been no substantial progress since last year.

Waste Management

European Commission officials are working on draft proposals for a directive on batteries and a directive on Waste from Electrical and Electronic Equipment. While the United States supports the objectives of the drafts to reduce waste and the environmental impact of discarded products, the manner in which these directives are written raise a number of important trade policy concerns. In particular, the draft directives' approach to banning certain essential materials (such as lead, mercury and cadmium) and mandating specific design standards appears to lack adequate scientific and economic justification and may serve as unnecessary barriers to trade. In addition, imposing the sole responsibility on the manufacturer for the collection and recycling of used products is unnecessarily burdensome.

The ban on nickel-cadmium in the current draft of the directive on batteries and accumulators appears to lack adequate scientific or economic justification and is unworkable for industry in its current form. The battery

industry presented a draft voluntary agreement in October 1998 to increase the rate of collection and recycling, but has yet to receive a response from DG-XI.

The draft directives are scheduled to be reviewed and voted on by the Commission in early 1999. If adopted, the proposals would then move to the Council and Parliament sometime in mid-to-late 1999. The United States Government will continue to monitor closely these proposals.

The United States is also concerned about a draft directive on the disposal of end-of-life vehicles. The directive contains substance bans that do not appear to be justified by scientific risk assessments, and which would, if implemented, impose onerous burdens on vehicle producers.

Voluntary Eco-labeling Program

On March 23, 1992, the EU Council of Ministers approved an EU-wide eco-labeling scheme. The scheme is a voluntary program which permits a manufacturer to obtain an eco-label for a product when its production and life-cycle meet general and specific criteria established for that particular product. The program is intended to encourage consumers to purchase products according to their overall environmental performance. EU eco-label criteria have been adopted and published for twelve consumer product categories: washing machines, dishwashers, soil improvers, tissue paper products, laundry detergents, light bulbs (single-ended and double-ended), paints and varnishes, bed linens and t-shirts, photocopy paper, and refrigerators. The Commission is also developing criteria for textile products, detergents for dishwashers, personal computers and footwear, and has completed studies in six other areas, including converted paper products (e.g. notepads and envelopes).

U.S. companies have complained about the non-transparency of certain aspects of the eco-labeling development process.

A Commission proposal to revise the EU scheme faltered in 1998 due to Council and Parliament disfavor and the proposal is back with working-level officials in the Commission. EU and U.S. experts met in October 1998 and agreed to the establishment of a bilateral technical working group to discuss broad eco-labeling issues. The group pledged to have ongoing contact and to meet face-to-face at least once a year.

Packaging Labeling Requirements

In 1996, the Commission put forward a proposed directive that would establish marking requirements for packaging, to indicate recyclability and/or reusability. The United States has expressed two potential concerns with this directive. First, to the extent that the EU new marking requirements differ from other marks widely used in the United States and being developed in the ISO, the United States is concerned that packaging, marketing and distribution operations will become more complicated and costly for both U.S. and European firms wishing to sell their products abroad, without achieving any concomitant environmental benefit.

The second concern is related to Article 4 of the proposed directive, which would prohibit the application of other marks to indicate recyclable or reusable packaging. Based on U.S. experience, this requirement is likely to pose a particular problem for glass and plastic containers, as it would require companies to create new molds solely for use in the European market. Discussions underway in the ISO may go a long way to

resolving the potential problems, especially as the Commission and the European parliament have indicated their willingness to review the proposed EU marks in light of an eventual ISO agreement. As ISO has not come forward with marking requirements, the European parliament went ahead and drafted its own marking requirements which will be discussed internally prior to the vote in February 1999 and the publication of the European Parliament's proposed amendment in spring 1999. The U.S. Government will continue to monitor this issue as it proceeds through the legislative process.

Metric Labeling

The 1980 Directive adopted to harmonize systems of measurement throughout the European Union according to the international metric system mandates metric-only labeling on most products entering the EU from January 1, 2000. An exception is made in a few specific areas such as air and sea transport in all member states, distances and draught beer in the United Kingdom and Ireland. Exporters, both European and American, have publicly voiced their objections, citing the costs of complying with conflicting EU metric-only and U.S. mandatory dual labeling requirements. In February 1999, the European Commission proposed to amend the Directive by postponing its implementation date by ten years, thus extending until 2009 the transitional period during which labeling of measurement in Europe can be indicated in both metric and American units. This amendment must be approved by both the EU Council of Ministers and the European Parliament before it can go into effect.

New Aircraft Certification

The United States continues to be concerned by the possibility that European aircraft certification standards are being applied so as to impede delivery of qualified aircraft into Europe. Processes and procedures currently employed by the European Joint Aviation Authorities (JAA) appear cumbersome and arbitrary, and in any event cannot be uniformly enforced. For example, France continues to insist on an exception to the JAA's decision on certification of Boeing's new model 737 aircraft that limits the seat density of aircraft sold to carriers located in France. The JAA decision itself took an inordinately long time, during which additional conditions were imposed progressively on the U.S. firm. The United States desires a transparent, equitable process for aircraft certification that is applied consistently on both sides of the Atlantic according to the relevant bilateral airworthiness agreements.

Hushkit or New Engine Modified and Recertificated Aircraft

In 1997, pressure on EU Airport Authorities to reduce noise levels resulted in a Commission effort to develop an EU-wide noise standard. When it became clear that it would be politically impossible to agree on such a standard due to the high costs it would impose on EU manufacturers and airlines, the Commission and Member States developed an alternative proposal. That proposal effectively passes these costs to U.S. and other non-EU air carriers and to U.S. manufacturers of noise reduction technology (hushkits) and new engines for older U.S. aircraft. The Commission has provided no scientific analysis demonstrating that the regulation would actually reduce noise at European airports. The proposed regulation establishes a design standard that restricts the operation of aircraft which otherwise fully comply with the performance standard adopted by the International Civil Aviation Organization to which the EU Member States agreed. The regulation would restrict the operation of aircraft that have been modified with hushkits, no matter how quiet, or refitted with new engines that do not have a 3:0 or greater "bypass ratio". "Bypass ratio" is not a reliable indicator of aircraft noise, but this distinction

would still permit the operation of EU-produced engines, which compete with those restricted by the regulation, that have a “bypass ratio” of 3.1:1.

Acceleration of the Phase-outs of HCFCs

The European Commission adopted a proposal in July 1998 to amend EU Regulation 3093/94 on substances that deplete the ozone layer. The United States Government actively opposed early drafts, which included phase-outs of some hydrochlorofluorocarbons (HCFCs) by 2000 or 2001, and would have disadvantaged U.S. producers while not necessarily benefitting the environment. The final draft, however, adopted a January 1, 2003 phase-out date for HCFCs used in refrigerated foam—in line with U.S. law—thereby protecting the export to the EU of U.S. refrigeration equipment.

The Council agreed to the 2003 date in adopting its Common Position in late December 1998. The Parliament, which voted to accelerate the date to 2002 in mid-December, will discuss the issue again in light of the Council common position and is expected to reverse its earlier decision and agree to the 2003 date. The U.S. Government will continue to monitor this proposal as it proceeds through the final stages of the legislative process.

Triple Superphosphate

The EU imposes a 93 percent water solubility standard for the fertilizer product triple superphosphate (TSP) to be marketed as “EC-Type Fertilizer.” TSP having a lower percentage water solubility can be sold in the EC, but without the “EC-Type” label. Scientific studies done to date on crops typically cultivated in EU countries show that water solubility rates of 90% or higher are not necessary to gain the agronomic benefits associated with adding TSP (or other phosphate fertilizers) to the soil. Substantially lower water solubility rates for TSP are more than adequate.

The effect of this unjustified standard is to restrict international trade in TSP and to deprive the EU consumers of TSP of the benefits of increased competition that would result if this unnecessary technical barrier to trade were eliminated. The United States has requested a justification for this standard in light of scientific opinion and trade rules.

Member State Practices

Some EU Member States have their own national practices regarding standards, testing, labeling, and certification. A brief discussion of the national practices of concern to the United States follows:

Greece: Greece insists on testing U.S. wheat shipments for Karnal Bunt disease. It will not accept USDA certificates stating that wheat comes from areas free from the disease. The testing method used provides a high evidence of false positive results and thus serves as a de facto ban on imports of U.S. wheat.

Italy: Italy's interpretation of EU sanitary and phytosanitary requirements has caused, or threatened to cause, problems for the following U.S. agricultural exports: processed meat products, wood products, poultry products, game meat, ingredients for animal feed, and seafood. In most cases, problems are limited to clarifying and satisfying import certification requirements that differ slightly from other EU countries. In other areas, such as game meat, imports are restricted pending further action by the EU Commission to

identify approved exporters. In addition, Italian imports of bull semen are restricted because of qualitative import standards for bull semen which favor domestic animals as well as high testing and registration fees.

Spain: In recent years, the transparency of Spain's product standards and certification processes has improved. Although Spain adapted its national regulations to conform to EU directives, there is still some uncertainty as to whether the earlier exemption from homologation and certification requirements for equipment imported for military use is still valid.

GOVERNMENT PROCUREMENT

Discrimination in the Utilities Sector

In 1990, in an effort to open government procurement markets within the EU, the EU adopted a utilities directive covering purchases in the water, transportation, energy, and telecommunications sectors. The directive, which went into effect in January 1993, requires open, objective bidding procedures (a benefit for U.S. firms) but discriminates against non-EU bids absent an international or bilateral agreement. The directive's discriminatory provisions were waived for the heavy electrical sector in a Memorandum of Understanding (MOU) between the United States and the EU, signed in May 1993.

On April 15, 1994, the United States and the EU concluded a procurement agreement that expanded upon the 1993 MOU. The 1994 agreement extended non-discriminatory treatment to over $100 billion of procurement on each side, including all goods procurement by all EU subcentral governments, as well as to selected procurement by 37 U.S. states and seven U.S. cities. Much of the 1994 agreement is implemented through the WTO government procurement agreement, which took effect on January 1, 1996. The discriminatory provisions of the utilities directive remain in effect in the telecommunications sector.

Member State Practices

Some EU Member States have their own national practices regarding government procurement. A brief discussion of some of the national practices of particular concern to the United States follows:

Austria: While the Austrian Government adheres to the WTO (GATT) Agreement on government procurement and does not have "buy national" laws, some major contracts are negotiated by invitation, and limited tenders and offset agreements are common in defense contracts. In 1998, a U.S. aircraft manufacturer was denied the sale of a helicopter due to pressure from a European competitor, even after the Austrian Government had approved the U.S. bid (the tender will be rebid). This pro-European bias also appears to play a role in privatization decisions, where local politicians have sometimes sought to discourage foreign bids by calling for "Austrian solutions" to privatization.

In common with other EU member states, the Austrian Government makes offset agreements a standard operating practice in defense contracts. Since 1978, the GOA has requested offsets for all military equipment purchases from foreign suppliers in excess of 300 million Austrian shillings (about USD 25 million at current exchange rates.) Theoretically, the offset allows the government to distinguish between bidders who are otherwise equally qualified. Because offsets are used to promote Austrian exports and to stimulate foreign investment in Austria, critics view the bidding system on defense contracts as vulnerable to distorting the principle of best bidder being awarded the contract.

Denmark: The Danish Government, its institutions, and entities owned by it are obligated to apply environmental and energy criteria on an equal footing with price, quality and delivery terms in their procurement of goods and services in a manner consistent with EU procurement rules. In practice, this will likely mean specification of products bearing the EU "eco-label" or products produced by firms with a satisfactory "ecoaudit." The environmental/energy requirement is likely also to spread to procurement by lower level governmental entities. The trend toward specification of environmentally certified products in government procurement raises concerns, given broader U.S. concerns with the EU ecolabeling scheme (see above).

Germany: Through four years of German implementation of the EU Utilities and Remedies Directive, U.S. firms continued to allege irregularities in public procurement bid procedures. Under the terms of the 1993 U.S.-EU Memorandum of Understanding on government procurement (and since January 1, 1996, the WTO Government Procurement Agreement), the system established for reviewing bid awards covered by the EU Utilities Directive was also made available to U.S. firms bidding on supply contracts in the heavy electrical equipment sector. The review mechanism provided an administrative means for challenging procurement practices in the electrical utilities sector, considered by many to be relatively closed to foreign suppliers. This review mechanism proved ineffective because it did not contain effective remedies.

In October 1995, the European Commission formally challenged the adequacy of Germany's implementation of the EU Remedies Directive. Moreover, in April 1996, the United States Trade Representative identified Germany under Title VII of the Omnibus Trade and Competitiveness Act of 1988 for discrimination in the heavy electrical sector. USTR suspended the imposition of the sanctions available under Title VII on October 1, 1996, following a decision by the German cabinet to address U.S. concerns and reform German procurement regulations by providing for court-based review of bid challenges, in line with EU requirements. In May 1998, the German Government passed a law incorporating the new procurement regulations, which combine administrative and judicial review, into existing German competition law. The law was approved by parliament and became effective on January 1, 1999. USTR, in consultation with industry, is monitoring the implementation of the new law to determine if it truly does improve access by U.S. companies to German procurement markets.

Greece: Greek laws and regulations concerning government procurement nominally guarantee non-discriminatory treatment of foreign suppliers. Officially, Greece also adheres to EU procurement policy, and Greece is a member of WTO Government Procurement Agreement. Nevertheless, many of the following problems still exist: occasional sole-sourcing (justified as extensions of previous contracts), loosely written specifications which are subject to varying interpretations, and preferences for technologies offered by longtime, traditional suppliers. It is also a widely held belief that firms from other EU Member States have an automatic advantage over non-EU contenders in winning Greek Government tenders. It has been noted that U.S. companies submitting joint proposals with European companies are more likely to succeed in winning a contract. Greece continues to insist on offset agreements as a condition for purchase of defense items.

In December 1996, the Greek parliament passed legislation that allows public utilities in the energy, water, transport, and telecommunications sectors to sign "term agreements" with local industry for procurement. "Term Agreements" are contracts to which Greek suppliers are given significant preference in order to support the national manufacturing base. This was made possible as a result of Greece's receipt of an extension until January 1, 1998, to implement the EU Utilities Directive. Actually, before expiration of the

extension, numerous term agreements worth billion of dollars were signed by Greek public utilities with Greek suppliers. Some of these term agreements are of 3-5 years duration, with an option of extending for another 3 years, thus excluding U.S. suppliers from vital sectors of government procurement for several years. The European Commission has been examining the expedited procedures by which these contracts were approved.

Italy: Italy's fragmented, often non-transparent government procurement practices still present obstacles to U.S. firms' participation in Italian Government procurement, despite some progress. Corruption, particularly at the local level, is still regarded as a problem in public procurement. Most recently, American companies have reported greater access to public and parastatal contracts. Italy has implemented EU regulations relating to procurement of goods and services and has made progress, with passage of the so-called “Merloni” legislation, towards more transparent laws and regulations for public procurement and open market competition. Italy has now completed implementation of national, EU and WTO procurement rules and regulations. Included in newly approved national legislation are provisions allowing project management services to be contracted out to private firms, in addition to project financing -- potentially opening up an entire new market in the engineering services sector with opportunities for U.S. firms.

EXPORT SUBSIDIES

Agricultural Product Export Subsidies

The EU grants export subsidies (restitutions) on a wide range of agricultural products including wheat, wheat flour, beef, dairy products, poultry, and certain fruits, as well as some manufactured products such as pasta. Payments are nominally based upon the difference between the EU price and the world price, usually calculated as the difference between the EU internal price and the lowest offered price by competing exporters. The Uruguay Round Agreement requires the EU to reduce export subsidies over six years by 21 percent in volume and 36 percent in value from a 1986-90 base period. Under the agreement, the EU is required to cut export subsidies by about $ 5-7 billion from recent levels. However, in a number of areas including beef, cheese, rice and olives, the EU appears to be rolling over unused subsidy from one year to the next. The United States is currently investigating this action as a possible violation of the WTO Agricultural Agreement.

Processed Cheese Export Subsidies

On October 1, 1997, Ambassador Barshefsky announced that USTR was invoking WTO dispute settlement procedures in the context of a Section 301 investigation to challenge practices by the EU that circumvent the EU commitments under the WTO to limit subsidized exports of processed cheese. Under its inward processing system for dairy products, the EU produces cheese for export from dairy components such as nonfat dry milk and butter. The processor receives a subsidy upon the cheese being exported, but the EU does not count these subsidies against its export subsidy ceiling on cheese. The United States contends this is a breach of the EU export subsidy commitments. Initial WTO Article XXII consultations with the EU on these practices were held in November 1997. The United States is considering next steps.

Canned Fruit

The United States and other canned fruit producing countries (Argentina, Australia, Brazil, Chile and South Africa) continue to consult with the European Commission regarding the EU internal support regime for canned fruit.

These governments believe that the operation of the EU support regime for fresh peaches and pears has allowed EU fruit processors to unfairly undercut the domestic and export prices for canned fruit for the EU trading partners.

Despite the EU claims of adherence to the letter of the 1985 U.S.-EC Canned Fruit Agreement, oversupply of the fresh fruit under the support regime may allow processors in certain Member States to ignore the minimum price requirements of the agreement. This issue has been raised in the WTO Committee on Agriculture, where eleven countries asked the chairman to convene consultations with the EU to address problems arising from the EU regime. The United States and 13 other countries, led by Chile, held a special meeting with the EU on canned fruit in June 1998 in Geneva. The EU did not respond to written questions provided prior to the meeting regarding the operation of its support regime for canned fruit.

Government Support for Airbus

Since the inception of the European Airbus consortium in 1967, its partner governments (France, Germany, Spain and the United Kingdom) have provided massive support to their national company partners in the consortium to aid the development, production and marketing of large civil aircraft. Since that date, the Airbus partner governments either have committed, or are in an advanced stage of consideration of providing, additional funds for derivative models of current Airbus aircraft. On February 2, 1998, the Government of the United Kingdom announced that it has agreed to a long-term loan of up to 123 million pounds (212 million dollars) toward the design and development of the new wing for the Airbus A340-500/600 aircraft. For 1999, the French parliament budgeted 644 million francs ($115 million) in reimbursable advances for this same aircraft program.

Government support for Airbus has facilitated its growth and the introduction of a range of large transport aircraft by allowing its national partner companies to avoid bearing the normal commercial risks that U.S. manufacturers face when investing in new civilian aircraft programs. Prior to the recent round of new development support, the Airbus partner governments bore 75 to 100 percent of the development costs for all major lines of Airbus aircraft and also provided other forms of support including equity infusions, debt forgiveness, debt rollovers and marketing assistance.

The individual Airbus partner companies are leading aerospace manufacturers in their home markets and, in some cases, have substantial government participation in ownership. However, last July the French Government announced a plan for the privatization of Aerospatiale. Under the plan finalized in December 1998, the Government of France transferred its minority stake in Dassault (45.76%) to Aerospatiale which was then merged with rival Aerospace company Matra Hautes Technologies, an offshoot of the Lagardère group. Matra will take a 30% to 33% stake in the new group, while another 20% will be floated on the stock market some time in April 1999. The French Government will then own less than 50% of the new Aerospace group.

The United States is concerned that the launch of new Airbus programs and the restructuring of the Airbus consortium may be used to justify additional government subsidies. The fact that Airbus captured nearly 50 percent of large civil aircraft orders in 1998 and its outstanding orders are over $90 billion clearly demonstrate that the Airbus consortium can no longer be considered an "infant industry" requiring government support. The United States also continues to be concerned that the European Commission and its Member States may attempt to influence commercial aircraft competitions in favor of Airbus aircraft in a manner inconsistent with its obligations. The 1996 National Trade Estimate Report provided examples of

such attempts. The United States will continue to monitor EU involvement in future competitions and its compliance with aircraft trade agreements**.**

To address U.S. concerns about the impact of European government support for its civil aircraft manufacturers, the United States negotiated a bilateral large aircraft agreement with the EU in 1992. This agreement expanded on the principles contained in the 1979 GATT Agreement on Trade in Civil Aircraft and contains specific disciplines on the provision of future European government support for aircraft development by Airbus and the repayment of past support. In addition, it includes a prohibition on government support for the manufacturing, marketing and sale of aircraft and a clarification of disciplines on government intervention in aircraft marketing or procurement decisions.

The United States held formal consultations with the European Commission in January and July 1998 under the terms of the 1992 bilateral agreement. At those meetings, the U.S. Government and the European Commission exchanged information under the Agreement's transparency provisions on direct and indirect government support and discussed government involvement in large civil aircraft manufacture and marketing. Ideas for improving the operation of the agreement were also examined.

Of particular concern are plans announced by European governments to provide financial support to develop new Airbus aircraft, including the A340-500/600. (In the past, some loans for Airbus programs, repayable from royalties on aircraft sold, have been effectively forgiven because projected sales did not materialize.) The U.S.-EU aircraft agreement requires that the European Union provide information to the United States on a "critical project appraisal" demonstrating the commercial viability of new aircraft programs at the time governments commit financial support to them. The EU has not yet provided the requested information.

Government Support For Airbus Suppliers

Belgium: The Government of Belgium and Belgian regional authorities are reported to subsidize Belgian aircraft component manufacturers which supply parts to Airbus Industrie. According to available information, the subsidy is provided in a foreign exchange rate guarantee program under which payments are made to a consortium of Belgian companies, Belairbus, which is an "associate member" of Airbus. The Government of Belgium and Belgian regional governments provide payments to the Belairbus companies to cover the difference between actual (i.e., marketplace) foreign exchange rates and a guaranteed rate. The specific level at which the guaranteed exchange rate was established has varied by Airbus aircraft programs as well as by the number of aircraft in each program. The United States has also posed questions to the EU under provisions of the WTO Agreement on Trade in Civil Aircraft and the Agreement on Subsidies and Countervailing Measures, the latter permits member countries to seek and obtain information on the nature of a practice maintained by another member and to clarify why it may not have been notified to the WTO as a subsidy. The EU reply failed to supply substantive answers U.S. questions but indicated that the Belgium program was being terminated.

France: In December 1997, the European Commission announced its approval of a French Government "reimbursable advance" to fund the development by European avionics companies of a new flight management system (FMS) for Airbus aircraft, the development of which by these companies the Commission said "would not be possible without aid". The Commission justified this subsidy on its estimation that a specific U.S. company had a "quasi-monopoly" on sales of FMS for Airbus aircraft and that the French Government funding would help reduce Airbus's dependence on the U.S. supplier. In fact, the

overwhelming proportion of Airbus avionics is already European sourced, and the FMS in question is installed in avionics equipment produced by one of the European companies designated to receive the subsidy. It thus appears that the intended effect of this subsidy is to entirely displace the U.S. company as a supplier of FMS for Airbus aircraft.

Government Shipbuilding Industry Support

Member States of the EU provide subsidies and other forms of aid to their shipbuilding and ship repair industries. Forms of aid have included subsidized restructuring of domestic shipbuilding industries, direct subsidies for operations and investment, indirect subsidies, home credit schemes, subsidized export credits and practices associated with public ownership of yards.

In June 1989, the Shipbuilders Council of America (SCA) filed a Section 301 petition, seeking elimination of subsidies and trade distorting measures for the commercial shipbuilding and ship repair industry. In response, USTR undertook to negotiate a multilateral agreement in the OECD to eliminate all subsidies for shipbuilding by OECD member countries. An agreement was signed in 1994 by South Korea, Japan, Norway, the United States and the EU and could enter into force only after ratification by all signatories. The initially-scheduled ratification deadline of January 1, 1996 was later extended to June 15, 1996 in order to accommodate the ratification procedures and time lines for certain signatories. The EU ratified the agreement and adopted implementing legislation in December 1995. All other signatories, except the United States, were able to ratify the agreement by the extended deadline. Although the United States has not yet ratified the agreement, the Administration supports ratification and plans to continue to push for ratification.

Until June 1998, EU aid to shipbuilding was governed by the Seventh Council Directive, which was adopted in 1990. Under the Seventh Directive, the Commission set annual ceilings for subsidies for shipbuilding and ship conversions (but not ship repair). Although the EU would have liked to see the OECD agreement implemented, on June 29, 1998, it adopted a Council Regulation establishing new rules on aid to shipbuilding because the Seventh Directive was due to expire at the end of 1998. According to the Regulation, operating aid, whose ceiling is dictated by the Seventh Directive (nine percent for shipbuilding contracts with a contract value before aid of more than ECU 10 million and 4.5 percent in all other cases), will be phased out by December 31, 2000. The shift away from operating aid to other forms of support (such as aid for restructuring, research and development and environmental protection, types of aid already covered by existing Community guidelines), is an attempt by the Commission to subject shipbuilding to the same state aid rules faced by other sectors. The Regulation aims to uphold the integrity of the common market by establishing a level shipbuilding playing field within the EU. However, the new EU regime on shipbuilding is more lenient than the OECD agreement.

LACK OF INTELLECTUAL PROPERTY PROTECTION

The EU and its Member States support strong protection for intellectual property rights. The Member States are members of all the relevant WIPO conventions, and they and the EU regularly join with the United States in encouraging other countries, primarily developing ones, to sign up to and fully enforce high IPR standards, including those in the WTO Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPs). However, there are a few Member States with whom the United States has raised concerns either through Special 301 or WTO Dispute Settlement, about failure to fully implement the TRIPs Agreement.

European Union

The U.S.-EU Transatlantic Economic Partnership (TEP) initiative, initiated at the May 1998 U.S./EU Summit, identifies intellectual property as an area where multilateral and bilateral cooperation can be intensified and extended. The TEP action plan for multilateral cooperation addresses cooperation on TRIPs implementation and WIPO treaty ratification, access to the Trademark Law Treaty, resolution of domain name trademark conflicts and pursuing measures to fight optical media piracy. On the bilateral side, a number of issues of interest to both the U.S. and the EU, including patent and design protection, will be addressed in the short- and long-term.

Industrial Designs

The European Commission proposed a directive on the Legal Protection of Industrial Designs in 1993 to provide for Community-wide registration of industrial designs, and up to a maximum of 25 years of protection against unauthorized reproduction of industrial designs. The legislation provides protection similar to a trademark with the criteria that the design must be novel and have a high degree of individual character.

A provision in the directive known as the "repair clause" has been hotly debated since the directive's appearance due to diverging Member State and industry views over design protection of spare auto parts. U.S. firms also have expressed different opinions on the issue, with U.S. auto manufacturers favoring strong protection for spare car body parts, and insurance companies and spare parts manufacturers preferring more flexibility in the directive. At a June 1998 Conciliation Committee, the Council and the European Parliament agreed to remove protection for spare parts from the proposed legislation pending further study, but to leave open the possibility of replacing it in a future amendment.

The Commission expects to finish a revision incorporating the Conciliation Committee results in early 1999, after which the legislation will return to the European Parliament under a simple consultation procedure. Whether the Council will adopt a final directive in the first half of 1999 depends on the speed with which the European Parliament issues its opinion on the compromise version. Although the parliamentary report should be pro forma, the European Parliament's 1999 session will be cut short by elections in June, leaving it little time to issue opinions. Once the directive takes effect, OHIM (the Office for Harmonization in the Internal Market – also known as the Community Trademark Office) will be the registrar for industrial designs.

Trademarks

Registration of trademarks with the European Community trademark office (official name: Office for Harmonization in the Internal Market – OHIM) began in 1996. OHIM, located in Alicante, Spain issues a single Community trademark which is valid in all 15 EU member states.

Trademark Exhaustion: The Trademark exhaustion principle limits a trademark owner's ability to resort to remedies against importers/distributors of trademarked goods outside channels authorized by the trademark owner. The current EU regime supports the principle of 'community exhaustion,' which allows resale of trademarked goods within the fifteen member states once the trademark owner licenses their sale in any EU country.

European Union

In 1998 a European Court of Justice ruling (in *Silhouette v. Hartlauer*) upheld the legality of community trademark exhaustion within the EU. The European Commission has defended the principle by maintaining that community exhaustion heightens competition within the internal market. However, member state opinion remains divided and at the insistence of the U.K. and Sweden, the Commission began a study into the economic impact of community exhaustion in the member states. European discount chains prefer, and have actively lobbied for, a system of 'international exhaustion,' which limits the trademark owner's right to control distribution of goods once he/she licenses them for sale anywhere in the world.

Madrid Protocol: The World Intellectual Property Organization's (WIPO) Madrid Protocol, negotiated in 1989, provides for an international trademark registration system permitting trademark owners to register in member countries by filing a standardized application. The European Community has not joined the Madrid Protocol although member states have. The U.S. has not acceded because it objects to voting provisions in the protocol that would allow the EC a vote upon accession in addition to the votes of its member states. Given the use of consensus decision-making procedures in WIPO and in the precursor Madrid Agreement, the U.S. has proposed an informal "gentlemen's agreement" that would establish voting procedures to address U.S. concerns about the EU vote in the Madrid Protocol. The EU has not yet responded to the U.S. proposal.

Utility Models: In 1997 the European Commission proposed a directive on utility models to harmonize a level of protection in the member states for industrial applications lower than that granted for patents. Under the directive, protection would apply to "any inventions susceptible to industrial application, which are new and involve an inventive step" for a maximum of ten years. Utility model protection may also provide temporary protection pending granting of a patent. Business groups have criticized the directive as being unclear and ambiguous, noting that implementation may do more harm than good by introducing additional business costs. It is unlikely the directive will reach adoption in the near term. However, both European and U.S. industry are united in disagreeing with the Commission that harmonization of this type is needed in Europe.

Geographical Indications: U.S. industry has expressed concern about the 1992 EU Regulation on "Protection of Geographical Indications and Designations of Origin for Agricultural Products and Foodstuffs" as amended by a 1997 regulation. Some believe it does not achieve a balance between protection for legitimate trademarks and legitimate geographical indicators. In practice, the regulation could bring registered trademarks in conflict with registered geographical indicators.

Patents

Patent filing and maintenance fees in the EU and its member states are extraordinarily expensive relative to other countries. Fees associated with the filing, issuance and maintenance of a patent over its life far exceed those in the United States. In an effort to introduce more reasonable costs, the European Patent Office (EPO) reduced fees for filing by 20 percent in 1997.

European Community Patent: The European Commission consultation process on a European Community Patent (one that would harmonize patent issuance in EU member states) has yielded a number of conclusions in the Commission's Green Paper. The paper acknowledges a consensus on the need for a harmonized patent system among EU member states, and proposes that such a system supplement -- not replace -- patents issued by the European Patent Office (EPO) in Munich (with a wider membership than the fifteen member states)

and national patent offices. In addition, the Commission believes the cost of an EC patent shouldn't be more than a U.S. or Japanese patent and that EU law on patentability of computer programs and software related inventions must be brought into line with the United States and Japan. The Commission will advance legislation for a European Community patent in late 1999. However, a stumbling block to this effort is disagreement among member states on which official EU languages will be used in patent applications.

Ireland: As part of the promised comprehensive copyright legislation, the Irish Government is also committed to addressing non-TRIPS conforming provisions of Irish patent law. Ireland's patent law, as it currently stands, fails to meet TRIPs obligations in at least two respects: (1) the compulsory licensing provisions of the 1992 patent law are inconsistent with the "working" requirement prohibition of TRIPs articles 27.1 and the general compulsory licensing provisions of article 31; and (2) compulsory licensing conditions provided for in the 1964 patent law, which continues to apply in some applications processed after December 20, 1991, do not conform to the non-discrimination requirement of TRIPs article 27.1.

Biotechnological Patenting

On June 16, 1998, after years of debate, the European Council adopted a directive on legal protection of biotechnological inventions. The directive harmonizes EU member state rules on patent protection for biotechnological inventions. Member states must bring their national laws into compliance with the directive by July 30, 2000. The directive excludes plant and animal varieties from patentability and, although a positive development for U.S. firms, will not provide the same level of patent protection that is provided in the United States to biotechnological inventions. In addition, the directive is not binding on the European Patent Office.

Copyrights

In April 1998, the European Commission proposed a directive on the "Harmonization of Certain Aspects of Copyright and Related Rights in the Information Society". The directive would require member states to implement harmonized regulations on the protection of copyrights and is seen as a first step in granting copyright protection for works in digital form. Although the directive was proposed following a lengthy consultation process, its provisions are controversial, especially a mandatory exception for private copying and for temporary reproductions that are "integral" to a technological process and have no separate economic significance. The European Parliament is expected to propose extensive amendments to the legislation in a 'first-reading' in February 1999. However, it is unlikely that the Council will adopt a final version in the first half of 1999.

Copyright Protection for Databases: By January 1, 1998, member states were required to transpose into national law the 1996 EU directive on the legal protection of databases. A new 'sui generis' right extends copyright protection for fifteen years to the contents of a database, whether or not the material is otherwise eligible for copyright protection. However, this right is available to non-EU creators of databases only on the basis of reciprocity. The U.S. business community, while supportive of protection for databases as essential to a sound legal framework for Europe's information society, remains concerned about the impact the reciprocity provisions of the directive will have on U.S. publishers of databases. Scientists worry that the directive will make access to databases prohibitively expensive although the directive permits member states to allow exemptions for groups accessing data for research or education.

Member State Practices

Some EU Member States have their own special practices regarding intellectual property protection and enforcement that do not necessarily comply with international obligations. A brief discussion of those which are of concern to the United States follows:

Austrian copyright law also requires that a license fee be paid on imports of home video cassettes and cable transmission. Of these fees, 51 percent are paid into a fund dedicated to social and cultural projects. In the United States' view, the copyright owners should receive the revenues generated from these fees and any deductions for cultural purposes should be held to a minimum.

Belgium, France: Belgium and France collect levies on blank tapes and recording equipment to compensate right holders for the private, home copying of their works and to provide a source of funding for local productions. These levies are distributed by national collecting societies to the various categories of right holders according to statutory provisions. National treatment is denied to some U.S. right holders, however, and the United States motion picture and recording industries have not been able to collect their rightful share of these proceeds.

Denmark: Denmark's intellectual property laws are generally adequate. However, certain problems exist. Denmark was named on the 1998 Special 301 Watch List because enforcement is made difficult by the fact that the Danish Government does not make available provisional relief on an *ex parte* basis to prevent ongoing infringement or preserve evidence in the context of civil litigation. Article 50.1 of the TRIPs Agreement requires that such provisional relief be made available in civil or criminal litigation. The availability of such relief is particularly important to the United States software industry because of the ease with which the evidence of infringing use can be eliminated if the infringers are forewarned of the right holder's interest. In response, the Danish Government has set up a committee to find out which legislative changes are needed in Danish copyright laws and other related legislation to meet its TRIPs requirements.

Furthermore, Denmark's equivalent of the Environmental Protection Agency is at present compelled by a Supreme Court ruling to permit competitors to rely upon extremely valuable test data for certain chemical products that a U.S. firm has submitted in order to receive approval to market its products in Denmark. This contravenes the objective of the TRIPs Agreement and perhaps TRIPs Article 39.3.

U.S. authors do not receive royalties from Denmark for photocopying of their works used in Danish schools and universities, because the Danish collecting agency Copydan will not accept the validity of "en bloc" powers of attorney issued by U.S. publisher and author organizations. Copydan maintains that it will pay only

to a U.S. collecting agency built on a model similar to its own. This issue is being pursued at present on an informal basis with the Danish Government.

Finland: Finland is working to achieve compliance with its obligations under the TRIPs Agreement in regard to *ex parte* searches. There is a support for a legislative fix for the matter and simple provisional changes to the law are already in the drafting stage.

Greece: Greece has been on the Special 301 Priority Watch List since 1994. Just prior to an out-of-cycle review in December 1996, the Greek Government submitted an "action plan" laying out the steps it would take by April 1997 to reduce audio-visual piracy. While some of these steps were taken, the Greek Government has lagged behind severely in licensing television stations in accordance with the provisions of the 1995 media law. The process, while finally underway after extremely long delays, was less than completed by December 1998. The U.S. Government launched a WTO TRIPs non-enforcement challenge and consultations under WTO auspices were started in June 1998. Consultations continue. Two other significant IPR problems are lack of effective protection of copyrighted software and of trademarked products in the apparel sector.

Ireland: Ireland is a member of the World Intellectual Property Organization and a party to TRIPs. Following intensive negotiations with the U.S. Government in 1997, the Irish Government committed to introducing into the parliament new copyright legislation by December 31, 1998, to bring Ireland's laws into line with its obligations under the TRIPs agreement. Dublin also agreed to enact a new smaller "break-out" copyright bill in advance of comprehensive legislation, which would address the Government's most pressing concerns with regard to Irish copyright protection.

This breakout bill was enacted in June 1998, and among other provisions, strengthened the presumption of copyright ownership and increased penalties for copyright violation. In mid-December 1998, the Irish Government informed USTR that because of delay in drafting the comprehensive legislation, the Irish Government would not be able to introduce the legislation in the Irish parliament by the December 1998 target. The Irish Government informed USTR that it now intends to introduce the new legislation no later than March 1999 and to make every effort to have it enacted by July 1999.

Examples of TRIPs inconsistencies in current Irish law which the government is committed to addressing in comprehensive reform legislation by the 1999 deadline include absence of a rental right for sound recordings, and no "anti-bootlegging" provision. An Irish failure to enact the legislation in accordance with its commitments may affect the 1999 section 301 review.

Italy: In 1998, the U.S. Trade Representative placed Italy on the “Priority Watch List” under the Special 301 provision of the United States Omnibus Trade and Competitiveness Act of 1988, due to national TV broadcast quotas in excess of the EU norm (see Services Barriers), and to a lengthy delay in passage of national legislation to address ongoing serious deficiencies in protection of copyright for sound recording, computer software and film videos. In October 1996, the Italian Government introduced anti-piracy

legislation in Parliament that would impose administrative penalties and increase criminal sanctions. The bill is still awaiting final Parliamentary approval. The United States will continue to monitor developments in this area closely.

Portugal: Portugal's laws on the protection of intellectual property do not provide adequate protection for test data submitted to regulatory authorities for marketing approval of certain products (including pharmaceuticals) as required by the WTO TRIPs Agreement. Portugal is currently in the process of updating several articles of its existing legislation, including the section which covers the protection of test data. The United States has informed Portugal of its concerns in this regard and will monitor the development and implementation of changes to the legislation.

Spain: Business statistics indicate that software piracy declined in Spain from 74 percent in 1995 to 59 percent in 1997, but still remains at a high level. U.S. companies hope that the judiciary will provide support for this problem by processing piracy cases expeditiously and by imposing adequate penalties on offenders. In recent years, the Spanish Government has increased its efforts to educate both the police and the judiciary as to the economic significance of this problem.

Sweden: While Swedish intellectual property laws are satisfactory, their enforcement has been problematic. The Swedish Government has not provided sufficient financial or personnel resources or training to the police and prosecutor's office, nor has it made IPR enforcement a top priority. During the past year, however, the Government has amended its law to allow for provisional relief in the context of civil searches in copyright enforcement cases, an action that has improved the software industry's greatest copyright enforcement problem. Another problem area, in which a conflict exists between the Swedish constitution's guarantee of freedom of information and the rights of copyright holders of unpublished works remains unsolved, although the Government has begun the process of changing its law to protect unpublished works.

SERVICES BARRIERS

Broadcast Directive and Motion Picture Quotas

In 1989, the EU issued the Broadcast Directive which included a provision requiring that a majority of entertainment broadcast transmission time be reserved for European origin programs "where practicable" and "by appropriate means." By the end of 1993, all EU Member States had enacted legislation implementing the Broadcast Directive.

The process begun by the Commission in 1993 to revise the Broadcast Directive in an effort to strengthen quotas was concluded in April 1997 through a conciliation committee that resolved differences between the European Parliament and the Council. By the time an agreement was reached on a revised directive, the divisive issue of strengthening European content quotas and expansion of the directive's scope to new services had fallen by the wayside despite the Parliament's protectionist line. The United States continues to monitor developments with respect to the Broadcast Directive.

Several countries have specific legislation that hinders the free flow of some programming. A summary of some of the more salient restrictive national practices follows:

France: The language of the EU Broadcast Directive was introduced into French legislation in 1992. France, however, chose to specify a percentage of European programming (60 percent) and French programming (40 percent) which exceeded the requirements of the Broadcast Directive. Moreover, the 60 percent European/40 percent French quotas apply to both the 24-hour day and to prime time slots. (The definition of prime time differs from network to network according to a yearly assessment by France's broadcasting authority, the "Conseil Supérieur de l'Audiovisuel," or CSA.) The prime time rules in particular limit the access of U.S. programs to the lucrative French prime time market. France's broadcasting quotas were approved by the European Commission and became effective in July 1992.

In addition, the United States continues to be concerned about the French radio broadcast quota (40 percent of songs on almost all French private and public radio stations must be Francophone) which entered into force on January 1, 1996. The measure has the effect of limiting the broadcast share of American music.

Italy: In 1998, the Italian Parliament passed Italian Government-sponsored legislation including a provision which makes Italy's national TV broadcast quota stricter than the EU 1989 Broadcast Directive. The Italian law exceeds the EU Directive by making 51 percent European content mandatory during prime time, and by excluding talk shows from the programming that may be counted towards fulfilling the quota. Also in 1998, the Italian Government issued a regulation requiring all multiplex movie theaters of more than 1300 seats to reserve 15-20 percent of their seats, distributed over no fewer than three screens, to showing EU-origin films on a "stable" basis. Cinema owners argue that "stable" needs to be interpreted flexibly (i.e., the quotas applied on a yearly rather than daily basis) in order to ensure continued profitability. Indications are that the government intends to apply the quota on a daily basis.

Portugal : In July, 1998, Portugal passed new television legislation containing language from the EU broadcast directive. The new legislation modifies and strengthens the existing quotas for Portuguese language, European, and independent productions. The new law, however, also includes provisions for flexible application of these quotas. In practice, available Portuguese and European programming is insufficient for broadcasting needs and, consequently, the quotas have not been strictly enforced. Portugal is also considering new draft cinema legislation, which may allow the imposition of distribution and screen quotas. The United States will closely monitor the implementation of this restrictive legislation.

Spain: Draft legislation implementing the revised EU Broadcast Directive awaits final parliamentary action, which is expected in 1999. The proposed new law maintains the same restrictions on non-EU programming as in the earlier law; i.e. it reserves a majority of broadcast time for European content programming. Both government-owned and private television networks readily meet the EU content requirements and according to government officials, no operator has had to alter its programming to comply with the directive since the viewing public has a preference for content that is culturally and linguistically Spanish. Although U.S. programs might have increased sales without the quota provisions of the directive, in fact American films and popular TV serials form a sizeable portion of prime time viewing.

In January 1997, Spain issued regulations implementing the 1994 cinema law that obliged distributors to earn dubbing licenses for non-EU produced films by distributing EU-produced films. The law stipulates that the first license is earned when box office receipts exceed 10 million pesetas ($70,500); a second when they exceed 20 million ($141,000); and a third when they exceed 30 million ($211,500). However, the regulations also included a provision that the dubbing license requirement would be phased out at the end of five years, i.e. by the end of 1999. Nevertheless, the screen quota provision, which requires motion picture exhibitors

in the course of each year to show one day of EU-produced films every three days of non-EU produced films, remains in effect.

In January 1998, the regional government of Catalunya adopted a Law on Linguistic Policy. One of the implementing decrees, scheduled to go into effect in March 1999, imposes film dubbing and screen quotas, which could have a negative economic impact on distributors and exhibitors alike. The decree stipulates that if a film opens with sixteen or more copies being shown at once, 50 percent of the copies would have to be dubbed into Catalan.

The decree also obliges exhibitors and reserve a minimum of 25 percent of their showings of sound films dubbed or subtitles in Catalan, a percentage that would be calculated on the basis of one year's programming. U.S. film companies active in the Spanish market welcome the end of the national dubbing license requirement by the end of 1999, but are concerned about the precedent that would be set for linguistic minorities in other regions of Spain if the Catalan law imposing dubbing and screen quotas goes into effect.

Computer Reservation Services

U.S. computer reservation systems (CRS) companies continue to face problems in the EU market, since several Member State markets are dominated by a CRS owned by that State's flag air carrier. Past cases have eventually been resolved after U.S. Government intervention or recourse to national administrative and court systems.

Acting on a complaint filed in 1996, the U.S. Department of Justice asked the EU competition authority to investigate a range of anti-competitive practices by a European firm. This was the first case under the positive comity provision of the 1991 U.S.-EU Antitrust Cooperation Agreement. The EU investigation is still underway as of February 1999; while the Commission cannot say when it will be completed, the final ruling may address some of the above concerns. The U.S. firm has also filed a complaint with the EU transportation authority against the European firm for violation of the EU CRS Code of Conduct.

There is also concern about how Swedish data protection regulations apply to American CRS operations in that country. One U.S-owned CRS firm complains that Sweden is the only EU member state in which it has not either already received or will soon receive data protection-related permits for its operations. The Swedish argument is based on the concern about levels of data privacy protection in the United States and on passenger notification issues. Resolution of the matter is being sought in the Swedish court system and under the U.S. –Swedish bilateral aviation agreement, and a decision is expected by mid-1999.

Airport Ground Handling

In October 1996, the EU issued a directive to liberalize the market to provide ground-handling services at EU airports above a certain size by January 1, 1998. While generally welcoming this move, U.S. airline companies and ground-handling service providers remain concerned that airports can apply for exemptions to continue to have a monopoly service provider through January 1, 2002, and can also limit the number of firms which can provide certain services on the airport tarmac (ramp, fuel, baggage and mail/freight handling) either for themselves or for other carriers. To some extent, these potential barriers are offset by more liberal provisions in the bilateral air services agreements which the United States concluded with eight

EU Member States (Austria, Germany, Belgium, the Netherlands, Luxembourg, Denmark, Sweden and Finland).

Germany: In January 1998, Commission competition authorities - acting on a complaint by several EU airlines – ruled that Frankfurt Airport Terminal Two and the western portion of Terminal One would have to permit airlines to handle baggage for their clients (self-handling) and by January 1, 1999 would have to authorize a third independent baggage handling service provider. Frankfurt had requested a derogation from the directive until January 1, 2001. This was the first decision under the 1996 directive.

Ireland: Airlines serving Ireland may provide their own ground handling services, but are prohibited from providing similar services to other airlines. The bilateral U.S.-Ireland aviation agreement places some restrictions on aviation services between the United States and Ireland. Under the agreement, for every north Atlantic flight to or from Dublin airport, a corresponding flight or stop must be made at Shannon airport on Ireland's west coast, making service to Ireland unprofitable for some U.S. airlines. U.S. carriers have told embassy that the "Shannon requirement" affects the profitability of their operations in Ireland, but has not stopped U.S. carriers from introducing new service between Ireland and the United States to start in 1999.

Postal Services

U.S. express package services remain concerned that the prevalence of postal monopolies in many EU countries restricts their market access and subjects them to unequal competitive conditions. Proposals to liberalize many postal services have made little headway in the face of entrenched Member State opposition, and the European parliament still expects a proposal from the Commission on the liberalization of postal services and a study on its impact on trade and markets. In the meantime, a U.S. firm has filed a complaint with the EU antitrust authority against the German Post for predatory pricing, abuse of dominant position, state aid and unfair cross-subsidization of services. The case, pending since 1994, has made little progress to date, apparently due to reluctance by the EU authority to act decisively against the German Government. The U.S. firm is concerned that the German Post is using subsidies to finance acquisitions and investments to strengthen even further its market position vis-a-vis private sector express delivery services. The company fears that further delay by the EU in ruling on the case will only exacerbate the unfair competitive situation.

Exemptions from Most-Favored-Nation Treatment

In January 1995, the EU notified the WTO of its intent to present a new draft General Agreement on Trade in Services (GATS) schedule of commitments, with accompanying list of MFN exemptions, to reflect the enlargement of the EU to include Austria, Finland, and Sweden. Two years later, in January 1997, the EU presented the draft document, which was discussed for the first time at a meeting of the WTO working party examining the consistency of the enlarged EU with Article V of the GATS (Article V is the services counterpart to GATT Article XXIV). At that meeting, the United States and other countries raised legal concerns that the draft expands to the three new Member States a number of MFN exemptions contained in the already existing EU-12 GATS MFN exemption list, thereby creating new opportunities for the three new Member States to discriminate against service providers of non-EU countries. The United States will seek to ensure that EU enlargement in the services area is consistent with the EU's WTO obligations.

Auditing Services

Greece: The transition period for de-monopolization of the Greek audit industry officially ended on July 1, 1997. Numerous attempts to reserve a portion of the market for the former state audit monopoly during the transition period (1994-97) were blocked by the European Commission and peer review in the OECD. In November 1997, the government issued a presidential decree which effectively undermines the competitiveness of the multinational auditing firms. The decree established minimum fees for audits, and restrictions on utilization of different types of personnel in audits. It also prohibited audit firms from doing multiple tasks for a client, thus raising the cost of audit work. The government has defended these regulations as necessary to ensure quality and objectivity of audits. In practical effect, the decree constitutes a step back from deregulation of the industry.

Shipping Restrictions

Spain: In 1992, the EU established a calendar for liberalizing cabotage restrictions, but only to vessels registered in a member country. The 1992 agreement among the EU member countries on a common cabotage regime is to be implemented during a transition period from 1993 to 2004. While cabotage within peninsular Spain has been liberalized, the EU has allowed Spain to restrict merchant navigation to and within the Balearic Islands, the Canary Islands and CEUTA and Melilla to Spanish flag merchant vessels until January 1, 1999. The Spanish Government has begun to liberalize merchant navigation for these routes, most recently holding a bid for a six-year contract for routes with inadequate service levels. However, state-owned company Transmediterranea was the only bidder for these routes.

Telecommunications Market Access

U.S. telecommunications equipment industry access to EU Member States varies widely from relatively open to nearly closed. As described in the section on government procurement, most EU Member States discriminate against non-EU bids in the telecommunications sector. Increasing privatization of the telecommunications sector in Europe may in the long-run make procurement less of an issue, but access may still be impeded through standards and standard-setting procedures, testing, certification and interconnection policies.

In the area of standards, the United States has raised concerns about the EU approach to standards for third generation wireless systems currently referred to as “3-G”. In December 1998, the EU Council and Parliament approved a decision on the coordinated introduction of a third generation mobile and wireless communications system called UMTS (Universal Mobile Telecommunications Systems). The decision calls for the establishment of a harmonized system for the granting of operating licenses by January 2000 and a common technology standard approved by the European Telecommunications Standards Institute (ETSI). The decision sets January 1, 2002 as the deadline for launching UMTS. The United States has expressed concern that this action, as well as moves by some Member States to grant licenses and reserve frequencies for UMTS, promotes a particular European-developed standard to the exclusion of other standards, bypassing industry-led efforts within the ITU (International Telecommunications Union) to achieve a global consensus.

Under the WTO Agreement on Basic Telecommunications Services, eleven Member States made commitments to provide market access and national treatment for voice telephony services as of February

5, 1998, the date the agreement entered into force. Four Member States had later phase-in dates: Spain (December 1, 1998), Ireland and Portugal (January 1, 2000) and Greece (January 1, 2003). Three Member States maintain foreign investment restrictions: France limits investment in France Telecom; Italy limits foreign investment in STET; and Spain limits foreign investment by government-owned operators. The European Communities and its Member States also adopted the pro-competitive regulatory commitments set forth in the Reference Paper associated with the WTO Agreement. All EU Member States have now formally ratified the Agreement.

The European Commission has been monitoring and reporting regularly on the implementation of telecom liberalization within the EU. The fourth report was released in December 1998. The report concluded that the bulk of the measures in the telecommunications package had been transposed into national legislation by the Member States, although some gaps remained. As of October 1998, the Commission was pursuing 84 infringement proceedings against Member States with respect to the regulatory package.

The Commission reported that telecommunications regulatory authorities had been established in all Member States, but expressed concern about the operation of some of these bodies. In several Member States, regulatory functions are allocated both to the Ministry responsible for telecommunications and to a separate administrative body. In a few cases (The Netherlands, Austria), the Commission observed a lack of clarity in the division of powers. In some member states (Belgium, Finland, Luxembourg, Ireland, France) it was noted that regulatory decisions could be influenced by State ownership considerations. Concerns were also noted about inadequate staffing by the regulators (Belgium, Greece, Italy, Luxembourg) or the seconding of staffing from telecom operators or government Ministries to the regulator (Greece, Portugal, Ireland).

The Commission report cited concerns with respect to licensing conditions (Belgium, Spain, France, Italy), lack of transparency in licensing (Ireland), the level of license fees (Germany, France; Luxembourg and Italy for mobile), time limits for the issuance of licenses (Belgium, Greece, France, Italy, Luxembourg), and cumbersome licensing procedures (Austria, Belgium, Italy, Spain). There are limitations on the numbers of licenses issued in Greece and Belgium has so far granted only provisional licenses.

In the area of interconnection, new entrants have complained that negotiations have been excessively lengthy in a number of Member States (Belgium, Germany, France, Austria), or have been refused or deferred because the incumbent has first required the other party to obtain a licenses (Italy, Luxembourg) or because of other issues (Denmark, Sweden). Substantial interconnection disputes have been reported in Denmark, Germany, Austria, Sweden, the United Kingdom and Greece. Only in France and the United Kingdom do interconnection charges fully meet the "best practice" targets set by the Commission. Charges in other Member States are higher for one or more types of services.

France requires new entrants to contribute to a fund to finance the cost of universal service. Italy has created a funding mechanism which will be applied in 1999 based on operators' results for 1998. The report notes that the methodology for calculating charges is a matter of concern for both countries.

The Commission report observes that in some Member States the present tariff structure of voice telephony provided by the incumbent operator appears to be artificial and that end-user tariffs do not follow principles of cost orientation. Some Member States do not have an appropriate cost accounting system for public telecom networks/services (Greece, Ireland, Portugal, Spain). In others, telecom operators with significant

market power do not have such a system in place (Belgium, Luxembourg) or the system lacks sufficient transparency to ensure the absence of cross-subsidization (Austria, France, Germany, Italy, Sweden).

Germany: Beginning in December 1998, Deutsche Telekom (DT) sought to revoke existing interconnection agreements and to impose additional charges, based on technical claims which DT has not yet substantiated. In response, the regulator so far has announced only that it will investigate complaints regarding DT's approach on an ex post facto basis. As a result new entrants, many of who have already faced delays of up to a year in interconnection negotiations with DT, confront worsened business conditions. DT's latest proposal appears unilaterally to impose non-justified technical requirements and unrelated charges on interconnection that are not based on costs. If so, it would create serious concern as to whether Germany is adhering to its WTO commitment that interconnection be provided in a timely fashion, on terms, conditions and cost-oriented rates that are transparent and reasonable.

Italy: In recent years, the Italian Government has undertaken a liberalization of the telecom sector, including privatization of the former parastatal monopoly Telecom Italia (formerly STET); creation of an independent communications authority; and allowing both fixed-line and mobile competitors to challenge the former monopoly. Following the EU January 1, 1998 deadline for full liberalization of its telecom sector, Italy issued more than a dozen fixed-line licenses in 1998, including to new entrants with U.S. participation. The government plans to issue a fourth mobile license in the first half of 1999. Concerns remain regarding interconnection fees and conditions; frequency allocation for mobile carriers; regulatory due process, transparency and even-handedness. But the Italian market is much more open to services exports in this sector than it was even one year ago, at the time of the previous report.

Belgium: Belgium amended its Telecommunications Act to provide the domestic legal basis to implement its obligations under the WTO Telecommunications Agreement on December 18, 1997. Key implementing regulations yet to be issued include those to formally establish a body to resolve interconnection tariff disputes and to govern to the utilization of telecommunications infrastructure. Industry sources note that the system lacks transparency, as the complete body of relevant legislation and implementing regulations is not easily available. The Belgian regulator, the Belgian Institute for Postal Services and Telecommunications (BIPT), is supervised by the Minister of Telecommunications, who is also responsible for the Belgian government's 51 percent shareholding in Belgacom, the former monopoly telecommunications supplier. While BIPT has won praise for its early efforts to introduce competition in a newly liberalized market, industry observers agree that increased independence and resources for BIPT would strengthen its ability to provide pro-competitive regulation. Interconnection rates in Belgium remain above the European average. Telecommunication operators and service providers in Belgium criticized Belgacom's 1999 reference interconnection offer, an average reduction of 15 percent, as unacceptably high and unlikely to ensure growth and competition.

Legal Services

Austria: To provide legal advice on foreign and international law, the establishment of a commercial presence is required as well as joining the Austrian Provincial Bar Association. Only an Austrian national can join the bar association.

Belgium: In order to be licensed to practice Belgian law, one must be a graduate of a Belgian university five year course of study. There is some provision for recognition of U.S. education which usually amounts to

2 or 3 years of part time study at a Belgian university to get the Belgian degree. There is a mutual recognition directive which will mean EU law degrees will be recognized. But U.S. degrees still will not.

Denmark: Foreign lawyers in Denmark cannot offer advice to international clients on international issues without being a member of the local bar, face restrictions on whom the foreign lawyer or law firm may advise and also face restrictions on the use of the original business name as in its home country.

Foreign legal consultants are restricted in their ability to advertise, including restrictions on the use of letterhead or signs on office doors. These restrictions are not applied to attorneys licensed to practice Danish law.

There are restrictions on the ability of foreign lawyers to associate with Danish lawyers. Foreign attorneys may hire Danish attorneys in private firms but foreign attorneys who are appointed as attorneys by Denmark cannot own a Danish firm. Also foreign attorneys who do not also have appointment as Danish attorneys cannot be partners in a Danish legal firm.

To be an attorney in Denmark, a person must be A Danish legal school graduate and a clerk in a law firm for three years.

France: There is a nationality requirement to quality as an "avocat."

Legal consultancy services in foreign and international law are required to be licensed in French law.

Non-EU firms are not permitted to establish branch offices in France under their own names. Also, foreign lawyers and firms are not permitted to form partnerships with or hire French lawyers.

Germany: There is a prohibition on foreign lawyers entering into professional associations with "rechtsanwalte."

Foreign legal education is difficult to obtain. It is estimated that a minimum of three years of study and another three or four years of internship after law school would be necessary prior to taking the German Federal bar examination.

Residence and the maintenance of an office in the judicial district where the attorney is admitted are prerequisites to maintaining one's status as a lawyer in Germany.

There are indirect citizenship requirements which are prerequisites for becoming licensed to practice German law. Also, residence and the maintenance of an office in the judicial district where the attorney is admitted are prerequisite to maintaining one's status as a lawyer in Germany.

Italy: There is a citizenship requirement for admission to the Italian bar. In addition, U.S. lawyers cannot offer advice on foreign and international law without being licensed in the practice of Italian law.

Netherlands: Foreign lawyers are not permitted to form partnership with Dutch lawyers. In addition, a foreign lawyer established in association with a Dutch firm must have practiced in his home jurisdiction for

at least three years and must agree to subject himself to the rules of ethics and supervision of the Dutch Bar Association.

Spain: There are nationality requirements to sit for the Spanish bar exam. Spain does not have a national bar exam nor do states (autonomous communities) give bar exams. Spanish graduates of approved law schools, once they are admitted to a state/regional bar association, a pro forma procedures, are entitled to practice law in that jurisdiction. Foreign graduates of approved law schools will receive national treatment provided reciprocity exists for a qualified Spaniard to practice law in the foreigner's country or state.

United Kingdom: The become a barrister, a litigator may be required to pass a one year diploma in law offered by certain polytechnics in London, complete a one year practical course at the Inns of Court School of Lw in London after joining one of the four Inns of Court, and complete a one year "pupilage" with a barrister in chambers.

To become a solicitor, a New York lawyer may be required to pass a one year diploma in law offered by certain polytechnics in London, complete a one year course for the solicitors' final examination and pass the examination, and complete a two year "articled clerkship" with a solicitor or firm of solicitors.

Accounting Services:

Austria: Citizenship is required to obtain a professional certification. Foreign accountants are not permitted to form a partnership with local firms. There are problems with using the international firm's name.

Belgium: There are difficulties obtaining fees as there are restrictions on fees to international firms.

Belgian nationals must be used on "Belgian Government consulting engagements.

Firms performing audit and attest work may not engage in ta practice, management consulting or accounting services.

Denmark: Foreign accountants cannot form partnerships with Danish accountants and hold majority shares in accounting firms without special authorization of Danish authorities.

There is a scope of practice limitation. A public accountant is not permitted to act as a liquidator or to arrange for a composition with creditors for a client.

France: There is a nationality requirement for establishment, which can be waived at the discretion of the French authorities. However, an applicant for such a permit must have lived in France for at least five years.

Germany: Accounting firms are not allowed to advertise their services.

Spain: In order for a foreign accountant from a non-EU country to obtain certification to participate in Spain, his country of origin must offer reciprocal treatment to EU firms.

United Kingdom: Recognition can be withheld for auditors with overseas auditing qualifications, unless reciprocal treatment is granted for U.K. accountants.

INVESTMENT BARRIERS

The EU has a growing role in defining the way in which U.S. investments in the Member States are treated. Although Member State governments traditionally were responsible for policies governing non-EU investment, in 1993 the Maastricht Treaty shifted competence over third country investment from the Member States to the Union. Member State barriers existing on December 31, 1993 remain in effect, but these may now be superseded by EU law. Direct branches of non-EU financial service institutions remain subject to individual member country authorization and regulation.

In general, the EU supports the notion of national treatment for foreign investors, and the Commission has traditionally argued that any company established under the laws of one Member State must, as a "Community company," receive national treatment in all Member States, regardless of its ultimate ownership. However, some restrictions on U.S. investment do exist under EU law and others have been proposed:

Ownership Restrictions

The benefits of EU law in the aviation and maritime areas are reserved to firms majority-owned and controlled by EU nationals.

Reciprocity Provisions

EU banking, insurance and investment services directives include "reciprocal" national treatment clauses, under which financial services firms from a third country may be denied the right to establish a new business in the EU if the EU determines that the investor's home country denies national treatment to EU service providers. In the recently adopted hydrocarbons directive, this notion may have been taken further to require "mirror-image" reciprocal treatment, under which an investor may be denied a license if its home country does not permit EU investors to engage in activities under circumstances "comparable" to those in the Union. It should be noted, however, that thus far no U.S.-owned firms have been affected by these reciprocity provisions.

International Negotiations

The French Government has withdrawn from the OECD’s Multilateral Agreement on Investment (MAI) negotiations. The other EU member states were unwilling to continue participating in the negotiations after France withdrew, thereby ending the talks in that forum. France and Belgium are also seeking to limit OECD work on investment to elaboration of behavioral guidelines for multinational firms. These actions will no doubt hamper efforts to reach a broad-based agreement on principles for regulation of foreign investment, despite general EU support for such an agreement. The European Commission’s legal competence over investment issues is evolving, but remains limited. In many instances, Member State practices are of more direct relevance to U.S. firms. EU Member States negotiate their own bilateral investment protection and taxation treaties, and generally retain responsibility for their investment regimes.

Member State Practices

Austria: Austria’s 1993 Banking Act (as amended) presents a number of market entry obstacles to U.S. banks. While European Economic Area member states’ banks may operate branches on the basis of their

home country license, banks from outside the EEA must obtain an Austrian license to operate in Austria. However, if such a non-EEA bank has already obtained a license in another EEA country for the operation of a subsidiary, it does not need a license to establish branch offices in Austria. In addition, as of December 31, 1998, limits for single large loan exposures and open foreign exchange positions will decrease considerably for branches and subsidiaries of banks from non-EU countries. As of that date, the capital of their parent company may no longer be included in the capital base used to calculate loan and foreign exchange position limits.

France: There are no general screening or prior approval requirements for non-EU foreign investment. Notification requirements apply to foreign investments, EU and non-EU, that affect national defense, public safety, or public health. The government is able to exert influence over privatized firms through "golden share" provisions, establishment or incorporation. France continues to apply reciprocity requirements to non-EU investments in a number of sectors. For the purpose of applying these requirements, the French Government generally determines a firm's residency based on the residency of its ultimate owners rather than on the basis of the firm's place of establishment or incorporation.

Greece: Both local content and export performance are elements which are seriously taken into consideration by Greek authorities in evaluating applications for tax and investment incentives. However, they are not mandatory prerequisites for approving investments. Greece, which currently restricts foreign and domestic private investment in public utilities (with the exception of cellular telephony and energy from renewable sources, e.g. wind and solar), has deregulation plans for telecommunications and energy. As regards telecommunications, Greece has been granted a derogation until January 1, 2001 to open its voice telephony and respective networks to other EU competitors. In the energy field, the Greek energy market will be gradually deregulated, starting in February 2001. U.S. and other non-EU investors receive less advantageous treatment that domestic or other EU investors in the banking, mining, maritime and air transport sectors, and in broadcasting. There are also restrictions for non-EU investors on land purchases in border regions and certain islands (on national security grounds).

Portugal: Most foreign investments in Portugal are only subject to post facto registration. However, Portugal retains the discretion to limit foreign investment in state-owned companies being privatized on a case-by-case basis. To date, this prerogative has not been exercised.

ELECTRONIC COMMERCE

The trade in transactions via the Internet is likely to reach $ 300 billion by the year 2000. The American proposal presented at the WTO Council in February 1998 is that deliveries over the Internet should not be subject to custom duties. But in June 1998, the European Commission adopted a position on the taxation of electronic commerce ("E-commerce"), which is under discussion in the European Parliament and the Council. This document (COM(97)157 outlines the main principles of indirect taxation to be applied to such services. In Europe, a domestic Value-Added-Tax (VAT), distinct from an import duty, is payable on deliveries of goods and the provision of services. The Commission intends to adapt the existing VAT tax to electronic commerce, and to consider electronic commerce as the provision of a service. In this way, when electronic commerce involves products being supplied via electronic transmission, including the sale of "virtual goods", it must be considered for VAT purposes as the provision of a service. The Commission aims to adapt its current VAT legislation so that services are taxed systematically within the Union when they are

supplied for the purpose of being consumed there. However, where services are provided from within the Community in order to be consumed outside, they should not be taxed and input VAT should be deductible.

The United States has been concerned about changes to the EU 6th VAT Directive which allow Member States to levy a value-added tax (VAT) on offshore suppliers of telecommunications and online services (i.e., companies not established or with their principal place of business in the EU). For EU Member States to levy the VAT in this manner, suppliers of these services would become liable for the VAT on the basis of where their services are consumed and would be taxed as if they were established in the EU (versus the standard practice, applicable to European service suppliers, of levying VAT on the basis of where the service was supplied or corporation established). In its schedule of commitments in the General Agreement on Trade in Services (GATS), the EU has undertaken obligations to provide national treatment to value-added telecommunications services.

The European Consumers Organization (BEUC) expressed its objections to the Commission position on e-commerce taxation in its present form, demanding that consumer transactions be removed from the scope of the proposed text in favor of a more broad-based and collaborative approach, and it disagrees with the application of the law of origin as a universal principle for electronic transactions within the EU. It criticized the Commission's understanding of the nature of the present and future transactions over the Internet and its subsequent implications for consumers wishing to buy products via the Internet. The United States will continue to monitor this issue.

The EU Data Protection Directive (see above) has special implications for electronic commerce. An overly-restrictive interpretation of the ways in which data can be processed and transferred under the directive could stifle many forms of e-commerce, even if a significant cut-off of transatlantic data flows does not materialize.

The EU Commission has drafted a Directive on Digital Signatures which is under review by the Council and the Parliament. It is not clear as of the publication of this report what form the final version of this legislation will take, but there are concerns that it could lead to the creation of a cumbersome approval procedure for electronic authentication systems within the EU market, and possible limitations on the technologies which could be employed to authenticate electronic transactions.

OTHER BARRIERS

Data Privacy

The EU Data Protection Directive went into effect in October 1998. As of the date of this publication, only four EU Member States have transposed the directive into national law, although a number of others are poised to do so. The directive seeks to protect individual privacy with regard to the storage, processing and transmission of personal data, while still permitting the free flow of data within the EU. The directive allows the transmission of data to third countries if they are deemed by the EU to provide an adequate level of protection, or if the recipient can provide other forms of guarantee (e.g., a contract) that ensure adequate protection. U.S. firms are concerned by the lack of transparency in the definition of adequate protection and the potentially cumbersome arrangements for executing a data transfer. The U.S. Government is engaged in a dialog with the EU Commission on a possible solution involving an industry-led self-regulating system to protect personal data transferred between Europe and the United States.