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EUROPE–92 TRADE PROGRAM

HEARING

BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

MAY 10, 1989

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EUROPE-92 TRADE PROGRAM

WEDNESDAY, MAY 10, 1989

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The committee met, pursuant to notice, at 10:05 a.m. in room SD-215, Dirksen Senate Office Building, Hon. Lloyd Bentsen (chairman of the committee) presiding.

Also present: Senators Baucus, Riegle, Rockefeller, Daschle, Packwood, Danforth, Chafee, Heinz, and Symms.

[The press release announcing the hearing follows:]

[Press Release No. H-14, April 6, 1989]

BENTSEN ANNOUNCES HEARING ON THE "EUROPE-'92" PROGRAM

WASHINGTON, DC—Senator Lloyd Bentsen (D., Texas), Chairman, announced today that the Finance Committee will hold a hearing on the European Community's (EC) program to complete its internal market by 1992.

The hearing will be held on *Tuesday, May 10, 1989 at 10 a.m.* in Room SD-215 of the Dirksen Senate Office Building.

Under the Treaty of Rome which established the EC in 1957, EC member countries agreed to form a common market and eliminate the barriers which divide them. In 1985, European leaders recommitted themselves to achieving this goal by 1992. The EC set out a comprehensive program to unify the European market through 279 EC directives aimed at removing the remaining physical, technical and fiscal barriers between member countries. Until recently, the EC had not paid much attention to the external impact of these directives.

Senator Bentsen asked that testimony for this hearing address three questions:

- Will "Europe-'92" result in a "Fortress Europe" with high protectionist barriers?
- Will "Europe-'92" destroy the Uruguay Round negotiations, which are seeking to establish more effective rules for world trade?
- Is the United States monitoring the progress of "Europe-'92" closely enough and are we prepared to speak out forcefully against objectionable features?

OPENING STATEMENT HON. LLOYD BENTSEN, A U.S. SENATOR FROM TEXAS, CHAIRMAN, SENATE FINANCE COMMITTEE

The CHAIRMAN. This hearing will come to order.

This morning we take on a big subject. We are talking about what collectively will be our major trading partner, Europe-1992. It could provide a new engine for energizing trade, or it could balkanize trade.

It could bring about a more efficient, more progressive, more competitive, and richer Europe. Or it could leave Europe worse off as it falls prey to those who would like to push protectionism in Europe. The EC could aim at Japan and we could be hit by the ricochet.

I have some feeling for the kinds of pressures that hit policy makers when they try to make major changes in legislation to make the economy of their countries stronger. Like the EC today, we undertook a major initiative on trade in the Trade Act of 1988. As in the EC, there were those who saw that effort as an opportunity to limit competition, to close America to imports. We got an awful lot of advice and counsel out of Europeans, Japanese, South Koreans, and others. We resisted protectionism, and we want EC to do the same.

When we talk about the Gucci Gulch that we had out here, sometimes we heard more French there than we heard in Quebec. We want to return that favor in Brussels. We want to give them the benefit of our advice and counsel.

There is a lot to be concerned about in Europe-1992. Some of my colleagues here in the committee joined me on a trip to Europe a month ago. We were listening in one country to them saying we are going to have 60 percent domestic content, and then in the next country they were saying, "No, it has to be 80 percent or we will not accept products from the other country."

Most of our major companies in this country do not seem to be particularly concerned about Europe-1992. I can understand that because they say, "We are going to put a plant inside Europe. We are going to build it in Spain or in France or in one of the other countries. If they put a wall up around Europe, it is of no real concern to us."

We have other concerns, too, for example on distortions in agricultural trade. I also get the feeling that Europe is concentrating more on Europe-1992 than it is on the Uruguay Round. Some, perhaps, want to put things into being that can be grandfathered into the Uruguay Round.

These are the kinds of concerns that we share. We hope that most of these will never come to pass. But it is important, I think, that we advise Europe of our concerns early on. It is much easier to fend problems off before they are in solid print and approved by the parliaments of the 12 countries than it is to try to reverse the decision later.

One of the things we did on the trip was discuss mirror legislation, for example regarding financial services. We were told afterward that our input was effective in avoiding protectionism in Europe on financial services and that some of our arguments were used in turn by those Europeans who argued for a revised directive on finanical services. So hopefully, we contributed to the process. That is not because we had a formal seat at the table, but because we communicated our concerns.

Our first witness this morning will be Ambassador Hills. As the U.S. Trade Representative, she will have a major responsibility in developing U.S. policy in response to Europe-1992 and coordinating its implementation.

Because of the key role of the Commerce Department, we had originally also scheduled the Secretary of Commerce, but he has a problem in that the FSX is apparently up for a very early vote in the Senate. He was trying to put some fires out on that and chose to testify before another committee on that issue this morning.

But we are very pleased to have Ambassador Hills. I would like to defer now to my distinguished colleague, the Senator from Oregon.

OPENING STATEMENT OF HON. BOB PACKWOOD, A U.S. SENATOR FROM OREGON

Senator PACKWOOD. Madame Ambassador, I am usually an optimist, but I am still not optimistic about Europe and Europe-1992. I listened to Senator Danforth when he and Senator Chafee came back from a trip that they made during the recess, and they got the same impression that I did, in terms of agriculture, that no matter what they say to you, they mean not in their lifetime. As lawyers would say, lives and being plus 20 years, or whatever that old rule was. They are not talking about any kind of agreement on agriculture, and as far as I am concerned, if in the Uruguay Round we do not reach an adequate agreement on agriculture then I will not vote for the agreement no matter else we reach on intellectual property or things we are interested in.

Second, I have the same fear growing that I had when the trip that Senator Bentsen led went several months ago, that Europe is talking about protection, and collectively, I think, it is going to be greater protection than we now find country by country. It may not be quite as individually frustrating to us if we have one domestic content law in Italy and another one in France and none in Belgium and if we have different standards for generators in Germany than we have in Luxembourg, but I think that what we are going to be faced with is a European community government procurement standard worse in toto than any of the individual ones we face now. And I think we are going to face a worse domestic content rule in toto than we face now in all but one or two of the countries.

My greatest misgiving, very frankly, is about some American businesses, and I continue to see their statements, who I think will be satisfied if they can get inside the market and be treated as EC companies, and then they are not going to worry about the companies in the United States who do not happen to have manufacturing or other operations in market. And they will join in the closing of that market to companies in the United States who cannot yet, because they have not gotten big enough, justify centering operations inside.

So I admire you. I hope you pull it off, but I am skeptical that when this is done we will achieve what we want and I honestly think we ought to be looking toward more bilateral arrangements of the nature of Canada where we can put together a deal that is good for us and good for the country that negotiates with us and hope that others come along. That is a preferable deal to what I fear could be a bad deal in Europe and a bad deal in the Uruguay Round.

Thank you, Mr. Chairman

The CHAIRMAN. I would hope in the interest of our hearing Ms. Hills that we would hold our opening statements to the brevity that was demonstrated by the Senator from Oregon.

Let me state that the arrival sequence is Senator Riegle, Packwood, Heinz, Danforth, Baucus.

Senator Riegle.

Senator RIEGLE. Thank you, Mr. Chairman. I will wait until the question period.

There are really only two areas that I would like to get into with you today. One has to do with the automobile activity, and particularly, how the EC intends to square off against Japan and also financial services, but I will wait for those until the question period.

The CHAIRMAN. Senator Heinz.

Senator HEINZ. I am going to reserve my time for the question period.

The CHAIRMAN. Thank you.

Senator HEINZ. At that time I will be very interested in finding out what concerns we have specifically about directives or draft directives, or, more importantly, when we find something, such as a performance requirement, for example, requiring that diffusion be done within the EC in order for a semiconductor to be considered an EC product, which we consider a problem, and whether we have a process for doing anything about them.

The CHAIRMAN. Thank you.

Senator Danforth.

Senator DANFORTH. No questions.

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. No questions.

The CHAIRMAN. Ambassador Hills, we are delighted to have you and look forward to your testimony.

STATEMENT OF HON. CARLA A. HILLS, U.S. TRADE REPRESENTATIVE

Ambassador HILLS. Thank you, Mr. Chairman, and members of the committee.

I am pleased to be here this morning. I filed yesterday or the day before a full written testimony, and I would just like summarize a few points.

The single market in the EC, when the individual country markets of the community are combined, will be the largest industrialized market in the world. I agree with you that it is critically important for us that this $4 trillion market remain open, that the EC adopt policies which promote and not frustrate competitive forces.

We believe that the internal market program is motivated by European industrialists' perception that they need a single, barrier-free home market in order to compete with the Japanese and with the Americans in the world market. We also believe that individuals who think in terms of international competitiveness do not have as their objective a fortress Europe that precludes competition.

That being the case, American companies in nearly all goods and services stand to benefit from EC-92. You might say that our support, however, for EC-92 is based on certain conditions, five in fact: one, that America and third-country firms must be permitted to enjoy the same business opportunities as EC companies do in the

single market; two, that EC-92 should reduce the level of protectionism in Europe and not substitute community-wide restrictions for existing national restrictions; three, that 1992 must contribute to multilateral liberalization by conforming to GATT principles, as well as to new agreements reached in the Uruguay Round; four, where multiple levels of guarantees govern the treatment of non-EC business in individual member states, and where the Commission is seeking to harmonize those divergent guarantees, harmonization should be at the most liberal, as opposed to the most restrictive, level; and finally, that the Community's internal market completion program needs to be carried out in a transparent fashion which permits accommodation to foreign interests.

With respect to the Uruguay Round, we have in fact found that EC-92's initiatives have frequently helped to advance the cause of negotiations in Geneva. The Round negotiations have positively influenced the EC in certain areas of 1992 activity. For example, regarding protection of intellectual property, the Community's position at the start of the Round was that it was willing to negotiate measures against trade in counterfeit goods, but nothing more. Now, the Community in large part we believe because of the 1992 intellectual property rights agenda is willing to negotiate in Geneva on a much, much broader range of intellectual property right protections.

And in the service negotiations, we believe that the emphasis in the Uruguay Round negotiations on national treatment has been quite helpful in restraining the Community from its earlier protective reciprocity approach in its banking directive.

In the administration we are coordinating our efforts through a 16-month-old task force on the EC internal marketing. There are 20 different agencies represented in these coordinating sessions. We are working quite closely with a number of private-sector groups to identify the challenges to the U.S. firms. The Department of Commerce has been extremely active in private-sector outreach programs.

And having said all that, let me make it clear that we do not share all of EC-92's objectives. We differ, for example, in our views of their broadcasting restrictions, the degree of foreign participation which should be encouraged in standard development, and whether national treatment in financial services should be condition.

But where we have identified our concerns, I have to say that the Commission and its member states have generally been willing after discussion to accommodate our interests. Thus, I am cautiously optimistic and quite anxious to continue the dialogue that we have established with our counterparts in Europe.

I am pleased to take your questions.

[The prepared statement of Ambassador Hills appears in the appendix.]

The CHAIRMAN. Thank you.

To be able to defend our interests effectively in Europe as they formulate Europe 1992, it is important we have the ability to track what is going on there. As I understand it your first source of information is the U.S. Mission to the EC in Brussels. I also understand they have six economic officers, one of whom is from USTR, the

rest from the State Department, that they have none from the Commerce Department, and that the Agriculture Department on the other hand has five people there.

It appears to me from what I saw that Agriculture was well represented, but I question the lack of commercial and technical expertise. When you get to setting standards, it is not something that is casually known. It is an arcane subject almost, and it is important to have people that understand it and will get our point of view across.

Now, you are the interagency coordinator of the effort that we have there.

Don't you think we need more commercial and technical expertise in Brussels?

Ambassador HILLS. Well, I must say that I was strongly affected by your reaction when you came back from your trip, Mr. Chairman, and I have talked to the current ambassador to the EC and to the ambassador-designate to the EC. I am told by them that we do have a corps of people who are adequate to the task, although the new ambassador has said, "Please, let me get confirmed and get over there. I promise to work closely with you, and I am sensitive to the concerns that you are expressing."

I have great confidence in the USTR representative who is there, and it is a fact that as directives are that they are published in a book like our Federal Register and that we get them on a daily basis, so I feel we are getting the information. But I do want to look and to work with our ambassador to be assured that we have a full complement of people that are there to do what needs to be done.

The CHAIRMAN. I get a feeling that you have some turf rivalry there. The State Department has historically not been very amenable—seems to me, from what I have seen—to the Commerce Department's assignment of their staff. I think Commerce is necessary to add the commercial and technical expertise. To the extent that you as interagency coordinator can help resolve what we need in the way of staff in Brussels, I think it would be helpful to us.

Now, you have to get that information out to exporting companies across this country to tell them what they face. When you get to the big companies, I think they are already taken care of. I understand that Gucci Gulch just moved to Brussels, that they have some 2,000 consultants over there that are now doing well. I saw the restaurants there. You could hardly get into them with the expense accounts that some of these people have. I must say they are doing very well.

But what are you doing as far as getting that information back? Are you relying on the trade associations? Is there more that can be done?

Ambassador HILLS. USTR is a tiny agency, and we do not engage in education or outreach, other than through our private-sector policy advisory committees, comprised of roughly 1,000 members who give us advice, and very ably I might say. But the Commerce Department does to a great deal in outreach efforts, and they publish all of these directives which are available to any business that has any interest.

In addition to our private-sector advisors, we also have an intergovernmental policy advisory group that is quite able, chaired by the Lieutenant Governor of Illinois, and Illinois, as you know, has seven offices abroad. I think that that group is quite sensitive to bringing to the tier of government closer to the smaller companies information and that they have made a number of helpful suggestions. But in point of fact, it is Commerce that primarily does this activity and I think it does it quite well.

The CHAIRMAN. That is good.

I am not talking about building an enormous agency over there for the USTR. But I think effective coordination is terribly important.

I must say I am basically optimistic about what is going to happen on Europe 1992. I know on financial services where we saw a change in attitude that it is still just a recommendation to the 12 nations that are involved and that implementation is up to them finally. I also see that some of them are recommending that any import quotas and domestic content requirements be phased out over a period of time. I am hopeful that this is the case.

But if that does not happen, if you really have a fortress here, are you prepared to take some kind of action? Would you go so far do you think as mirror legislation to try to see that our interests are protected?

Ambassador HILLS. I do not think we are going to see a fortress Europe, Mr. Chairman, and I think that the most important thing we can do now is to impress upon our counterparts in Europe the tremendous advantage and growth potential that exists in keeping both of our large markets open. They will be the largest. We will be the second largest. Mutually open markets are a tremendous benefit to their entrepreneurs, as well as to ours. This trade openness has been the motor of growth over the last 40 years, and I think that that line of analysis has enable us to be effective in counteracting the protectionist impulses that they face—and we face here—in some of the directives that have issued, including the one you mentioned in the banking sector.

The CHAIRMAN. I would say, Madame Ambassador, that I do not think we are going to see a fortress Europe either. I am optimistic about it, but I must agree with the Senator from Oregon about the reaction we got on agriculture. I think that is a serious problem. We have not made the kind of headway I would hope for and we have to continue to push very hard on that.

And looking at the list here, Senator Packwood, you have some questions.

Senator PACKWOOD. Madame Ambassador, when you met with us initially in terms of agriculture, our position was that we wanted to see if we could get a firm, fixed date for the elimination of market-distorting subsidies; is that correct?

Ambassador HILLS. Yes.

Senator PACKWOOD. And that was a hangup for Europe, and so at one stage you briefed us and you said that you had said to them, "All right, folks, we will change the order of negotiating, not that we have gotten rid of the goal, but we will change the order of negotiating." We picked up that European kind of thought that

meant we were foregoing that goal. Subsequently you have used the term "progressive and substantial reductions?"

Ambassador HILLS. "That corrects and prevents trade distortions in agriculture."

Senator PACKWOOD. All right.

Well, I want to know what is our bottom line bargaining position on agriculture with the Europeans, or others, and whether you are hearing back what we are hearing back, that they think "progressive and substantial" means eons of time?

Ambassador HILLS. Senator, you refer to our earlier discussions with respect to our negotiating position then, which was to "eliminate," but there was no agreement as to a specific date, nor did I ever talk to you about a specific date. When they tell you, as you have reported, that not in their lifetimes do they want to address an elimination or ridding the world of trade distortions in agriculture, that is what we are negotiating. We have a framework agreement, and we have a long-term goal that is not phrased in terms of "eliminating," but now is phrased in terms of "substantial progressive reductions that will correct and prevent trade distortions in agriculture." And if you want to debate whether "elimination of trade distortions," or "substantial progressive reductions that correct and prevent trade distortions," is better than the other, I will say they are the rough equivalent. Our task over the next 18 months is to negotiate the time frame and hence the slope of the curve, and I am not a bit surprised that they would tell the ranking Republican on the Finance Committee not in their lifetime because that is their negotiating position.

They have adopted a common agricultural program, and I am sure they are telling their farmers politically not to worry, that there will not be a sharp slope of a reduction. And what we are trying to negotiate at the table is a sharp slope in the reduction. How sharp it will be, I cannot tell you until December of 1990, but we feel committed to the notion that the world trading system is going to be much better off if we can rid the world of trade-distorting measures, and that has consistently been our position.

Senator PACKWOOD. Well, is our policy to be in these measured reductions that there is to be some period of time in which to measure, or is that kind of a debatable point year by year as we go on?

Ambassador HILLS. We have only defined the short term as 1989 and 1990 and the long term, thereafter. The first tranche in the reduction will be 1991, but, as I say, all content in all 15 framework agreements, all we have is an agenda. We are going to negotiate short term and long term commitments. We have to put on the table by October of this year our short term commitments. It is a political objective because, you know, what we really have is one year. Our long-term commitments will start in 1991.

Senator PACKWOOD. Are you indicating that, long term, a satisfactory solution to you will be a progressive and substantial reduction leading toward the elimination of market-distorting subsidies that has no stated terminal point as we start down that slope?

Ambassador HILLS. No, I think you are going to have to identify a year in the process. Otherwise, you will not know the decline of the downward slope.

Senator PACKWOOD. All right.

Ambassador HILLS. I think you are going to have to have some target, and you know, it does not help the negotiations for me to sit here and say what our specific strategy is. I can tell you what my long-term goal is, but quite honestly, of course, I would like the year designated out in a relatively short number of years. The Europeans are going to want to wait until their grandchildren have died. This is all part of a negotiation.

Senator PACKWOOD. I understand so long as our policy is that we want a terminal date, not an ephemeral date that has no fixed point of reference.

Ambassador HILLS. I would say that what you want and what I want is an elimination of these trade distortions over time and we do not want unilaterally to bring down our restrictions until other nations bring down theirs.

Senator PACKWOOD. Thank you, Mr. Chairman.

The CHAIRMAN. Hang tough, Madame, and I think you will. [Laughter.]

Senator Riegle.

Senator RIEGLE. Thank you, Mr. Chairman.

It sounds like you are getting a good warm-up. [Laughter.]

Let me ask you with respect to automotive trade between the United States and Europe. As you know, we presently run a large deficit in that activity. Now, there are other factors that relate to that, including American companies that are established in Europe and have been for many years, particularly Ford and GM. But if you just take the posted trade back and forth in cars for 1988, we will export to Europe, or did export to Europe, about 47,000. They sent our way about 514,000. So we are roughly ten to one.

It is a $6 to $8 billion item in our trade deficit, so it is a significant item. We tend to lose track of it because of the deficit with Japan, for example, is so much larger, but I am concerned about where the Europeans may be headed with respect to their overall approach to automobile imports and exports.

As I am sure you know, there are now in place some very tough restraints on foreign cars coming into individual countries, and if you take a look at the penetration that Japan has thus far achieved in Europe, it is far lower, for example, than it is here. Europe has been much tougher. And also, if you look country by country, France, of course, limits the Japanese to three percent of its market; Italy and Spain limit it to one percent; and Britain to, despite all of the free market talk that we hear from that direction, 11 percent.

So, you have that pattern built in, and I am wondering if you are far enough into the assessment of how the automobile and truck production side of this is likely to work and the rules will work to be able to begin to judge where this is going.

Will there be overall limitations put in place in effect that will likely require the Japanese to want to come and build plants somewhere in the European market system, and does that seem to be where it is going? And if so, I would like to understand that now, because I think that has some major implications for ourselves. I think if that happens all the signs are that we probably have all of the automobile manufacturing capacity we need now worldwide. So if you add a new increment on top, with say the Japanese coming

into the European market to set up plants to get around what might become these Europe 1992 barriers that are established, I think that has some major implications for us.

So can you give me a sense as to how you see that moving, what seems to be the direction they are taking in that area?

Ambassador HILLS. The Japanese have invested in the United Kingdom in the automotive area, but I think it is too early to say how the European community will harmonize the restrictions that you have alluded to, and of course, all of our discussions with them are to keep those kind of barriers at a minimum.

Senator RIEGLE. I will be very surprised if all of a sudden the Europeans invite the Japanese to start to ship in a large number of foreign produced cars. So it seems to me that they are almost going to require the Japanese to do what they have done here, I mean come on shore, start to build some plants and so forth.

But there is no clear sign yet as to what may be in the offing?

Ambassador HILLS. With respect to the Japanese coming in?

Senator RIEGLE. Well, with respect to how the Europeans will play this game in the direction of Japan and how Japan may respond to it.

Ambassador HILLS. The Europeans have expressed some concern about Japanese entry, but I do not think that we have a clear picture of how they are going to deal with that concern, and they keep assuring us that they will not put up barriers that will inhibit us.

Of course, our auto manufacturers are in ventures in Europe now. Our industry is an oligopoly, and our auto manufacturers are in Europe, but I do not know that we can tell you today what the strategic plan of the Japanese is or how the Europeans will react to their strategic plan.

Senator RIEGLE. Well, with respect to our own trade in automobiles back and forth with Europe, I would hope that with a ten to one adverse ratio that we would work very hard to try to make it possible for American-built cars to make their way into that market.

Now, I realize the Europeans may, as they already have, impose some very tough restraints towards the Japanese who are viewed by them, properly, I think, as trade predators, as I think they are with us as well. But in terms of trying to whittle us down, I think anything that falls in the $6 to $8 billion a year range, which is adverse to us, is a pretty big item, and obviously, it radiates out because it is a high value-added product.

So I would hope as we go down the track here that there will be emphasis placed on the question of trying to enable us, as currency shift and other changes are made, that we can have a better chance to export American-built cars into the European market. That would be very helpful to us, and it would be an area where I think we could start to whittle down the trade deficit. Chrysler, I know, is now doing some exporting abroad of cars built here in an increasing number.

So I just would ask you to focus that one, if you will, because I think it may be an area that has some potential for us on the up side and if it gets off to the side, I think it could be very hurtful to us.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Senator Heinz.

Senator HEINZ. Madame Ambassador, I note on page 9 of your testimony your discussion of rules of origin-local content issues, and you go on to indicate you have not identified, as yet, any troublesome EC rules of origin or local content issues.

Nonetheless, when substantial transformation decisions are made in the context of anticircumvention measures, they can amount to the same thing. And of course, this is what appears to be taking place with the rule on the diffusion of semiconductors. There is a specific instance which could have a very substantial effect on government procurement practices.

You have identified, and it is well known, that there will be some kind of European government procurement benefit for European-identified products; as I understand it, their three percent rule. Obviously, therefore, this particular kind of problem with semiconductor diffusion could come to roost right in that area.

Are you concerned about that specific issue, and if so, what can you or do you intend to do about it?

Ambassador HILLS. We have discussed this with the European Community, and we are negotiating this within the Round, so that we are hoping that prior to 1992 that we will at least have had a good negotiation with Europe in the context of the 96 nations that are in the Round dealing with this area of rules of origin government procurement.

Senator HEINZ. Well, what about the specific issue of how this anticircumvention substantial transformation rule on diffusion could force American companies to have to do a very substantial part of their semiconductor manufacturing in the EC?

As we all know, and as Japan has reminded us with their success, there are tremendous economies of scale in manufacturing semiconductors. If you have to split up your manufacturing operation between the United States and Europe to accommodate this particular rule, you will not be cost competitive.

So with respect to this specific problem, which can have direct effects on our competitiveness because of the nature of this critical industry—I know you think it is critical—what are we trying to do, or have we no particular position with the EC on the diffusion issue?

Ambassador HILLS. Well, of course we have a position there. This is an area that we are negotiating with the European Community, just as we had the area of reciprocity in——

Senator HEINZ. Well, what is our position? Is our position that it is wrong and they should abandon it?

Ambassador HILLS. It is that rules of origin end with semiconductors when manipulated in an exclusionary way through the diffusion. I mean that is at a point of manufacture.

First of all, rules of origin tend to be restrictive by their nature. We have them. They have them. We will be willing to bring down ours if they are willing to bring down theirs. As to how those are manipulated, and if they are manipulated for an exclusionary purpose, of course, we are against it. And that is the process of our negotiation.

Senator HEINZ. But are we against this one, and if so, have we made our opposition or displeasure or whatever it is we have, known?

Ambassador HILLS. We are discussing this very issue with them now, and we have asked that this be included within the Uruguay Round negotiations.

Senator HEINZ. Madame Ambassador, maybe I am not making myself clear.

Are you saying that we are not protesting this specific problem with the Commission or not? I just am not clear.

Ambassador HILLS. We have protested. We are protesting.

Senator HEINZ. Anything you could send me documenting that, I would appreciate.

[The information appears in the appendix.]

Senator HEINZ. Let me take a moment to commend you on something that you have reported on, on page 10, which is the very strong position you have taken with the EC ministers on the broadcasting issue where you have quite correctly pointed out that moving from a 60-40 Euro-programming requirement to a major proportion quota is an unacceptable action for them to take. You have been very strong on that. I commend you and I urge you to stay strong on that.

Thank you very much.

The CHAIRMAN. Thank you.

Senator Danforth.

Senator DANFORTH. Madame Ambassador, an accomplished preacher telling me how to preach sermons, once said, "Tell them what you are going to tell them, tell them again, and then tell them what you told them." So I am going to tell you what I have told people before and what Senator Bentsen told you, just for emphasis, really. I too am concerned about the staffing situation in Europe. I normally do not spend a lot of time fussing about how people are doing what, but I shared your view, as you stated in your opening statement, that where we have identified concerns, the Commission has generally been willing to address those concerns. That was the basic impression I got when I was in Europe.

I think that the basic view of most people—at least those I talked to in Europe who were involved in the 1992 program—is that they do not want a fortress Europe, that they do want an open trading system, and I think that Europe 1992 is probably going to operate to the advantage of the United States. However, it is all in the details, and we have to be very, very keyed in to how the details, are handled. I know that you have heard this so many times, it is coming out of your ears, but I really do want to say it again. I think we have to be staffed adequately to deal with those details.

Another thing that was told to me when I was in Europe was that it is critical that our people at the various European embassies who are keyed in to the commercial problems within the member states know everything that is going on in Brussels and that the negotiators we have in Brussels, our ambassador to the EC, know everything that is going on throughout the Community. I hope that we are in gear so that all of the concerns that emerge, all of the countless people who are watching this process from various vantage points, have their views funneled in to those who could

do something about it. You have heard this before and I simply want to state it again.

I might say that a couple of nights ago at an affair at which both you and Senator Bentsen were present, I was speaking with the president of a trade association here in Washington, and he told me that he has a vice president in charge of the Senate and that vice president has two professional staff people also monitoring the Senate, plus a support staff of people. It seems to me that if one trade association is so attuned to all of the developments and nuances of what is going on with just 100 people and some staff people here in the Senate, surely it is important for us to invest whatever is necessary to make sure that we know the nuances of Europe 1992 and that we are able to register our concerns on the theory that they will be taken care of.

I do have one question for you, believe it or not.

Before Senator Chafee and I went on our trip, an American businessman told me that in his view, Europe 1992 was just another way of saying "industrial policy." I raised that with various people in Europe and they said, "No, that is not so at all." On the other hand, the president of Philips Electronics made a speech to the European Parliament last March in which he called, quite expressly, for an industrial policy.

Let us suppose that is the direction of Europe. It certainly is the direction of Japan. There is debate going on in this country right now about whether it should be the direction of our country.

What should we be doing about it? How should we right now be alert to the possible emergence of industrial policy in Europe, and what, if anything, should we be doing about it?

Ambassador HILLS. When you are talking to the business executive I would think it useful to find out his definition of industrial policy. I look at what is going on in the European Community as a massive deregulation. They are erasing barriers among 12 nations, and it should make it easier, both for the entrepreneurs there to ship their goods from one corner to another and also for our businesses, large and small, to get their goods in.

To do that, they are adopting 279 directives which deal with mercantile policy, if you will. If that policy is industrial and the process is deregulating, it should be positive. We know from the directives, that have been enacted, and about 40 percent have, that we have had grievances with relatively few so far. And of those that have been drafted but not passed, which we have also reviewed, we have had relatively few—clearly they deal with commercial policy. Just moving goods around Europe deals with commercial policy, but I gather from your question that you have a more negative view of the words "industrial policy" than simply dealing with those matters with interest to industry.

Senator DANFORTH. I mean involvement of government in the nurturing and development of various business enterprises.

Ambassador HILLS. I do not see the purpose of the European Community "single market" to be primarily that, but I will be quick to say, at the same time, that Europe has been much more nurturing of business than has the United States.

We have followed a path since the War of being much more committed to free enterprise, and we believe that our path has created

more jobs and more vigor in our economy than what has happened in Europe. Indeed, we believe that the contrast between the jobs that we have created, our relatively lower unemployment figures, our generation of 20 million jobs during the 1980's, has caused Europe to focus on the need to get some of this regulation out of their lives and to erase those barriers among the 12 nations and to do some other things that could be productive.

Now, they may take some wrong turns. It would not surprise me. We do from time to time. But we are watching the process and we are trying to be on top of the issue, but I would not say that the drive, the motor, behind 1992 is to adopt an industrial policy in the terms that I think you are using that term.

Senator DANFORTH. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. Thank you, Mr. Chairman.

Madame Ambassador, I too want to repeat somewhat the same message that you have heard several times and most recently stated by Senator Danforth.

When I was in Brussels too with Senator Packwood, Senator Pryor, and our Chairman, I had the impression that in Brussels we are somewhat outgunned, and I will tell you why.

First of all, it just overwhelmed me, frankly, that there are 10,000, or I do not know how many thousands, of employees working for the Commission in Brussels. As you know, there is this gigantic, big black building with all these wings on it and all these people running around in Brussels. There are so many people there it is like an anthill. And second, they are so bureaucratic, much more bureaucratic than the member governments, or the ministers and officials we met from various European countries.

It was my impression that our mission over there is outgunned and frankly, did not quite know what is really going on. I think this was partly because we did not quite have the same number of personnel. I do not know what all the reasons are. I just did not sit down at the meeting we had and come away with a good feeling that our people are solidly representing us over there and know all of the ins and outs and know what is going on. I did not get that feeling and it bothers me, and I think in part it is because of some of the statements you have heard earlier this morning, namely, that maybe we need a little more firepower over there to find out what is happening because, as has been stated, it is going to be in the details. It is going to be in these directives as they come out. And I suspect that a lot of directives are going to come out near the end, a big flurry, and we'll say "Oh, my gosh, where were we? Why did we not know that this was going on, that this was going to be in a directive?" and whatnot.

I spoke to a British MP during our trip. He told me that Britain's largest overseas mission, but for military personnel, is in Brussels. Of course, Britain is a member of EC. But still, they know where the action is, and it seems to me maybe we ought to have a little more firepower where the action is, too, with respect to EC-92 so we can protect ourselves. And as you know, a lot of trade associations and a lot of American companies certainly have a lot of personnel dedicated to EC-92.

So I urge you to take several extra steps to boost our presence and our understanding from the USTR's point of view and the government's point of view as to what is happening. I do not get the sense that we really know exactly what is happening.

Now, coming back home, if you are going to be as effective as I know you can be, it seems to me that our government also has to speak more strongly in a more unified basis with respect to not only 1992, Europe 1992, but Japan, FSX, and whatnot. So I would like to know your ideas and how we can help you and how we can frankly help our own country be a little more effective in stating our economic objectives compared with foreign policy and national security objectives, not to belittle those, but to just give our country a little more economic say.

So I would like to know who chairs the economic policy councils, how often you have met, does each agency have basically one vote or not? Just share with me, if you could, your ideas as to the composition of the economic policy council, decisionmaking, and how we can get a little more economic say and the American government's positions.

Ambassador HILLS. Senator, I think that this administration has spoken uniformly on economic issues and perhaps it is because of the way the Economic Policy Council works. On most trade issues, which have been predominate on the agenda of the Economic Policy Council, the positions are developed by an interagency staff committee, which means that USTR chairs and coordinates bringing together representatives from State, Agriculture, if that department is pertinent to the issue, Commerce, Defense, if that department is pertinent to the issue, and a variety of other agencies. The Council of Economic Advisors is represented, as is the National Security Council. So that we have a holistic view of what are the various concerns. That interagency work product is then reviewed at a deputy or assistant secretary level by the Trade Policy Review Group (TPRG). The TPRG's work product, unless there is no dissent at all, and I think that there is no need to take the time, it goes to the Economic Policy Council where I would be making the presentation. Now, the Secretary of Treasury chairs the Economic Policy Council, but I make the presentation and deal with the trade issues.

Senator BAUCUS. On Super 301 issues will the Secretary of Treasury also then chair the Economic Policy Council?

Ambassador HILLS. Of course, but that process I have just described is ongoing in our office right now. We have representatives of every agency there working on a vast number of topics. A work product will come out. I meet with the USTR chair of that group every morning since it commenced, and we will review it at the deputy level and we will send a recommendation forward.

Senator BAUCUS. My time is up. I just want to ask one quick question.

Do you think that you should also be a member of the NSC?

Ambassador HILLS. Well, the NSC is already a member of the Economic Policy Council, and on issues where trade has been relevant, I have been invited to the NSC meetings. I do not think it is necessary for me to sit in on a strategic defense discussion, but there are obviously times where trade is relevant. I feel very com-

fortable that when such an issue arises that General Skowcroft will keep me apprised. We work very well together.

Senator BAUCUS. And you have sat in on NSC meetings?

Ambassador HILLS. I have sat in. Yes, indeed, I have.

Senator BAUCUS. Thank you.

The CHAIRMAN. Thank you.

Senator Daschle.

Senator DASCHLE. Thank you, Mr. Chairman.

Madame Ambassador, I would like to see if I could use the time I have this morning just to get a better appreciation of reciprocity. I am still grappling with our overall assessment of where the EC is with regard to reciprocity. You mention on page 6 reciprocity with regard to the Second Banking Coordination Directive.

How do you appraise the position on reciprocity generally with EC? How does it differ as you would describe their position on reciprocity from our own? And as you answer that part of the question, how does it relate to our current position, both with the Omnibus Trade Act of 1988 and Section 22?

Ambassador HILLS. Reciprocity connotes to us, and it does to the Europeans, too, that foreigners would have to give the same rights to European entrepreneurs on foreign soil as the Europeans would give to foreign entrepreneurs coming to Europe. In the banking sector, with the initial draft of the Banking Directive it suggested that Europe was contemplating erasing all barriers so that if you were a banker in the United Kingdom, you could offer financial services in Spain or Portugal. With a reciprocity standard, if that were not possible with a trading partner, such as the United States, a restriction would apply. Thus, if a UK banker came to New York and could not bank in Texas, perhaps a barrier would be erected because that situation would not be the mirror image of the freedom that Europe offered to its trading partners.

Senator DASCHLE. And does that position with regard to financial services represent their position overall with regard to reciprocity?

Ambassador HILLS. I am just giving you the definition and the only place we saw it suggested was in the services arena.

We had a number of discussions with our counterparts, all 12 trading ministers, expressing our concern because, of course, we follow the GATT principle of national treatment. We will treat foreigners as well as we treat our entrepreneurs here at home. Our concern was based on a very practical reason in the banking sector; we do not have interstate branching. We do have the Glass-Steigal Act and were Europe to impose a reciprocity or a mirror standard, we would not have been as well treated.

At the end of our discussions, that reciprocity standard has been softened and it is not as I have defined it any longer. So we felt that we were effective in bringing to the attention of the Europeans the adverse impact, at least in this market, that such a standard would have. But we have not seen reciprocity raised in the other negotiating groups.

National treatment is the standard of GATT as a general proposition. In fact, one of the three priceless principles of the GATT is national treatment, transparency, and most favored nations. Those are the three rules that we find most significant to protect.

Senator DASCHLE. But as a position in this country, has it not been to a certain extent clarified that in certain matters of trade, conditional reciprocity is part of the U.S. position today as a result of the 1988 Trade Act?

Ambassador HILLS. Well, there is certainly language in the 1988 omnibus bill that would suggest a mirror image approach and some have urged that. That would make it very difficult for us with many of our trading partners, particularly the lesser developed world, which has not developed or graduated to the extent of openness, even appreciation of the benefits from openness, which is what we have been trying to persuade in the course of our Uruguay Round.

Senator DASCHLE. So your position would be that as far as the 1988 Trade Act goes, conditional reciprocity is really not implied?

Ambassador HILLS. I would say that it is not a tenet of the Act, and of course, that Act is 1,100 pages. If you are looking at the sections that I am looking at very closely today, like Super 301, no, I do not think there is a mandate for reciprocity.

Senator DASCHLE. Let me ask you, and I see the yellow light is on, just again, from an educational point of view, how do you view Section 22 as it relates to our position on reciprocity?

In agriculture in particular, we have relied upon Section 22 on numerous occasions obviously, in dairy in particular.

Does that not run counter to our position with regard to reciprocity as you have now described it?

Ambassador HILLS. My understanding is Section 22 is grandfathered because it was adopted prior to the GATT and hence, we have a 22 waiver, if you will, outside of our usual trade principles.

Senator DASCHLE. Well, of course, it is grandfathered, but obviously we either subscribe to the philosophy behind Section 22 or we do not. We can say it is grandfathered, and I understand why that would be an appropriate position to take, but it says nothing about our own philosophical belief with regard to the utilization of that in the future. Whether or not we use it, regardless of whether it is grandfathered or not, depends in part upon our philosophy with regard to reciprocity it would seem to me.

Ambassador HILLS. If you put it that way, I would say that it is not our intention to bring down any of the barriers that we would admit to having unless our trading partners do likewise in the course of a mutual negotiation. But that is in a sense a reciprocity, but probably not as that term is traditionally used.

If your concern is, are we going to unilaterally pull down our trade restrictions watching our trading partners either maintaining or erecting them, then the answer is we are not.

The CHAIRMAN. Senator Rockefeller.

Senator ROCKEFELLER. Thank you, Mr. Chairman.

One question only, Ambassador Hills.

With EC-92 approaching, there is a lot more talk about regional trading blocks, North America, Asia, and Europe. I am not really sure that such blocks are inevitable or what I think about it at this point. But I do know one thing—that there is a lot of talk in Asia now about regional structures, for their own purposes or, perhaps, to deal with, not only us, but also EC-92.

One of those suggestions came from former Prime Minister Nakasone who suggested that there be an Asian OECD. Recently, the OECD met informally with Taiwan and Korea, and I am not sure if the idea was to bring them into the Western system, and thereby head off a so-called Asian trading block, Japan dominated, or not.

It would seem to me that it is a better direction for the newly industrialized countries to be linking up with the nation states of the industrialized world, the OECD, rather than forming an Asian trading block with Japan. I am not really sure how I feel on that subject, and I wonder if you have any thoughts about this issue of regional trading blocks as a result of EC-92.

Ambassador HILLS. Well, let us say that I think that the best trade policy is to have expanded and open markets worldwide, multilateral expansion, if you will, which does not mean that we would not want to consult regularly with Asian nations. They will be much better off if they keep trading with the United States which has provided them with a vibrant market.

I do think that we can do a lot more in consultations and discussions with the Asians and with other nations in the Asian theater, which is not to sponsor trading blocks, but to sponsor liberalization. We have 18 months left to the Uruguay Round and it is extraordinarily important that all nations, wherever they are located on the globe, to subscribe to worldwide liberalization, not just in a given area, but in all areas.

And so it is to their benefit, as well as to ours, and to the growth of the world's trading system, to keep their eye on the Uruguay Round. And I think that these consultations, which I do favor, can be a force behind that to push that through.

So the fact that we go over and talk with our European friends or go out into Asia and talk to our Asian friends, that is all consistent with our overall trade strategy, which is to open and expand worldwide markets.

Senator ROCKEFELLER. All right.

Thank you, Ambassador.

The CHAIRMAN. Thank you.

Gentlemen, we have a very distinguished panel waiting to testify, but if a member feels it important to ask another question I will defer. Senator Chafee, you have not had a chance.

Senator Chafee. No thank you, Mr. Chairman.

The CHAIRMAN. Are there any further questions?

[No response.]

The CHAIRMAN. If not, thank you very much for your attendance. You have been quite helpful.

Ambassador HILLS. Thank you very much.

The CHAIRMAN. Thank you.

Our next witnesses will be Mr. Richard Heckert, former Chairman of the Board, Chief Executive Officer of Du Pont, and representing the National Association of Manufacturers; Mr. Lionel Olmer, who is representing the U.S. Chamber of Commerce, who is a partner of Paul, Weiss, Rifkind, Wharton & Garrison, and Vice Chairman of the Subcommittee on EC-1992; and Mr. Matthew Coffey, who is President of the National Tooling and Machining Association, Fort Washington, Maryland.

Mr. Heckert, if you would proceed, please.

STATEMENT OF RICHARD HECKERT, CHAIRMAN, BOARD OF DIRECTORS, NATIONAL ASSOCIATION OF MANUFACTURERS, WILMINGTON, DE

Mr. HECKERT. Thank you, Mr. Chairman.

I am going to skip over my oral testimony rather quickly. I think most of the points that are relevant to this issue have been touched on. I simply want to emphasize those that I agree with strongly.

I will acknowledge that I am no longer chairman of Du Pont. I am, however, Chairman of the National Association of Manufacturers. Undoubtedly, some of my thoughts are biased by 40 years in another capacity.

I am pleased to testify on behalf of NAM regarding the European Community's internal market program, so-called EC-92. Our organization has recently published a major study, "EC-92 and U.S. Industry." The study covers the major issues for U.S. industry in detail, and I will submit this document for the record of the hearing along with my full written testimony.

[The executive summary of the report and the prepared statement of Mr. Heckert appear in the appendix].

Mr. HECKERT. For perspective it may be helpful to know that NAM's membership covers over 80 percent of this country's manufacturing production and manufactured exports. Members range in size from the largest U.S. industrial firms to over 9,000 smaller manufacturing companies with fewer than 500 employees each. Thus, NAM's views reflect a broadcross-section of U.S. manufacturing interests.

And from there I will depart from the script and talk about four aspects of this that I think we really have to keep in front of us at all times as we deal with the question.

First of all, there is no question that the formation of another large and relatively accessible, quite affluent trading block is extremely beneficial to the U.S. business interests. I have no question that however well or poorly that exercise is carried out, at the end of the day we will be better off than we are today.

We have suffered for a long time in this world for being the most attractive market for exporters in other parts of the world. That is an enviable position in one sense, but it also exposes you to a lot of attention, a lot of intense competition. Now we are going to share that with Europe and that is very good. And I would submit that this will benefit not just those who have the ability and the desire to invest within the Common Market, but those who make and sell products in the U.S. and who export.

Now second, I really do not believe that protectionism is in the long-term interest of the European Community, and therefore, I do not think they will move very much in that direction. It is entirely possible, and even likely, that in the process of making this enormous change in the way they do business that they will make some errors, and we should catch all those that we can and point them out to them and help them correct them.

But Europe and European companies have for many, many decades attached much more importance to export markets than companies in the United States. They think internationally and they depend very, very importantly on markets outside the Common

Market. Given that state of mind and that history, I think it is inconceivable that they will deliberately fall into the trap of turning protectionist and having an adverse effect on international trade worldwide.

The third point that I would make is that if they do make mistakes, how quickly they correct them and how well they respond to our concerns will be importantly determined by our resolve. You know it is one thing to spend a lot of money and time and intellectual effort in deciding what is wrong with the program that emerges over there. It is quite another to respond to issues as they surface.

One of the reasons that we have had so much trouble with trade in the past is that as a country we have had great difficulty ever responding to a particular issue. Now, I certainly am not suggesting that we ought to be careless with the heavy artillery, but I do think that some of the problems we suffer as a country stem from the fact that we simply do not step up to problems and face them forthrightly with our overseas trading partners.

So the way that the administration and Congress posture themselves will have a very important impact on the outcome of this exercise. We have got to be willing to protect our interests and that goes far beyond Ambassador Hills' activities.

Finally I would observe that I think we fall in the trap of comparing what we hope will emerge out of EC-92 with perfection. I would remind you that access to Europe is far from perfect today. It is very difficult to do business across the many countries that make up the Common Market, and even if this change is less than perfect, it is very likely to be better than what we have now. So I hope they will do it very well, but I have every reason to believe that whether they do it well or not so well, we are better off with one big market over there with relatively few internal boundaries.

Those four points I hope you will keep in mind. They are very important. I want to comment on one other concern which the Chairman expressed and I understand. This is whether those who have the ability to invest overseas will take this whole exercise lightly and those who are left here depending on exports will be the ones who suffer.

My company's experience I think is fairly typical of large companies that invest internationally. We find that about half of our international business is based on products that are made and sold overseas and about half on exports. And as international investment grows, so do our exports. That ratio has remained remarkably constant throughout the last two or three decades.

So I think you have to recognize that when U.S. companies are aggressive and invest in overseas markets to serve overseas markets, they are also taking steps which will inevitably lead to more exports. It just follows as night does day, and I think many companies would cite that same experience.

Senator CHAFEE. Mr. Chairman, could he just repeat that last conclusion about the exports?

The CHAIRMAN. Yes.

Mr. HECKERT. Yes, let me give you numbers. You will be able to grasp it perhaps even easier.

For the last 10 years Du Pont's international business has been about a third of the total, 32, 33, 34 percent. Recently it has climbed to a little over 40 percent. The export component of that as a percent of the total was 15 percent, now approaching 20. So exports have grown as international investment has increased and it stays remarkably close to half of our total international business as that business grows.

Now, it may be a different ratio for other companies, and I am sure it is, but the point is that you do not just invest overseas. When you do that, invariably you create the opportunity to market U.S. products that are exported to those same areas. Very important, and there is a lot of data that you can access that will make that point very convincingly.

I think those are the important thoughts that I would like to get across, and I invite your questions and comments. I should acknowledge that I have Steve Cooney with me who is the NAM staff person who prepared the NAM report on EC-92. If you have questions dealing with that, he will be glad to respond.

Thank you.

The CHAIRMAN. Thank you.

Mr. Olmer.

STATEMENT OF LIONEL H. OLMER, VICE CHAIRMAN, SUBCOMMITTEE ON EC-92, U.S. CHAMBER OF COMMERCE, WASHINGTON, DC

Mr. OLMER. Thank you very much, Mr. Chairman, for the opportunity to be here and to present my views and the views of the U.S. Chamber of Commerce Policy Subcommittee on EC-1992, on which I serve as vice chairman.

I present views that represent my experience as a former trade official in the first Reagan administration, as an attorney involved in international business activities, and a perspective that attempts to reflect the wide spectrum of membership in the U.S. Chamber.

I have prepared a statement for the record and will only spend a few moments calling to your attention a few specific points.

First, I think it important to look at the motivation of the European Community in terms of why it has approached 1992. Most sharply, I believe, it needs to be acknowledged that it is not being done for our greater good. It is being done because Europe feels it is falling farther behind in the race for markets of the 21st century. It feels the hot breath of Asia and it is not so enamored of the competition from many sectors of the American economy.

Second, there are some signals that have emanated from Europe that warrant serious caution on our part, both the business community and the government of the United States, and I speak when I say "government" of the Congress as well as the administration.

And third, the economic assumptions on which the rosy forecasts for EC-92 are based would probably drive the Congressional Budget Office through the roof. They presume more of the same, no recessions, energy prices relatively stable, and so on.

There are incorporated from the signals from the EC a few specific areas that have been touched upon earlier in the examination

of the U.S. Trade Representative, and they include, and I hope we get into it in questions, local content, standards and certification, and the targeting of selected industries, most specifically high technology and commercial aircraft.

And I would like to close by asking a sort of rhetorical question: "what is to be done about it?" Foremost, it strikes me that this is an instance in which there is a great need for the closest kind of cooperation between government and the private sector. Often, we have been criticized as a nation for an adversarial relationship between the private sector and the government. Perhaps sometimes the criticism has been warranted. I think that we cannot afford that kind of adversarial relationship in respect to EC-92. In my view, it will subsume most of the trade issues with which we now deal, including market access in Japan, including high technology trade with the East Bloc, and so on.

Among the things, in addition to this partnership of which I speak, that are important is monitoring of what is going on. Both the private sector and the public sector need to do a better job, and they need to be better focused. The government now has, as Mrs. Hills mentioned, more than 20 participants in the interagency committee, but I have been advised that there are 54 representatives that show up, including someone from the World War II Battlefields Memorial Commission, and I do not believe that that is the way to get a sharp, focused, assertive policy developed.

I think that specific timetables need to be established by which we will say, "Either we achieve this to our satisfaction or we will have to resort to other means to achieve similar or the same objectives." I do not yet see that happening within the government.

So, Mr. Chairman, those are just a few brief observations that I have extracted from my written testimony, and with that, I will turn to your next witness.

The CHAIRMAN. Thank you.

[The prepared statement of Mr. Olmer appears in the appendix.]

Mr. Coffey.

STATEMENT OF MATTHEW COFFEY, PRESIDENT, NATIONAL TOOLING AND MACHINING ASSOCIATION, FORT WASHINGTON, MD

Mr. COFFEY. Thank you, Mr. Chairman.

At the risk of disagreeing with Senator Danforth, I would like to point out that our trade association has no vice presidents, let alone a vice president for the Senate. [Laughter.]

I am here today speaking for the tooling and machining industry, which is an industry which is a high precision industry, a high technology industry, an industry which cuts across all industries. You cannot make a car without it. You cannot make a microchip without it. It is the industry which makes the reverse third dimension of the final product.

So it is an industry that is critical to the defense-industrial base, and it has a special characteristic. It is an industry of small companies. There are 3,000 members in our association. The average employment is 20 employees. It is an industry which competes domestically and internationally, and it is an industry which is entrepre-

neurial, self reliant, innovative, probably more patents and more new products developed in this industry than any other in the country.

My intention today is to fill your plate with ideas and perhaps some controversy, because as I look at EC-92 I do see the opportunity, but I see substantial problems. Listening to the prior testimony, the popular song runs through my mind. The popular song is "Don't Worry, Be Happy." I suggest to you that we should worry a little and perhaps we will remain happy.

The problems that I see in the relationship between Europe and the United States at the present time are as follows:

First, I think U.S. policy is poorly positioned to respond. When you consider that we have five major departments and agencies who have a piece of this pie: the Department of Defense, USTR, OMB, State, and the Department of Commerce. And then we have that minor agency which seems to be disappearing from the face of the Earth called the Ex-Im Bank that I think we need to talk about.

I think Europe in the past two decades has developed a very sophisticated offset policy against U.S. manufacturers. It is an offset policy that U.S. policy has failed to address, but it is doing more to create deficit problems, in my opinion, than just about any other thing we have seen.

Europe has direct manufacturing subsidies to their small manufacturers, and I have an example to talk about that later. Small European manufacturers are encouraged to form consortia with government sponsorship, while small manufacturers in the U.S. live in the fear of treble-damage lawsuits under the antitrust laws.

Finally, Europe has a VAT on products. The United States has no taxes at all on imports.

And last, our President is not involved directly involved in negotiations for major purchases, while European leaders are.

So what do I think we should do about all this?

First, I think it is time that we decide that the Commerce Department really is the agency to represent our point of view around the world where business is concerned and give it the necessary ability to launch the kind of program that we need.

I think you need to rebuild Ex-Im. It is unbelievable to me that while our trade deficit has been going from $40 billion to $160 billion, Ex-Im's funding has gone from $5 billion to $411 million. Ex-Im is now in the position where it can probably fund one Boeing deal, period, and it is done for the year. It does not make a lot of sense to me.

I think you need to enact the Credit Reform Amendments of 1987 which Senator Heinz introduced and get Ex-Im's profitable loans off budget. It is the only way that we are going to build the kind of financing mechanism we need to make American manufacturers aggressive in that market.

I think we need to enact H.R. 423, the Flexible Manufacturing Act, which Congressman Wyden introduced to free small manufacturers of their fear of the antitrust problem.

I think we need to revisit the Business Transfer Tax because it does provide a mechanism to balance our problems in trade with social welfare costs.

I think we need to develop countertrade and offset policies against importers and foreign companies and governments where they are involved and we need to develop a federally-chartered export trading company to encourage small manufacturers to export.

I also believe we should consider a federally-chartered venture capital company to stimulate growth for small consortia of manufacturing companies.

And we should support through the Department of Commerce aggressive U.S. participation in the standards that are being created in Europe. And there is a proposal before Commerce at this time from the American National Standards Association which we think we should give our encouragement to.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

[The prepared statement and the addendum to the prepared statement of Mr. Coffey appear in the appendix.]

The CHAIRMAN. Well, we have seen some varisome views, and that is good.

Mr. Heckert, Du Pont does have a plant in Europe, is that correct?

Mr. HECKERT. Several, Mr. Chairman.

The CHAIRMAN. All right.

There is no question in my mind that companies are being pushed to open plants in Europe because of their concerns that Europe-1992 might be protectionist.

I remain optimistic about Europe-1992, but I cannot help but remember that the EC is the same group of countries that put together the European Common Agricultural policy. It is extremely protective and very disruptive to free trade. The idea that they might become more export oriented, I am not sure. I hope that is right.

One of our problems is that we have had such a great domestic market, we have not needed exports—we thought—to the degree that smaller countries did. As I look at the countries of Europe, the largest of those 12 had 60 million people. Now they will have 320 million, and they will have a domestic market that will be even grander than ours. I hope you are right, that they remain very much export oriented and, in turn, allow access to their markets.

But one of the big debates I had while I was over there was about Nissan, up in the lake country, developing and manufacturing automobiles. Some Europeans were talking about requiring 60 percent domestic content, local content, and the French said they would not accept the cars unless they had at least 80 percent local content. The Japanese came back and said, "All right. We will go to 80." They are talking about a very big plant. That is protectionism as far as I am concerned. Those are some of the things that disturb me.

Now, Mr. Coffey, you represent small companies, and those are companies that I understand, even though small, are quite capable of putting out quality products, very competitive from a quality standpoint.

Do you feel there are some basic differences between your interests and those of large American companies involved in Europe?

Are they being addressed by our representatives in these negotiations?

Mr. COFFEY. I do feel that there is a dichotomy, and I think you expressed it well when you said the large companies are already established in Europe so they have got theirs in terms of their inclusion in the market. Small company exporters look at the European environment as a hostile one, and I think I have made that clear in my statement.

I have with me a very simple little part here, and it is probably very unspectacular to most people, but this a part which, Mr. Chairman, by some happenstance just happens to be made in Texas. [Laughter.]

The CHAIRMAN. Well, I am delighted to see such quality.

Mr. COFFEY. It is a part made to 25 millionths of an inch tolerance. Twenty-five millionths of an inch is virtually inconceivable in terms of your ability to see it or to recognize it. But this is a piston made by Ruska Company in Houston, a small company, and this piston is used in measuring gases in a gas pressure gauge. It is sold around the world and the only place that Ruska has a problem is in France where the French government is subsidizing research to compete with them on this valve.

There are a lot of very small companies in this country that have know-how, that have great skills and feel that they are lacking in protection when they go off shore. They are lacking in the ability to compete on financing. They are lacking in the resource of a trading company to do marketing, shipping, all those things, and to take some political risk for the countries that they have to deal in.

So I think that, yes, there is a big dichotomy between a large company's perspective on this and a small company's perspective, and yet, I think that a lot of America's know-how, a lot of America's ingenuity is residing in those small companies.

The CHAIRMAN. Thank you.

Mr. Olmer, if there was one thing that we should concentrate on as they formulate Europe-1992, what would it be?

Mr. OLMER. That is an extremely difficult question, Mr. Chairman.

I would harken back to language that former President Reagan used in the context of strategic arms, trust but verify. Be suspicious or skeptical. I see so many areas in which manifestations of protectionism, or what we would call protectionism, will arise.

I might have selected the automobile sector, which is the single most important sector for Europe because of its ripple effect throughout other industries, and perhaps if you concentrated on that, you would see the way in which protectionist tendencies reach out into these supplier industries, and perhaps our policy could be formulated on that.

But we have a lot of work to do on our own side as well, and I hesitate to single out automobiles. We need to do a better job in formulating our own policy and expressing it withtime-certain deadlines.

So I am sure I have not responded adequately, but I do not think anyone could, in a capsule, select one issue.

The CHAIRMAN. Thank you.

Senator Packwood.

Senator PACKWOOD. Mr. Heckert, the Chairman mentioned the Nissan plant in England and France were demanding 80 percent domestic content. The plant was approaching 70 percent. I do not know how they are going to resolve that, but I asked a number of the European officials when we were there whether they would let any of the Hondas from Marysville, Ohio, in which are about 65 percent domestic content now, and they are exporting. They do not make this particular car in Japan, so they are exporting around the world out of there. The answer was "no." They want the Honda plant to be in Europe.

What do we do about that?

Mr. HECKERT. Well, again, this is a question of being willing to identify problems and insist that there be some mutually acceptable resolution.

Senator PACKWOOD. And what should be do if we cannot get them to agree to a mutually acceptable solution?

Mr. HECKERT. Well, then you have to begin to talk about quid pro quo.

Senator PACKWOOD. All right.

Mr. HECKERT. There is a lot of concern about the word "reciprocity." It means exactly what the user intends it to mean and it is different for almost every user. It is not too far from the Golden Rule when you think about it.

Senator PACKWOOD. But we realize that it cannot necessarily be sectoral.

Mr. HECKERT. It may or it may not be.

Senator PACKWOOD. Well, it may not be. I remember several years ago we had a situation with Korea where they would not let us sell insurance in Korea.

Mr. HECKERT. Yes.

Senator PACKWOOD. Reciprocity was of no use. They do not sell any insurance here.

Mr. HECKERT. Ah, but they sell other things.

Senator PACKWOOD. That is right. So that is why I say it cannot be sectoral. So long as the NAM and Du Pont would be willing to say, "You will not let us sell insurance. You will not let us sell cars. You will not let us have banking services. We are going to take a reaction against you." And the reaction may be adverse to Du Pont.

Mr. HECKERT. It may be.

Senator PACKWOOD. It may be something that you buy from Europe in your manufacturing process.

Mr. HECKERT. It could be.

Senator PACKWOOD. All right. So long as you are willing to gc along with that, that is fine.

Mr. HECKERT. Well, I am not suggesting that we ought to become gunslingers. I am saying that you have to have resolve on the major issues, and one of the reasons we have been disadvantaged in the past is that we have stuck with free trade ideology, come hell or high water. And all of us believe in it, but the rest of the world has a different operating standard and we simply refuse to recognize it.

If I may go on just a bit, most of the thoughts that were expressed by my associates here I would support. Again, I do not

speak for Du Pont, I speak for NAM, and we have a lot of small companies in that organization who helped build our policy statement and our description of what we ought to be doing about EC-92.

The fact is the most important thing that we can do in this country is to provide a competitive environment for business and industry right here in the United States. That is really getting at our international trade problems.

Senator PACKWOOD. I will make you this bet, though. Europe, on average—now, it is worse in Scandinavia and not quite as bad in the United Kingdom—has much higher rate of taxation than we do totally, and if they ever succeed in putting Europe together in 1992, I will wager that the Northern European countries are not going to be wild about wage scales one third of the Northern European in Greece, Portugal, Spain.

Mr. HECKERT. That is right.

Senator PACKWOOD. That, in the long run, their manufacturing costs are going to be higher than ours, and that means that if we are at all efficient that we can manufacture in this country cheaper than they will be able manufacture in the market.

And the question is will the kinds of companies thatMr. Coffey represents be able, not only to manufacture efficiently, but get into the market, and I think the market is going to say, "No, we do not want that because we cannot compete with you." They are saying it to Japan now.

Mr. HECKERT. I think this can be accepted as most likely, namely, Europe will take care of its own economic interests. That is what their leaders believe their business is, and so we will have to watch them constantly to be sure that they do not introduce rules or tricks of one kind or another that are adverse to American interests. But that is their job, looking after their people and their economy, and I believe that when they look at both sides of the question, the importance that they attach to overseas markets, they are going to be reasonable. Now, neither one of us knows.

Senator PACKWOOD. If we are willing to say that we mean retaliation, which is not protectionism, that is when all else fails and you finally negotiated it down to the end and you each turn up whole card and you cannot agree. We say, all right, then it is tit for tat, and if the major American businesses that could be hurt by the retaliation are willing to say in the long run that is what we have to do for our sake, not just America's, our business' sake, then that is good.

Mr. HECKERT. Bear in mind what I believe is that that behavior will not necessarily result in a protectionist world. I think that we will get the attention of our trading partners and we will get some corrections of unacceptable practices.

Senator PACKWOOD. Now, Mr. Coffey, let me ask you. Your company sounds like exactly the kind I am talking about it. They cannot justify a manufacturing plant in Europe in most cases.

Mr. COFFEY. Exactly.

Senator PACKWOOD. And if they cannot get into Europe, they are just shut out.

Mr. COFFEY. That is correct. That is correct. And, Senator, just for your information, I mean there is tremendous technological in-

novation going in the United States right now and tremendous technical investment going on. There are small companies in the United States right now whose labor costs are less than five percent of their cost for a product. I can tell you that there is no country in the world that can compete against five percent labor costs. They are all going to be higher. So that kind of innovation is going on through technology right now, particularly in our industry which is always a leading-edge technology industry.

Senator PACKWOOD. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Senator Riegle.

Senator RIEGLE. I want to just continue along that line of discussion.

It seems to me the problem, however, if I may say to Senator Packwood, about us establishing our ability to be the low-cost manufacturer, which in the case of the Texas company it may presently be, and that is that there are a whole host of other factors apart from trade barriers and trade cheating that pile in on top of this, for example a higher cost of capital in this country. I assume that that particular outfit that has gotten its labor costs down is probably very capital intensive.

Mr. COFFEY. Yes.

Senator RIEGLE. And so it is very sophisticated. It has expensive equipment, and it obviously is paying a higher real rate of interest than most other modern countries are paying or having to pay in terms of cost of capital. I suspect the taxation rates are higher, partly because we carry the burden for the Free World defense to a greater extent, and we have certain other aspects of trying to address pollution costs and things of that kind that indirectly get factored into the cost of doing business in this country.

And it seems to me that as the world continues this interconnecting process that anything that impedes our ability to be able to trade fairly, we have to fight. No question about it. I mean in a sense it is engaging in a fight that is already going on. It is a fight against us now that is being waged with various unfair trade practices, but if we do not have an effective counter-response, then we are going to slide backward. There is just no other way around it.

And I am greatly concerned now that we are still not conceptualizing this in a broad enough framework, not that it is easy to do. The world has changed so fundamentally that about as close as we get to an understanding is this kind of a discussion.

But it seems to me the United States now must take itself through a new kind of analysis where we develop a national strategy for dealing in a global economy where we really develop a much higher order of national teamwork and cooperation and very sophisticated responses in terms of our financial mechanisms, our trading mechanisms, the degree to which we foster research and development and technology advancement, and the degree to which we face off against trade cheating in the world in all of its various forms that otherwise will cause us, I think, to slide backward. And I think in many areas now, you can document the backward slide.

The trade deficit is just one example. We are adding a billion dollars of international debt every three days in this country off the

trade deficit, partly because of problems that have been illustrated here.

Mr. Olmer, let me ask you. You mentioned the automobile sector in terms of possibly the one that would come to mind in response to the Chairman's question.

Can you take that another step or two in terms of just how we ought to think about the integration and the competitive problem where you have high value-added production of that kind that quickly gets into multiples of several billions of dollars, and also the down-the-line job creation? Obviously it is very important from a European point of view that they keep high value-added production where they can because of all of the ancillary job creation that goes with it. But conceptualize a little further, if you can, as to what that means in something like cars and trucks and that part of the industrial base as we continue to accelerate this integration of the world economy.

Mr. OLMER. Well, as you well know, Senator Riegle, we are talking about the steel industry, glass, textiles, rubber, and increasingly, electronics. I learned a fascinating statistic in preparation for this hearing: by the year 2000 there will be approximately $1,500 worth of electronic components in every automobile produced.

The fact of the matter is that Europe is not today competitive with either Japan or the United States in the production of automobiles and that presents a political dilemma. The European Commission, the European governments, have an interesting and very difficult decision facing them in the immediate future.

France has thus far gone along with Prime Minister Thatcher's formulation on the Nissans produced in the United Kingdom, but Italy has not. Italy accepts 2,600 Japanese automobiles a year, period. Any automobiles produced in the United Kingdom with 80 percent European, not just United Kingdom, but European content, Italy will continue to consider Japanese and count against that 2,600. The Commission, I am advised, has told Italy that it is going to have to knuckle under; but we will see.

If they do not—or if the way which I think is sort of typical in today's world, but it has been typical of negotiations on trade issues in my experience with the European Community over the years, especially in agriculture and steel—they will have a side agreement, a so-called gentlemen's agreement, and the Japanese may agree to continue limiting shipments to particular parts of the European Community. Well, that may have a ripple effect on our economy. We may get more of what might have been sent there, or we may get automobiles produced in Europe by Japanese subsidiaries shipped to the United States.

The allocation of subsidies is a very serious issue. There is only one way they are going to be able to deal with the political problems in Europe and that is by paying people off, paying industry sectors off, and I think that will have a ripple effect in other areas as well.

Sorry for going on.

The CHAIRMAN. Senator Heinz.

Senator HEINZ. Thank you, Mr. Chairman.

Mr. Olmer, welcome back to Congress. It is nice to have experienced witnesses like you, as well as——

Mr. OLMER. You mean old.

Senator HEINZ [continuing]. Your associates. [Laughter.]

It applies equally, so I chose not to mention that.

On pages 3 and 8 of your testimony, you mentioned European targeting of high tech and commercial aircraft through what you refer to as "tens of billions of dollars" of government subsidies. Now, that is an extraordinary amount of money. It is, if accurate, a de facto exemplification of the industrial policy challenge that Senator Danforth was told that EC-92 might amount to. Certainly, it comports with the speech of the Phillips executive he referred to.

What is the relevance of that to EC-92 as you see it?

Mr. OLMER. Thank you, Senator Heinz.

In responding to that question I might relate it to agriculture and steel and automobiles. That is to say I believe that Europe does want to reduce the subsidies that are being wasted in the agricultural sector.

I believe that Europe is serious about creating an integrated market and to gather within the 12 member states more productive companies, but a lot of companies are going to have to go under. A lot of companies may have to get into new kinds of businesses, and if there is success in the agricultural negotiations, there will be a lot of people out of work. I do not know what the average European-wide is, but many of the countries have in excess of nine percent unemployment today.

Europe has spent roughly $14 billion to sustain Airbus in its 20 years of existence. It knows, it has acknowledged, that Airbus has never made a profit and never will make a profit, from its inception to as far as the eye can see.

There are a lot of companies in the United States that are dependent on the aerospace and civil aircraft manufacturing sector, small component suppliers. The Europeans want to create a component supply industry, and I think that if we let them get away with that, they will take it as a precedent of acceptability. I mean they keep us sullen but not mutinous, and that is okay.

The CHAIRMAN. Keep us what?

Mr. OLMER. It is an old Navy term, Senator Bentsen, and I am sure you will recall it. It is keep the sailors sullen, but not mutinous.

If we do not react too strongly, it will be seen as tolerable. A demarche from the State Department is not going to cause any serious indigestion if it is not followed up with tough action, and I would be concerned that if nothing is done about that area, the Europeans will take it as a precedent applicable to the bail-outs that are going to be required in agriculture and in a host of other industries and companies that are going to either go under or are going to need some help from government.

Senator HEINZ. Lionel, what should we do about it, particularly in the context of EC-92 and anything that Ambassador Hills does in the next month or two or three?

Mr. OLMER. I have a couple of responses, Senator Heinz.

One is that you properly asked about the accuracy of the number tens of billions. The number for Airbus alone comes from a Department of Commerce, Economic Policy Council sponsored study, which has still not been released to the general public, which cal-

culates between $12 and $14 billion for that industry sector alone, that particular project alone, leaving aside what has been spent on computers, telecommunications, semiconductors, and so on.

As to what to do about it, I think that the U.S. Government has got to come up with some timetables. I was heartened by Senator Packwood's interest in getting some dates out of the U.S. Trade Representative with respect to agriculture, and I think that needs to be done with respect to 1992. Either we get the kind of assurances that are backed up by references in the directives that the EC issues, or we respond in a way which lets the EC know in unambiguous terms that it is not acceptable.

Senator HEINZ. Mr. Chairman, I see my time has about had it.

The CHAIRMAN. Thank you.

Senator Danforth.

Senator DANFORTH. As we deal with the Europeans with respect to 1992, do we—and by "we" I mean our government and our business community—have our act together? That is, is the business community focused on the details of 1992? Does it know what is going on? Is it making preparations for 1992? Does it express its concerns to our government? Is our government receptive, and is our government effective in dealing with these problems?

Mr. Coffey?

Mr. COFFEY. Well, Senator, I think I have made pretty clear my feeling on that subject. I do not feel that we have our act together because we have not addressed some of the very fundamental trading relationships with Europe, the offset policy, the counter-trade policy, which is a very ingenious policy on the part of Europe because it was not imposed government to government. It was imposed government to individual company in the United States.

And the ripple effect of that kind of a policy is that the company in the United States offering 130 percent of value taken back from the country really winds up being a net importer into the United States in addition to making promises of domestic content in Europe, which takes the supplier industry out of the United States and into Europe. So I think there is a big, major policy issue that we have never had a debate on in this country, and yet, it has been in existence now for ten years. And company by company the European countries are knocking off deals of this kind.

I think that, you know, as far as our association is concerned representing small manufacturers, we have taken advantage of the export trading law. We have formed an export trading company. We have put all 3,000 of the companies in that trading company. We are attempting to build a marketing structure to market these companies in Europe, and you know, despite all that aggressive action, we have a very hard time communicating with the United States Government.

Mr. HECKERT. Could I respond?

I think that the major industries are paying very close attention to their interests in Europe and know exactly what is going on. I am not sure all of that is being communicated to government, but I suspect when a major issue surfaces that they are concerned about that they think you can help with, you will hear about it.

Some of it they just regard as, you know, the natural course of events, and Europe, as I repeat, is not perfect today. Nobody in this

room is naive enough to think it is going to be perfect in 1993. If it is no worse, marginally better, and is one market with relatively few internal boundaries, it is a huge plus for U.S. interests. We just have to keep that overall perspective in mind.

I think the people who have large stakes in Europe are paying attention to what is going on. Obviously some of the rules have not been written yet or decisions made. I think it is a mistake to pick something like agriculture where we have not had huge success and assume because it has been tough sledding there, that everything else is going to turn out the same way.

When agriculture was singled out as the number one goal of the current GATT round of negotiations—an area where we in the United States felt we had to make some significant progress—I thought, "Oh, boy. If there is one thing that everybody in the world knows, every country takes care of its farmers." And to change that culture around the world is going to take some time.

Now, I think Ambassador Hills described it very well. We can have a very clear view of where we want to go and we can work very hard for very significant change. But I would not jeopardize everything else that we have agreed on with our trading partners around the world on a large amount of success early on in that area. I think that is an unrealistic expectation.

Senator DANFORTH. Lionel?

Mr. OLMER. Well, the question of whether all companies great and small have their act together is really a relative one. To a company with 20 employees that has 60 percent of its sales opportunities in Europe, that is a pretty big question for it. But in the large picture of a $170 billion export effort, it is rather small. And yet, I think we have an obligation to that small company just as well.

The Chamber of Commerce has embarked on a 1992 educational program and I think that is a major first step. We do have to inform the business community at large, small, medium, and big, as to what the stakes are, what the sore points are, what the problem areas are. I think we need to work more effectively with government, and I do not yet see any problem with doing it, but I do not believe it has yet happened, because the government has not yet focused on what our priority interests are.

I share the view of the last speaker regarding the prioritization of agriculture, and yet, it was something we said early on was going to be number one. We have somewhat backed off from that, I think, is the perception around the world. However strongly the Europeans feel about agriculture, they feel equally strong about not being left behind in high technology. They feel equally strong about the steel sector and textiles.

So I think we have an awful lot of work to do, and they look on all of those industries as near and dear to their future success.

Mr. HECKERT. That is true.

The CHAIRMAN. Are there further questions?

Let me state, gentlemen, as I listened to the three of you, I think you have been extremely helpful and I think you have articulated the positions of those groups that you sought to represent very well. As I read some of the writings concerning Europe-1992 and trade and the trade deficit, some of them are so superficial, but you have talked about the complexities of them, understanding full

well that the Europeans are going to fight for their self-interest. That is their job, but so must we. In trying to accommodate those differences to result in the benefit of all is our objective.

Thank you. You have been very helpful.

[Whereupon, at 12:02 p.m., the hearing was concluded.]

APPENDIX

ALPHABETICAL LISTING AND MATERIAL SUBMITTED

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC, June 22, 1989.

Hon. ANNE BRUNSDALE,
Chairman,
Hon. RONALD CASS,
Vice Chairman,
U.S. International Trade Commission, Washington, DC

Dear Madam Chairman and Mr. Vice Chairman: Recently reports have appeared in the press suggesting that you will be meeting with officials of the European Community and of the General Agreement on Tariffs and Trade to discuss the need for harmonizing antidumping and countervailing duty rules. You have also been reported as criticizing current antidumping and countervailing duty laws of the United States.

We believe it is important that the International Trade Commission (ITC) remain a source of independent advice to both the Executive and Legislative Branches on trade matters, but there is no mandate for the ITC to negotiate with foreign officials. Moreover, we would appreciate learning about policy problems you have with the operation of existing U.S. law from you directly rather than from press reports.

We would be interested to know your comments.

Sincerely,

DAN ROSTENKOWSKI,
Chairman, Committee on Ways and Means.
LLOYD BENTSEN,
Chairman, Committee on Finance.

U.S. INTERNATIONAL TRADE COMMISSION,
Washington, DC, June 24, 1989.

Hon. LLOYD BENTSEN,
Chairman, Committee on Finance,
U.S. Senate, Washington, DC

Dear Senator Bentsen: I have received your June 22, 1989, letter concerning my meetings here in Europe with officials of the European Community (EC) and the Central Agreement on Tariffs and Trade (GATT). Clearly, there has been some misunderstanding about the purpose of my trip and the content of my discussions. I am happy to clarify the record. for both you and Congressman Rostenkowski, to whom I am sending a similar letter.

As you know, the Commission is currently preparing a comprehensive report for your Committee and the House Ways and Means Committee concerning the impact of the EC-92 market unification program on United States interests. The primary purpose of my trip to Europe is to enhance my understanding of the EC-92 initiative. The briefings and discussions arranged by the State Department and USTR with American officials, EC officials, representatives of non-EC countries affected by EC92, and business groups within the EC are serving this purpose well.

During my stay here in Europe I have also taken the opportunity to speak with officials, academics, and business groups who are interested in the work of the Commission, particularly with respect to the implementation of dumping, countervailing

duty, and safeguard (escape clause) provisions. While the views of foreign practitioners are not directly applicable to U.S. practice, they provide useful perspectives on these issues. Let me note that not only would it be improper for me to engage in policy negotiations of any kind in these meetings, but I am making this limitation on my role clear to all those with whom I am conferring.

What I have had to say is identical to themes I have dealt with in my published opinions and in my speeches in the United States. First, we and our trading partners have an interest in making certain that our cases be conducted openly, that our reasoning be transparent, rigorous, and thorough, and that we employ the best analytical tools available. Second, I have noted the increasing frequency of cases before the Commission in which the domestic producers are themselves foreign-owned firms, where foreign producers are U.S.-owned firms, and where the product at issue is an intermediate product necessary to the production of another article important to the U.S. economy that is manufactured by a domestic industry vociferously opposed to the petition. These matters present interesting intellectual issues bearing on the implementation of dumping and CVD regulations that I believe merit discussion. In most investigations where they arise, the Commission majority reaches the same results that I do.

I certainly agree with your final observation regarding the desirability of close consultation between ITC Commissioners and members of Congress. As you may be aware, I discussed these and other issues at the meetings I held with the staffs of your Committee and the House Ways and Means Committee, and at a breakfast the Commission hosted for members of the House Ways and Means Committee.

I would welcome the opportunity to meet with you personally to continue discussions on these and any other matters upon my return.

Very truly yours,

ANNE E. BRUNSDALE, *Chairman.*

U.S. INTERNATIONAL TRADE COMMISSION,
Washington, DC, June 25, 1989.

Hon. LLOYD BENTSEN,
U.S. Senate, Washington, DC

Hon. DAN ROSTENKOWSKI,
U.S. House of Representatives, Washington, DC

Dear Chairman Bentsen and Chairman Rostenkowski: I am happy to respond to your letter of June 22. I hope you will understand that I can only address the statements I made, not those attributed to Chairman Brunsdale. We were not interviewed together by the reporter who prepared the press report to which I believe you refer, and I am certain that the Chairman will respond for herself.

First, I am not negotiating with foreign officials, nor have I at any time indicated an intent to do so. Although I do not know what the Chairman said regarding our trip to Europe, I would be greatly surprised if she described our talks as anything other than what they have been: discussions arranged by the Department of State with U.S. officials road, officials of other countries and of the European Community, and with private parties, designed to provide us with a better understanding of the European "single marker" process and of the way in which other officials implement laws similar to Title VII of the Tariff Act of 1930. In some discussions, we also have explained the operation of the U.S. laws that we are in part responsible for implementing.

Second, let me emphasize (that in speaking to reporters and foreign officials, I have not addressed the proper scope of U.S. trade law, nor do I believe the reports of my public statements (which are not always perfectly accurate) make such a claim. I do not take it to be the role an ITC Commissioner to set trade policy, to urge Congressional changes in U.S. trade policy, or to critique U.S. trade policy. I have described the way U.S. trade law works, and I also have discussed differences between U.S. trade, law and other national trade laws. For example, in response to a question from one reporter, I noted that U.S. antidumping law differs from the antidumping laws of Canada and of the European Community in that it does not have a "public interest" exception. The ITC is nowhere directed to examine the overall effects of dumping on the U.S. economy; we examine only the effects of dumping on a particular segment of U.S. industry. In contrast, the EC and Canadian antidumping laws specifically direct administrators not to impose antidumping duties, regardless of the effect of dumping on the competing domestic industry, if such duties would harm overall national economic interests. It is inconceivable to me that such observations would be construed as criticizing U.S. antidumping law

or would be regarded as inappropriate to the role of members of an independent agency.

I do not, however, hesitate to consider and discuss critically issues relating to the interpretation and implementation of trade law. I very much take it to be my role to read carefully the statute I apply, to think about its application, and to try to make its application consistent with established legal principles. In that regard, I disagree with the way some of my colleagues read U.S. trade law. I have said so in a great many published opinions. While I believe that the sort of differences of interpretation that I have raised in that context are important, they do not call for changes in U.S. trade law. Indeed, the very point I have made repeatedly is that the issue is not what the law should be, but what it is.

The interpretation of U.S. trade law by the ITC is also a matter that I have discussed before public audiences. Everything I have said in that context I have also said in published opinions. Although I am willing to discuss issues of legal interpretation before any audience, when speaking in other countries, I am careful always to note that the ITC is unanimous in most cases, no matter what differences in interpreting the governing legal standard inform the individual commissioners' judgments.

I would be glad to discuss any of these issues directly with you or members of your respective staffs. As you may know, during the past few months, I have discussed a variety of issues, including many of those touched upon in this letter, with members of the staffs of the Senate Finance Committee and House Committee on Ways and Means at meetings that were hosted by Chairman Brunsdale. Please let me know as well if any other information about my views, statements or activities would be of interest.

Sincerely,

RONALD A. CASS.

PREPARED STATEMENT OF MATTHEW B. COFFEY

INTRODUCTION

I am here today on behalf of the National Tooling and Machining Association.

Our industry has two distinctive characteristics. First, it is the backbone of all American manufacturing. Anything that is mass produced by machinery—whether toasters, pens or silverware, rocket parts, car engines or computer keyboards—is shaped by tools, dies, molds, machining and special machines. Without our "products", there can be no mass production. It was the creative genius of our predecessors in the 15th century that gave America its industrial might and preeminence. Today, our members are one of the nation's most technically innovative and advanced industries—at the cutting edge of high technology. And if America is to continue to have a domestic manufacturing capacity of any kind in the next century, then we must have the ability to create the tools, dies, molds, machining and special machines that allow our factories to work. There is no other service or product that is so essential to every aspect of American industry.

The second distinctive characteristic of our Association, and one that is particularly relevant to this Committee's deliberations, is that we represent the classic American "small business" industry:

- 12,000 separate companies
- 80% under 20 employees
- typical firm has 8 or 9 skilled craftsmen, with 1 or 2 support clericals
- virtually entirely owner-operated; a truly entrepreneurial industry.

There is probably no other manufacturing industry in America that has this "small business" profile—a profile usually found in local retail and service businesses (cleaners, grocers, drug stores) not in manufacturing and production.

Our industry is so highly fragmented because of the unusual nature of our manufacturing process:

- *customized*—almost every job is a custom assignment to meet a special need, not susceptible to mass production;
- *industry specific*—while heavily concentrated in such fields as automotive, defense and aerospace, our companies work for every industry and every American manufacturer collectively we cover the whole economy, but on an individual basis most of our firms tend to focus on niches in particular industries;
- *creative*—our work often requires the development of innovative designs and new production techniques which involve extensive research and testing;

• *skilled*—our workers are highly skilled craftsmen, trained in engineering, mathematics and technical design;

• *precision*—we produce extremely complex close-tolerance products, regularly meeting standards of 1/10,000th of an inch--equivalent to 1/20 the width of a human hair; and

• *service*—while we produce tools, dies, molds, and precision metal parts, our customers are themselves manufacturers and we must respond to their frequently changing technical requirements.

Because of the small size of our firms and the customized nature of our work, this has always been an extremely competitive industry. Our members compete against each other and against foreign firms for each piece of business. As a result, there is constant pressure for quality work and cost effective innovation that continually selects the best-managed and most skillful firms for survival.

Our members are consequently independent, determined and self-reliant. They not only run every aspect of their own businesses, but they take personal responsibility for quality and service and for the economics of their firm. They have no one else to lean on, to turn to or to blame. They are realists who must deal with changing economics and new technologies. And they accept the burden of adapting to change if they are to remain competitive and survive.

THE CHALLENGE

Our industry is in the process of massive changes, which challenge the innovativeness, management skills, and financial resources of NTMA's membership. The members are challenged to change their process technologies, which have undergone rapid conversion from old-line mechanical controls to computer-driven lasers. They are challenged to upgrade their work force to fit with the new capital and technologies. They are challenged to adapt to the demands of their customers as they are undergoing rapid technological change and a restructuring in the way they do business—new processes, new materials, finer tolerances and specifications, and new business locations.

A final set of challenges comes from international competition. We are seeing a competitive environment around the world change rapidly and substantially because of three major factors:

• The movement offshore of major U.S. manufacturing facilities with the corresponding purchase offshore of the supporting tools, dies and molds;

• the development of increasingly high-level technical expertise and skills by foreign firms (largely as a result of past U.S. policies to strengthen these foreign economies); and

• the favorable economics of foreign firms based on such factors as government subsidies, lower cost of capital, lower employee benefit costs and fewer mandated costs imposed by government regulation.

While our members recommend free and open competition, these factors have placed unrealistic capital burdens on small owner-operated businesses.

EUROPEAN COMMUNITY '92

Some of our members have been successful in the European market because of their ability to compete, when the dollar was strong, with know-how and technical superiority. Most of our members don't even try because they find the market too complicated, the standards too numerous, and up-front costs too high.

The development of the European Community '92, however, offers a tremendous opportunity. It represents a single market with over 300 million consumers, thereby larger than the U.S. market. It theoretically could offer easier and more free-wheeling competition because of products being designed to world standards as opposed to twelve individual country standards. By eliminating individual country tariffs and border regulations and controls, it could make uniform marketing throughout the market possible.

Those are the ends held out by the political leaders in Europe and the European Community bureaucracy. But there are problems in this land of opportunity.

ANTI-TRUST

In preparation for 1992, European governments are allowing rationalization of companies to occur. One only has to look to the example in the German Forging Industry where, with government encouragement, Krup, Klockner and Theissen have been allowed to form a single new company without the concern for anti-trust that hampers American industry. The crankshaft industry is also undergoing mergers in anticipation of becoming world-class competitive with government assistance.

Small U.S. manufacturing companies are at a severe competitive disadvantage because they are not allowed to join together domestically in consortiums, except under the imperfect form of an export trading company. We have formed an export trading company for our industry.

We believe the Flexible Manufacturing Act, HR 423, proposed by Rep. Wyden, represents the appropriate approach to flexibility, freeing small companies to form temporary consortia so they can market and compete jointly in what promises to be a highly competitive world market. We believe that American companies should have the same freedom to compete in Europe that European companies have to compete in the U.S. We do not shy from competition; we just ask the government to make the rules equal, and we do not presently believe they are equal.

STANDARDS

The European Community bureaucracy is currently funding the development of uniform standards for the European Community market. Standards could be a substantial competitive disadvantage. If the International Standards Organization (ISO) which is headquartered in Europe, decides to amend its standards to conform to new European Community standards rather than the European Community agreeing to present world standards, American companies could suffer tremendous competitive disadvantage. Small companies would once again not compete.

SUBSIDIES

To the extent that individual governments encourage targeted segments to the industry through favorable financing arrangements, export credits and counter trade policies, they in fact make American sales more difficult. When are we going to stop treating the Export-Import Bank as a welfare program and make it an effective instrument of trade policy? The Credit Reform Act proposed in 1987 should be resurrected with amendments to encourage small business exporting.

COUNTER TRADE

The American government must revisit the entire issue of counter trade. At present there is a one-way street with European countries demanding that American companies take counter trade in products sometimes equal to or in excess of the amount of the sale. Government policy has been to ignore counter trade, or to force American companies to accept it for defense reasons. Now that we see big, powerful companies being put together with government encouragement in Europe to exploit a market bigger than the U.S. market, we must focus on the issue of counter trade and re-think the American position.

CONSUMPTION TAX

Every European country charges a form of consumption, or value added, tax on every product sold in that country. Those taxed products pay for elaborate social welfare systems and reduce the taxes on income and profits in Europe. If we are interested in helping U.S. companies persevere in the trading relationship, then consumption taxes on imported goods into the U.S. must be realistically addressed. Whether the approach is Senator Roth's Business Transfer Tax, or a direct consumption tax on imports, it offers a way to meet the increasingly higher demand for social services that cannot be financed out of present general revenues.

SUMMARY

The National Tooling and Machining Association has launched an aggressive program to interest its members in the European Community '92. It has formed an export trading company covering all 3,000 of its current dues-paying members so that they might more freely engage in foreign competition. Since the dollar has been rationalized, we have seen more and more European firms coming to the U.S. tool and die industry asking for quotations. In general, the world is moving toward a more balanced trading system. The European Community can accelerate that process or stifle it. The challenge for the U.S. government at this time is to review its policies on anti-trust, export financing, foreign military sales, foreign subsidies, counter trade, and consumption taxes so that it can flexibly respond to governments in Europe. If government subsidies or industry targeting occur, we must be prepared to retaliate. Large corporations who have manufacturing facilities in Europe have a real advantage. Small companies that have no facilities in Europe will be at a competitive disadvantage unless the Congress and the Executive Branch agencies are

vigilant in watching every step in Europe and being prepared to respond quickly before traditions get built up in the new market.

ADDENDUM

PERSPECTIVE OF EUROPE

Many Europeans believe that the post-World War II economic order has changed fundamentally to favor them. They see a world in which economic and even political power is being shared on a trilateral basis among the United States, Japan and Europe. They believe that "The global economic order now in process makes obsolete the undisputed economic and political leadership provided by the United States in the decades after the war." Europeans appear to resent statements by American presidents and political leaders that we are now actively designing strategies to maintain and guarantee our economic superiority into the 21st century. (See, for example "Europe in the World Economy: 1988 Stuttgart Conference" by Alfred Herrhausen, Executive Board Speaker of Deutsche Bank, and Lothar Spath, a German state governor, in the McKinsey Quarterly, Winter 1989.)

This attitude lies behind the fierce competition from Europe that American small businesses face. It is an attitude that gives rise to massive European subsidies for business and to restrictive, quasi-protectionist policies of Europe including their infamous offset policies, which I will speak more about later.

Europeans also very much look forward to the greater trade bargaining clout they anticipate having with the advent of Europe 1992. I fear this clout. I believe that Europe may expand the request for offset or trade reciprocity required of U.S. companies seeking to sell into the European market. In other words, the large offsets imposed by the European countries for military sales may be imposed on smaller sales, gradually affecting more and more U.S. companies, including members of our own Association.

THE PROBLEM OF OFFSETS

This issue has been well-documented in Winning the Countertrade War: New Export Strategies for America (John Wiley & Sons, New York, 1989, a recent book written by Matt Schaffer). A brief statement is needed about this issue because offset is a troubling index of the forces we now face as a country for doing business in Europe. Every country in Europe has an offset policy yet America does not have such a policy.

The practice of demanding offset or mandated reciprocity from U.S. companies began with the F-16 sale to a consortium of NATO countries in 1975 and with the Swiss purchase of Northrop's F-5 in the same year. Offset in the first case for the F-16 included mainly a co-production agreement, where a certain percent of the planes had to be constructed in Europe (the Netherlands) as part of General Dynamics' price for making the sale. Northrop had to commit to export a value of products from Switzerland equivalent to 30% of the $400 million contract. The U.S. companies had little choice but to comply with the European offset request or lose the sale. This type of policy has now spread to certain other sectors outside the area of defense, such as telecommunications, and to countries in Europe such as Spain which had no offset policy before 1980. Other notable examples of offset included Raytheon's sale of the Patriot missile to West Germany in 1984 and Boeing's sale of the airborne radar plane AWACS to Great Britain and France. (Japan has been similarly successful in extracting offset agreements from U.S. companies, such as in the recent FSX case where technology transfer and co-production agreements were necessary in order to win the sale.)

In my view, U.S. companies have been valiant and creative in meeting these offset requests and should be left alone by the U.S. government to make their best offer. From America's point of view, having some sale built in this country is better than having no sale at all. U.S. companies should expect to joint venture with co-production agreements more frequently in today's world. It is a fact of life that can also grant access to new markets and to financing, as when successfully concluded by Boeing in the sale of the 767 sale to Japan's commercial fleets after co-production and co-financing agreements were concluded allowing some 6% of the plane to be built in Japan.

However, U.S. companies should not be at the complete mercy of foreign governments set on extracting (extracting is a polite word) every ounce of economic advantage out of sale, as if the goal of every European country, or Japan, is to be certain that all or most of the product is produced in the purchasing country and all or

most of the key technology to make the product is transferred out of the United States as well.

The offset policies of Europe have now been imitated by a number of U.S. allies and trading partners, including Israel and Saudi Arabia in the Middle East and several countries in Latin America and Asia including Japan, The People's Republic of China, South Korea and Indonesia.

Why is this a problem for the United States, and what is to be done? In particular, why is offset a problem for small business in this country?

THE EFFECT OF OFFSET ON SMALL BUSINESS

Prime contractors understandably seek help from their sub-contractors in coming up with ways to comply with a European offset request. There are numerous examples when sub-contractors have risen to the occasion by transferring technology overseas or by purchasing components from overseas, all in order to help the prime contractor win the sale. General Dynamics' partnering with its sub-contractors successfully in this way has helped it to win a number of hotly contested sales. Caterpiller, another large U.S. exporter, similarly has an ingenious "materials management program" designed to help the company's suppliers source or purchase their own components from overseas countries such as China where Caterpillar needs the countertrade credit in order to win sales into that country. (Countertrade credit is like offset. You can win a sale into a country only if you can demonstrate that you have generated exports or the equivalent from that country.)

The bottom line is that considerable pressure is put on the smaller company to transfer technology or to purchase components from overseas. These actions by smaller companies are often in their best interest. However, in one case, Menasco Texas, a subsidiary of Colt Industries and a supplier of landing gear to General Dynamics, was obliged to transfer technology to a Dutch company called DAF as part of the F-16 sale to NATO. (See Eileen White, The Wall Street Journal, September 10, 1987, pp 1 and 15.)

However, let me be very clear. The pressure generated by offset on U.S. companies, whether large or small, to purchase components from foreign countries and to manufacture in foreign factories is definitely not good for the U.S. trade deficit.

There is a further, perhaps even more difficult problem caused by offset for the smaller manufacturer here in the United States.

Offset and the whole pervasive set of policies the concept has spawned overseas puts enormous pressure on the largest U.S. companies to purchase components from overseas and to locate their factories overseas. Some business is definitely taken away from small business in the process. True, some new sales may go to the smaller U.S. company as prime contractors are successful, but the pressures of each transaction are all in the opposite direction, to direct the flow of purchasing out of the United States.

WHAT IS TO BE DONE?

Offset works with awesome effectiveness. That is why countries ask for it. Few companies large or small have the power to resist complying as fully as possible. The threat of losing the sale looms very large. After winning a contract, the company continues to be under pressure to comply. Otherwise, penalties in the offset will take effect, or worse, the non-complying company will lose future business in that country. Complying well can build a marvelous reputation for a U.S. manufacturer in a country, as happened in the case of General Dynamics in Turkey.

Pressure is clearly needed on our trading partners to curb their growing appetite for offsets. The offset values that were 30% of contract value only three years ago are now 130% of contract value in some cases, and the percentage is climbing.

Since offset harnesses purchasing clout so effectively, how does the United States generate pressure? In discussions through the GATT (General Agreement on Tariffs and Trade) European countries have not been receptive to U.S. attempts to negotiate curbs on offset. We have little bargaining leverage without some offset policy of our own. The Europeans do not take us seriously.

DILEMMA FOR THE UNITED STATES CONGRESS

I believe that Congress needs to begin thinking about how to enact an offset policy for this country. Such a policy could accomplish two important objectives:

(1) Create bargaining leverage to use in reducing our allies' demands for offset. In this scenario American offset policy becomes a bargaining chip.

(2) Offset by-passes government policy of the targeted market and applies pressure initially on the company wishing to make the sale.

To understand this latter point, consider the following line of argument. France and Britain know the United States government may not be happy if a 130% offset is applied on Boeing in order for that important U.S. company to make a valuable AWACS sale. Yet Britain and France proceed anyway, applying the policy not on our government, but directly on the U.S. company. Congress holds hearings. The White House might like to say something (following the wishes of the Commerce Department) but does not. Boeing wants the sale. The two countries say domestic pressure over the huge cost requires the offset to justify an expenditure of foreign exchange on such a large scale.

Japan similarly uses the offset concept to insist that General Dynamics transfer technology in the FSX sale and co-produce a major portion of some 60% in Japan. We have little direct bargaining leverage, so General Dynamics makes its best deal and the United States does what it can to safeguard some technology and production here in this country.

We must understand that we have very little bargaining leverage in these situations. It is natural. It is structural. In a large purchase, the bargaining clout remains with the buyer and not the seller.

We need an American offset policy to harness U.S. purchasing clout!

BUILDING A U.S. OFFSET POLICY

It is essential for U.S. offset policy to be directed at foreign countries with similar policies already in place (Europe, Japan, Canada and Australia), and not at U.S. companies struggling mightily to win export sales. In this treacherous offset environment, the U.S. companies must always be free to make their best deal.

The above countries have been most effective in applying offset in cases where the purchases are made on a government basis. Even though U.S. government purchases from overseas are relatively small by comparison with Europe, we could consider taking the first step by requiring offset on these purchases. Despite a buy-America policy, the Pentagon might consider requiring offset of European companies seeking to gain entry to that lucrative market.

However, even if offsets are applied on all U.S. purchases from overseas, the effect would be minimal on our trade deficit. Applying offsets on large foreign importers into the United States such as European and Japanese car manufacturers, would get attention very quickly. Conceptually, we would be doing unto others as they now do to us in the area of their government purchases. Actually, many Japanese and European companies, especially trading companies, are already large exporters from the United States. The Japanese trading companies already are among the very largest exporters from the United States, exporting more from this country than thousands of other U.S. manufacturers. Many European and Japanese importers into this country are already thus well-positioned to export even more from the United States.

A U.S. offset policy would say:

(1) Yes, we believe in free trade.

(2) Rather than applying more trade barriers with additional tariffs and quotas, we believe that large importers into the United States bear a special responsibility to export more from this country.

(3) Imports into the United States above certain levels would be allowed only if the importer achieved an established export level. (Many Third World countries now insist that a sale into a country be balanced exactly with an export. European countries appear to say the same thing when their offset percentage rises to 100%.)

Since the United States has failed to enlist much cooperation from its trading partners in dealing with the deficit, perhaps it is now time to gain the help and support of foreign companies. Perhaps they should have been the target of our trade balancing efforts all along, since in many cases foreign governments have little power over them anyway.

The exports generated from my member companies through such a policy would be beneficial to those companies and to the resolution of America's trade deficit.

An offset policy may be interventionist (actually counter-interventionist since Europe adopted widespread offset policies first) but at least, Mr. Chairman, it would foster more trade rather than less trade. And the policy would be integrative rather than restrictive in the sense of erecting walls and barriers. European companies would be obliged to look at American products more seriously, including those made by tool and die companies and by thousands of other U.S. companies.

DEVELOPING EXPORT MARKETS FOR SMALL COMPANIES

The creation of an offset policy is basically an exercise in international marketing. Another approach could be equally helpful. Small companies especially in this country are hampered by the absence of sophisticated international marketing staffs. The sort of hands-off orientation programs by the Commerce Department are too passive probably to be very helpful.

What this country needs is a good export trading company! I mean not an import company that brings products into the United States, but an export trading company that develops markets overseas.

Small companies need this service in America even more than large companies.

The trading company would not only develop markets for small companies but would handle whatever shipping, documentation and financing was necessary after the sale was made. Who knows why such trading companies never developed in the United States to the extent possible in Europe and Japan. However, many powerful export trading companies do exist in those countries. In competitive bids they sometimes favor their own national exporter rather than a competing bidder from the United States.

When Westinghouse recently sold an air defense radar system to the Kingdom of Jordan for $100 million, the American defense contractor relied on Mitsubishi Trading Company of Japan to trade the phosphate which Jordan offered in order to pay for the sale. Without Mitsubishi's trading network, the phosphate might never have been sold by Westinghouse in sufficient quantities to allow the sale to go forward. In fact, Mitsubishi traded 80% of the phosphate within the first six months of the transaction.

What would have happened if a Japanese company had been competing with Westinghouse for this valuable sale? Almost certainly Mitsubishi would have had a hard time working for Westinghouse, even though a partnership relationship existed. National loyalties might have prevailed.

While there are numerous examples of where U.S. companies have won sales by putting together the best countertrade transaction, there are also many examples where sales have been lost without the presence of an American trading company to help facilitate the sale.

I must quickly add that in a sale like the one Westinghouse made to Jordan, hundreds of small company subcontractors in the United States benefitted.

This is how a trading company might have benefitted both large and small manufacturers in the U.S.

If the private sector has been incapable of creating and sustaining a general trading company in this country, then I believe that our American government ought to start one for the benefit of companies here and to carry out other vital national objectives. Why not barter American wheat and commodities for valuable Third World products, rather than have wheat stored in bins or rotting on docks. Why not use a trading company to develop more trading with Eastern Europe, the USSR, The People's Republic of China, India and other countries where currency conversion problems and the absence of hard currency (i.e. dollars, yen, etc.) makes trading difficult!

WHY BOTHER TO EXPORT?

Exports project American influence into the world. Wealth allows us to pay for defense. Export trade builds jobs. Export trade is not only economics. Trade is national defense! Exporting more is a matter of the gravest national importance.

Trade also builds a strong, healthy currency. The rise of America's trade deficit has precipitated a dramatic fall in the value of the dollar compared to Japanese and most European currency. Investors from abroad are swarming into the United States to buy land, buildings and companies at relatively bargain basement prices. The Japanese stock market is worth substantially more than the New York Stock Exchange. The real estate value of the Japanese land mass is said to have far greater value financially than the entire United States. Most of the largest banks in the world are in Tokyo, not based in New York.

Should the penalty for America's failure to export be so great?

Sure, trade deficits would matter less if the world had one currency, perhaps constructed from a basket of currencies as the Europeans intend to do with the advent of Europe 1992. But in the real world of the foreseeable future, trade deficits do matter, and in any event exporting projects influence into the world.

There is an old trade joke making the rounds: Taiwan's hotels are flooded with Japanese salesmen and American buyers.

We need more American salesmen and saleswomen, and we need them now. This is especially true for small companies and for the members of my national Association.

WE NEED MORE EXPORT CREDIT NOW

The U.S. Export-Import Bank is an overlooked but critical part of the new trade strategy that I am advocating for small business. Eximbank is equally important for the larger American companies seeking to export.

Eximbank is a model for how the U.S. government, if it puts its creative mind to it, can intervene on behalf of large and small U.S. companies to support their exports with competitive and attractive financing. Exim is also, by the way, a model for how the U.S. government might also start a trading company. Eximbank is highly effective with a small number of people, less than 400. During much of its history, it actually made a profit.

Can you imagine? There is actually a government agency that made a profit. Most trading powers consider their Eximbanks highly worthwhile even when they must be supported by small government subsidies. The force behind profitability is fairly simple. If they have financing of 5-10 years at interest rates of 8-10%, many U.S. companies could sell exports against competition in the world that is loaded with financing in this critical range. Eximbank's cost of borrowing from the U.S. Treasury has often been lower slightly, hence the profit, especially if small loan commitment fees are added in.

We all know the shameful litany of figures. While our trade deficit of $40 billion in 1980 grew to the $160 billion figure by 1988, Eximbank lending to support U.S. exports dropped from $5 billion to a paltry $410 million during the same period. Since Eximbank lending is almost always mixed with commercial bank lending, Exim loans support far more than their actual dollar value. In the late 1970s, with annual lending in the $3-5 billion range, Eximbank was supporting roughly 20% of U.S. manufactured exports.

Fortunately for America, as our trade deficit shot sharply higher in the 1980s and as Eximbank lending was cut, the price of oil fell by more than half.

Can you imagine how much worse the U.S. trade deficit would be if oil prices stayed high during this period! How much lower would the dollar have fallen! How many more U.S. companies and office buildings would foreign companies have been able to buy? We are not out of the woods yet.

As the example of Eximbank helps to illustrate, the strong dollar of the early 1980s did not by itself cause the huge increase in our trade deficit. And a weaker dollar cannot completely cure it.

The two greatest structural features in our trade deficit are a lack of competitive financing and marketing. An actual trading company run by the U.S. government could help to get a major marketing effort going by U.S. companies, putting more sales people into the field and offering countertrade where necessary to win contracts. A greatly enhanced Eximbank, with the guideline of trying to break even or make a small profit, would lead the financing effort.

One of the great trade ironies is that the U.S. Export-Import Bank, founded in 1934, was actually the model for Eximbanks founded in Japan, Taiwan and South Korea and several other countries that are now lending far more aggressively than we are.

When U.S. companies choose to produce in factories located overseas, it is not only to comply with a foreign country's offset request, but to take advantage of the more attractive financing offered through foreign export credit agencies, the equivalent of our Eximbank.

For example, in 1983 Rockwell of Pittsburgh was trying mightily to win an $8 million printing press sale to Zimbabwe. The French competitor Harris had already won the sale because they were backed by a highly concessional aid loan that was basically a grant. The terms of this loan, which could not have been matched easily by an U.S. Eximbank loan, were no down payment, 4% interest and a 20-year repayment term. (I know a lot of people who would like to buy a house with such a loan.) Rockwell tried a desperation measure. They sourced or produced the printing press in the United Kingdom to get the best possible export credit loan. This business was shifted away from America because we had no way to compete, since our Eximbank was so sharply cut back.

One further step was needed. In addition to the ECGD, or British export credit agency, loan, Rockwell offered 100% countertrade or counterpurchase to Zimbabwe. Rockwell thus offered to buy $8 million, 100% of the purchase price, in nickel and ferrochrome from Zimbabwe and took the risk of selling this on the world market. Aggressive trading and financing won the sale for Rockwell after the contract had

already been awarded but not signed with Harris. Such trading and financing are not magic and may not win all the time, but they sure help, especially in combination. The British export credit loan was still not as attractive as the French loan (although more attractive than anything possible from our Eximbank) but when the countertrade was added in, the overall Rockwell package was best.

Eximbank is not foreign aid. It is domestic aid of the best sort. It creates jobs in the U.S., and it helps small and large business alike to build themselves up. And of course it can perform this invaluable mission with the very real potential to make a profit.

EXPANDING THE EXIM CONCEPT TO AID AND THE PENTAGON

The giveaway nature of critical lending programs located elsewhere in the U.S. government could be cut back using the Eximbank concept of lending to break even or make a small profit. In return, the budget allocations for such programs could be raised significantly. I am thinking in particular of AID grants and loans in the State Department and the Foreign Military sales program (FMS) located in the Pentagon (although administered by the State Department) There are a spectrum of loans located in both AID and FMS which could be made on a breakeven or slightly profitable basis. There is of course still a role for highly concessional or grant funds extended to less developed countries, but AID and FMS ought to become far more active if they can do it without impacting the U.S. budget.

As most American businesses know, FMS and AID are critical sources of financing to support U.S. exports. virtually all of the FMS and AID loans have to be spent on U.S. products and are thus critical to small businesses in America seeking to export either directly or as sub-contractors to a major primes who win the sale.

The cutback of FMS has been especially harmful to American sales of defense equipment overseas. In most countries of Europe this slack could be picked up by the export credit agency of that country, such as Hermes in West Germany. However, in the United States our Eximbank is expressly forbidden from supporting military sales to richer countries, and as a matter of policy does not make loans supporting military sales.

I urge Congress to amend Eximbank's charter to allow it to finance military exports, as is done by most of our trading partners in Europe.

I also urge Congress to dramatically increase the budgets of Eximbank, AID and FMS on the understanding that most of these new loans should be made on a break even basis (loans made at the cost of borrowing).

This is needed as part of a major export effort by the United States and would be extremely helpful to small and large businesses alike.

PUTTING ONLY THE SUBSIDY ELEMENT OF EXIM, FMS AND AID IN THE BUDGET

If Exim, FMS and AID can make many loans at a profit, why should this part of their lending authorities even go in the budget at all? We are penalizing ourselves here because obviously great sensitivity has to be shown by Congress when allocating any new budget increase. The way to deal with this issue is to use the good old American profit-making concept.

I urge Congress to put only the subsidy elements of Eximbank, FMS and AID in the budget. Profit-making loans should be kept out and have no impact. This was done for Eximbank from 1971 to 1976, and in this era of budget restraint should be done again, only this time for all government lending agencies. The Credit Reform Act, proposed in 1987 but not enacted, actually takes this approach. I hope this critical tactic will be adopted by Congress as part of our challenge to improve the trade deficit.

The Charter of a trading company could specify that its role is to make a profit and to engage in trading and countertrading beneficial to the United States and to American companies.

Once the trading company was up and running, doing well, it could be spun off and sold to the private sector. The company would have to have quasi government status because successful traders and marketers will expect to be paid performance bonuses substantially in excess of normal government salaries. Small base salaries would have little budget impact. Bonuses would be paid only as a percentage of actual profits realized. The company could report on a dotted line basis to the Commerce Department.

EXIMBANK

The most serious potential objection concerns the possibility that a number of bad loans might be made if Exim lending were substantially increased.

The actual repayment record to Eximbank is excellent. After the freezing of Iranian assets, Eximbank negotiated a settlement on 90% of its Iranian portfolio against assets frozen and held outside the country. In South America, the Brazilians are repaying their rescheduled debt. In Mexico, out of $470 million paid in claims on bad private sector debt, the most troubled area, Eximbank has already collected $180 million and expects substantial additional recovery. This recovery record is really remarkable.

The need for financing and trading or countertrading capability is illustrated by yet another of the many export sales lost because of a lack of U.S. competitiveness in these areas. In 1984 a fierce international competition arose over a $90 million telephone switching contract to Uruguay. Several European and American firms were competing against each other.

Ericsson of Sweden won not only because it had the best financing but the best countertrade as well. The financing was provided by Sweden's export credit agency along with support from Brazil's export credit agency, because Ericsson had skillfully included Brazilian content in the project. The strategy also appealed to South American nationalism as well.

Ericsson also asked the British investment banking firm of Samuel Montague to arrange for a countertrade with Uruguay. Montague proposed to do this by trading $90 million of beef, leather, fish and other products from Uruguay. The trading was done through Surinvest, a joint venture between Montague and Uruguayan partners. In other words, through Montague, Ericsson proposed 100% countertrade or counterpurchase.

FINANCING AND TRADING DISADVANTAGE

Most Americans will find this statement hard to believe but it is true. The U.S. company going into an international export competition will almost always, indeed probably always, have a worse financing package than at least one of its foreign competitors. Our now out-moded free-trade notion that the government ought to stay out of private export sales has caused U.S. exporters, with many small companies among them, to lose hundreds of millions of dollars in sales. True, the government is certainly not needed in all these sales or even most of them. But it is needed in a lot of them. Eximbank rarely competes with private sector banks for loans, and to the contrary is viewed by private banks as a stimulus for lending, since the commercial banks always have at least some part of a loan with Eximbank. Exim, in other words, co-lends with the private banks, who regard Exim's presence in the loan as a greater measure of security. The likelihood of repayment is increased.

Countries like to repay Eximbank loans because that is the only way to assure that new loans will be granted.

As the Uruguayan example illustrated, it is also terribly important to have a strong trading capability as well. What often happens in world trade today is that two or three products are relatively equal or at least will do the job. Their relative prices matter less if one has both the best financing and the best countertrading terms. All across the world, awards are often made not on the basis of price and quality, but on the basis of financing and countertrading incentives offered.

I know this is shocking, but believe me, it is increasingly true, even though a low price and high quality are still helpful.

NEED FOR A NEW FEDERAL VENTURE CAPITAL CORPORATION

I hope the need for this type of operation is self-evident. There is plenty of venture capital in the United States. However, this capital is motivated by pure economics and not necessarily the strategic interests of the United States. Foreign venture capital, speeded by the sharply lower dollar, is pouring into the United States. European and Japanese firms are buying up new technologies at a rapid rate. There is more desirable technology in America than our own venture capital firms can fund. The Pentagon, concerned about this situation, has in some ways turned its DARPA into a high technology venture capital fund.

However, it is quite clear that this concept has to be expanded outside the narrowly defined defense high-tech area. Who can say what important technology might be lost to foreign control? A struggling U.S. firm might have to sell a significant, even a majority interest in itself, in order to get the foreign capital it needs to survive, develop and ultimately thrive.

Many technologies in the area of computers, communications and, in my own area of tooling and die making, would benefit.

I urge Congress to capitalize and create a Federal venture Capital Corporation. The corporation should probably be located in the Commerce Department. The U.S. government could sell its interest in various successful companies to other companies it deems acceptable on security grounds. This type of business could be profitable.

The government could also pick its partners in such venture decisions.

Eximbank, The Federal Trading Company and The Federal Venture Capital Corporation all have this potential to make a profit; actually putting money into the U.S. Treasury.

TAX POLICY TO BENEFIT SMALL BUSINESSES

Over the past several years there have been offered several broad-based taxes which might both generate revenue for deficit reduction and simultaneously improve exports. They are the Business Transfer Tax proposed by Senator Roth, and the combination of the Business Alternative Minimum Tax and the Competition Enhancement and Tax Relief Act introduced by Congressman Schulze. These approaches offer a number of attractive features.

- They raise 68% of the $215 billion in revenues from taxes on imported products, improving the competitiveness of U.S. products domestically. Since it would not apply to U.S. exports, it would make U.S. products more competitive in world markets;
- They would make our tax system more competitive with those of many of our trading partners. The EEC, Korea, Brazil and Mexico use a V.A.T. system, and both Canada and Japan appear moving toward a Value Added Tax;
- They would stimulate savings by discouraging consumption. This in turn would lower interest rates; and
- The significant revenues generated could be put to good use. In addition to additional deficit reduction, they include the reinstatement of capital gains, a 5% ITC targeted to productive investment and the repeal of the alternative minimum tax. In addition, the revenues could be used to fund a more liberal accelerated depreciation for productive equipment and an expanded, broadened and permanent R&D tax credit. The $10 million gross sales small business exemption would assure it does not interfere with job formation, most of which occurs in small businesses in our country.

THE NEED FOR LEADERSHIP AND COHERENT POLICY

Underlying many of our trade problems is a lack of coherent policy and coordination.

(1) Too often the Commerce Department loses important battles in government, especially when it comes up against the State Department, the Pentagon and the U.S. Treasury Department.

(2) To win more often, and thus for the first time to coordinate trade policy fully, Commerce needs more power and more tools than simply the granting of export licenses, one of its current major functions.

(3) Such tools could include control over both a Federal Trading Company and a Federal Venture Capital Company. Yes or no, power over all Federal export loans, to be reviewed for export content, is worth considering as well.

(4) Above all we need to avoid fragmentation, which currently characterizes the situation. Commerce, STR, OMB, State, the Pentagon and a host of other government agencies all compete over trade policy. The result is that we have never had a trade policy in this country but need one badly to survive and thrive in today's trade dominated world.

(5) Some say we should turn the Commerce Department into a MITI in order to compete with the Japanese and Europeans. I disagree. The type of Commerce Department I propose would be far more powerful in a way uniquely and creatively American.

(6) We need a President who cares about trade as a major issue. In most countries, the Trade minister or Oil minister is more important than the Foreign minister. Most countries have the luxury of spending far more government time promoting trade than on negotiating with the Russians on Arms Control. We don't have that luxury, but we could certainly demand that more presidential time be spent on trade.

A TYPICAL CASE

In 1985 U.S. defense contractors lost an aircraft sale to Saudi Arabia because the President failed to get personally involved and because the United States refused to

accept oil barter as a payment for some half of the planes. Included in the package was the construction of airfields in Saudi Arabia as well as radar and other facilities. The package was valued at over $10 billion and was won by British Aerospace.

Prime Minister Thatcher personally lobbied for this sale, and is reported to have called the President so as not to offend him. British Aerospace, with British Government encouragement, gladly accepted oil as payment for a major portion of this lucrative sale.

Once again, the U.S. had lost a major export opportunity, one that would have given sub-contracts to thousands of small businesses all across this great country.

PREPARED STATEMENT OF RICHARD E. HECKERT

Mr. Chairman, I am Richard E. Heckert, Chairman of the Board of Directors of the National Association of Manufacturers. Until late April, I was Chairman and Chief Executive Officer of E.I. du Pont de Nemours and Company. I currently chair the Finance Committee of the Du Pont Board of Directors.

I am pleased to testify here today on behalf of NAM regarding the European Community's internal market program (EC-92). NAM has recently published a major study, *EC-92 and U.S. Industry.* This study covers the major issues for U.S. industry in detail. I would like to submit this report for the record of the hearing, along with my full written statement.

For perspective, it may be helpful to know that NAM's membership covers over 80 percent of this country's manufacturing production and manufactured exports. Members range in size from the largest U.S. industrial firms to over 9,000 smaller manufacturing companies with fewer than 500 employees each. Thus, NAM's views reflect a broad cross-section of U.S. manufacturing interests.

Mr. Chairman, three questions were asked in the invitation to today's hearing. Before addressing them specifically, I would like to give you my overview of the EC-92 process and its implications for U.S. industry.

• *I start from the simple view that a larger, more affluent and more integrated European market has to be a more attractive market for U.S. companies.* This applies to all U.S. companies—those that service customers solely through export, and those that combine exporting to Europe with local production. If EC-92 succeeds in creating a larger and more integrated market, it will give U.S. companies two continent-wide targets of opportunity—our own domestic market and the E.C.—instead of one. That will be good for business.

• *I also do not believe that protectionism is in the long-term interest of the E.C., because their companies and countries are historically more export-oriented and export-dependent than are we in the United States.* This is well recognized within Europe. And there are powerful forces at work in Europe to oppose protectionist solutions to external trade issues that arise under EC-92. The United States should make it clear that we want to work with the E.C. to improve—not reduce—access to each other's markets and to reduce world trade barriers.

I must add that if the E.C. does choose protectionist solutions in certain instances that disadvantage U.S. trade or U.S. producers, then we should retaliate. The E.C. will play the trade game in ways perceived to further their own interests. What would you expect them to do? But it is in the interest of both Europe and the United States to maintain and expand the world trade system.

Both U.S. industry and Congress have important roles to play in shaping our response to EC-92. We must both carefully follow the development of EC-92 programs and respond to actions that adversely affect our trade relations. But I think we also should be careful not to engage in overly harsh rhetoric and not to pursue policies that block reasonable accommodations. Congress in last year's trade bill has given the Executive Branch the tools it needs to protect U.S. trade interests and open markets. A good example of this is the telecommunications provision in last year's trade act—a provision which NAM supported. This provision is already being used to gain improved access to the E.C. telecommunications market. In short, Mr. Chairman, to paraphrase that well-known European, Oliver Cromwell, "Put our trust in the E.C., but keep our powder dry."

• *We should remember that access to the E.C. market as it exists today is not ideal—and that substantial gains are possible for U.S. industry if E.C. market barriers are reduced or eliminated.* Not only are there imperfections within the European "common market" that is supposed to have been in existence over thirty years, but there are over a thousand national quotas, trade restraint agreements and other restrictive measures within the E.C. that affect external trade. At the very least, we believe that the overall situation will not get worse under EC-92. And at best we

see substantial gains—for internal E.C. growth and for growth in world trade as a whole.

This, Mr. Chairman, is my general overview of EC-92 and the U.S. response. In the remainder of this statement, I want to focus on the three questions that were asked in the notice of this hearing. I also want to comment briefly on some of the major specific trade issues that are mentioned in the NAM report.

EC-92: FORTRESS EUROPE?

First, will EC-92 lead to "Fortress Europe" and another defeat for American trading interests by locking U.S. products out of lucrative European markets? As I already indicated, I do not accept that argument. Trade is very important to the Europeans. It is clearly in Europe's best interest to keep its borders open as a quid pro quo for access to other world markets.

My personal belief is that our concerns about EC-92 are overblown and could prove counterproductive. U.S. firms that export to Europe or operate there should accept that major and perhaps irreversible changes are taking place in that market. We should focus on being as competitive as possible so we can share in the benefits a truly integrated market could yield. At the same time, we must be attentive and react quickly to any developments that are negative for U.S. interests.

My own company--Du Pont—has been doing business in Europe for many years. Last year our European sales were $9.5 billion, representing over 30 percent of our total sales worldwide. We have a strong presence in Europe with manufacturing, marketing, R&D and technical organizations structured to serve the regional market, as well as global markets.

As citizens of Europe, we are excited about the elimination or reduction of physical, technical and fiscal barriers to increased trade within the Community. We believe that reducing these barriers and associated costs will increase growth throughout the European Community. In other words, it's good economic policy.

Some economists have questioned the expectations for EC-92. The European Commission's own report concedes there will be some initial loss of economic growth, due to industrial restructuring as EC-92 takes effect. But the Commission believes that by the mid-1990s, the total E.C. gross domestic product will be 5 percent higher than it would have been without the EC-92 package.

Our view is that the benefits from EC-92 will come quickly. Companies are already increasing efficiencies and searching for new partners both from within and outside Europe. As the business community becomes more convinced that EC-92 is going to happen, it is making decisions and improving productivity in critical product lines to anticipate the increased competitive environment. This is the key opportunity for U.S. companies, especially those with a competitive edge in innovative products and materials. E.C. companies are looking for partners and sources of supply that can improve efficiencies now. They are not waiting until they see how the EC-92 program pans out over the long run.

But what about U.S. companies that today primarily serve the E.C. market through exports? U.S. exporters have much to gain from EC-92. As the NAM report shows, the three-year fall in the dollar after 1985 has tremendously boosted U.S. exports to Europe—9 percent in 1986, 14 percent in 1987 and 25 percent last year. This enabled the U.S. to cut its trade deficit with Europe in half in 1988. In early 1989, we have actually run a surplus with the E.C. Yet, there have been no serious adverse consequences overall for European growth. We are now seeing the strongest across-the-board growth in Europe that we have seen for 15 years. This is truly a case of the rising tide lifting all the boats.

Moreover, maintaining and improving the world competitive positions of E.C. companies is a stated goal of EC-92. They are going to need access to advanced and competitively priced technologies and products from U.S. companies, as well as European companies. Our strongest trade surpluses are in capital goods and in technologically advanced industrial materials such as chemicals. For this reason, the E.C. is unlikely to want to keep out competitive and innovative U.S. goods.

EC-92 AND THE GATT ROUND

The second major question asked of witnesses at this hearing is, will EC-92 harm the current world trade negotiation? I believe that it will not.

In every announcement on EC-92, the European Commission has said that it will honor present international trade obligations. Where they are opening up their market beyond present E.C. or GATT rules, they have said that they are willing to discuss access for non-E.C. trade partners.

Let's put them to the test. They say, in areas like banking and public procurement, that they are willing to allow non-E.C. countries access on the basis of genuine and effective national treatment. They have also said they are willing to discuss this on a bilateral basis, or multilaterally in the GATT. They have made similar statements about product testing and certification.

The recent U.S. trade law gives the U.S. government plenty of latitude to negotiate in these areas:

—In the current GATT Round;
—In the already existing GATT Codes on non-tariff barriers;
—And in direct negotiations with trade partners to remove barriers.

We should be pursuing our trade policy objectives in all these forums.

U.S. CONCERNS ABOUT OBJECTIONABLE FEATURES OF EC-92

Thirdly, the Committee has asked whether we are prepared to speak out forcefully where there are problems or issues with details of EC-92 proposals. I think the NAM report, which details concerns with specific proposals, provides an answer to that question from U.S. industry's point of view.

While I have already indicated that EC-92 represents a major opportunity for U.S. industry, specific proposals still on the drawing board could create problems for U.S. industry as they are further developed and implemented. Creating and maintaining opportunities for U.S. companies as exporters and investors will not come easily or without some controversy. There are many decisions on specific issues that can enhance or reduce our ability to trade with the E.C.

Let me cite a few examples of issues from the list in the NAM report that we will be watching closely.

Technical and environmental standards. The harmonization of technical standards is widely seen by U.S. companies as a major benefit—a product made or sold in one E.C. member state could be sold in all of them. But there are serious concerns regarding adequate and timely access to the standards-setting process as well as to testing and certification procedures. This is the top concern of the largest number of NAM members.

NAM has communicated its views on these matters to the Commerce Department and to Congress. E.C. standards bodies are already taking steps to improve the timeliness and availability of information on standards projects. We also hope that discussions will soon begin regarding mutual recognition of testing and certification procedures—between the U.S. government and the European Commission where appropriate, and between U.S. and E.C.-wide private standards bodies as well.

Reciprocity. Much of the concern about "Fortress Europe" stems from the European Commission's controversial strategy for dealing with trade issues. The Commission has announced that it reserves the right to make access to the benefits of 1992 for non-member country firms conditional upon a guarantee of similar opportunities in those firms' own countries.

The October 1988 E.C. statement redefining reciprocity has alleviated some U.S. industry concerns. This statement has been followed by important changes in the Second Banking Directive which indicate further modification in the E.C. policy on reciprocity.

The European Commission has confirmed that U.S. companies with investments in Europe will continue to be treated as E.C. citizens under Article 58 of the Treaty of Rome. It has also clarified that the E.C. does not expect "mirror image" treatment in foreign markets but only treatment that is non-discriminatory as compared with local companies. In revising the Second Banking Directive last month, the European Commission has further declared that it will adhere to a national treatment standard as the basis of reciprocity in this case. While we still have concerns with the E.C. reciprocity approach, we hope that national treatment will be the basis of reciprocity in all areas where it is applied by the E.C.

Rules of Origin, Local Content and E.C.-wide Quotas. Completion of the internal market will result in the transfer of much authority over trade policy from the member states to the Commission. This includes the possible replacement of national trade quotas and restrictions with E.C.-wide measures. Quotas and trade restrictions exist today within Europe at the national level in many products. The E.C. intends to replace these with E.C.-wide quotas or other trade measures. Such measures should be consistent with GATT obligations, which would insure protection of U.S. interest under the GATT and consultation with the E.C.'s trade partners.

Moreover, the E.C. is continuing to develop rules of origin and local content rules for the application of specific antidumping penalties. NAM members are seriously concerned that the evolution of such policies, for example in the semiconductor in-

dustry, could lead to development of general local content rules. Such rules have previously been opposed by both the United States and the European Community in the present GATT negotiations.

NAM will be closely following future policy developments in these areas and the others listed in the report. We will keep this Committee informed about our views and concerns.

Mr. Chairman, this concludes my testimony. I would be pleased to answer questions.

Enclosure.

EC-92 AND U.S. INDUSTRY EXECUTIVE SUMMARY

The plan to complete the opening of European Community internal market by 1992. known in shorthand as EC-92, promises to have major effects on U.S. industry. The overall view of U.S. industry is strongly positive. NAM members emphasize the positive impact of strong and dynamic growth, in an increasingly deregulated market.

This report aims to provide guidance for NAM members on the changing European business environment. It focuses on the specific issues and proposals related to EC-92 that have been identified as being of most concern to U.S. industry, rather than the overall history, politics and economics of the E.C. internal market program. The report is based on extensive consultations by the author with NAM member firms in the United States and Europe, cooperating business associations, and information provided by representatives of the U.S. government, staff of the European Commission in Brussels and officials of E.C. member-state governments and private trade associations.

This report is divided into two parts:

Part I: Evolution of EC-92 and U.S. Industry is an overview of both the interests of U.S. industry in EC-92 and the development of the EC-92 program. The major subjects of this part of the report are as follows.

What Is at Stake for U.S. Industry?

As indicated in NAM's recent comprehensive trade report, the E.C. may be the strongest and most important market from the perspective of increasing U.S. exports. The fall in the dollar, improved E.C. growth rates and the relatively open E.C. market has led directly to a three-year boost in the level of U.S. exports. The 1988 level was $27 billion higher than in 1985. This has also meant reducing our trade deficit with the E.C. from $24 billion to $12 billion. accounting for over a third of the total $33 billion improvement in the U.S. trade deficit in 1988. Moreover, the E.C. is far and away the most important host for U.S. manufacturing investment abroad—at $65 billion, more than half the worldwide total.

The E.C. Internal Market Program

The basic thrust of EC-92 is to *complete* the internal market established as a European objective by the Treaty of Rome over 30 years ago. As laid out in the E.C.'s 1985 "white paper," this involves the pragmatic elimination of three major types of barriers.

—*Physical barriers* at the borders to the free flow of goods and persons;
—*Technical barriers* that prevent goods produced or traded in one member state from being sold in others;
—*Fiscal barriers* much as the red tape. delays and costs of different national tax systems which prevent cross-border trade.

Also associated with the elimination of these barriers are major initiatives in related areas, including competition policy, encouragement of research and development. establishment of coordinated monetary policies with possible monetary union, and decisions on common social policies.

Prospects for Completing EC-92 and the Process of Adopting EC-92 Policies

The first part of the report reviews the major issues involved in the completion of the ambitious EC-92 program. It notes that whatever the outcome of these politically sensitive questions, which could prevent the goals of the 1985 White Paper from being fully achieved, many directives and policies related to 1992 will go into effect as they are approved by the E.C. The reappointment of President Jacques Delors for a second term as President of the European Commission, beginning in January 1989, indicates the strong commitment of E.C. member states to achievement of the internal market goal. During the term of the new commission, which ends on De-

cember 31, 1992, the conditions for U.S. companies of doing business in the E.C. will be changed in a major and irrevocable way.

The first part of the paper concludes with an analysis of how EC-92 policies are developed and adopted within the E.C. institutional framework. It also summarizes the ways in which U.S. companies can seek access to provide and receive information on how the process may affect their interests.

Part II: Major Issues for U.S. Companies in EC-92 reviews the major issues that could either enhance or reduce the opportunities for U.S. companies as investors in or exporters to the E.C. These major issues represent the subsections of Part II of the report. Within each subsection, the report analyzes the principal relevant proposals of the EC-92 program that have been adopted or considered to date.

(1) *Technical and Environmental Standards*—The harmonization of technical standards, a major part of EC-92, can have a major impact on current and future access of goods produced by U.S. companies for the E.C. market. The expedited adoption of common E.C. standards is widely seen by U.S. companies as a major benefit. However. there are serious concerns regarding timely and adequate access to standards information through the voluntary E.C. "CEN/CENELEC" standards-setting process. Also. U.S. companies have concerns regarding the implementation of E.C. certification and testing recognition procedures.

(2) *Public Procurement*—The enhancement of existing E.C. rules on the opening of member government procurement and the extension of E.C. rules to the sectors presently excluded from GATT or E.C. discipline are designed to increase dramatically cross-border procurement within the E.C. The new rules, at least in the previously excluded sectors, will not necessarily apply to non-E.C. source products. But the E.C. has indicated a willingness to consider open access on a reciprocal basis, either bilaterally or multilaterally.

NAM members have indicated concern with the new local content rules included in the proposals regarding procurement in the presently excluded sectors, but are encouraged by the principle of opening these markets within the E.C. and the commitment to negotiating opening of these sectors to other signatories of the GATT procurement code.

(3) *Reciprocity*—The controversial stated E.C. policy of extending intra-E.C. market opening initiatives to non-E.C. producers only insofar as E.C. trading partners provide equivalent access to their markets for E.C. producers has led to great public concern with the emergence of a "Fortress Europe" in world trade. The October 1988 Commission statement on the definition of reciprocity has alleviated some U.S. industry concerns regarding this subject.

(4) *Sectoral Trade Issues*—This report particularly focuses on the future development of E.C.-wide common commercial policies and other sectoral initiatives regarding automobiles, telecommunications and information technology, because of the broader implications of policies in these areas.

(5) *Rules of Origin and Local Content*—U.S. industry is strongly concerned with the development of E.C. rules that determine whether goods are of E.C. origin, not only for the application of specific trade benefits or penalties, but also on a more general basis regarding the treatment and access of foreign companies or producers in the E.C. market.

(6) *Intellectual Property*—Enhancement and completion of a Europe-wide system of protection of trademarks, patents and copyrights is a process that predates EC-92. But it has been stimulated by plans to create a more integrated market. Generally, U.S. companies are supportive of proposals to allow registration in one member country to be valid for the whole Community, as well as to broaden the products that are covered by E.C.-wide copyright rules. There are concerns, however, with some proposed reform procedures.

(7) *Social Dimension*—The increase in unemployment in the E.C. between the early 1970s and the 1980s has been a major stimulus for the acceptance of the EC-92 program. The "social dimension" of EC-92 includes new initiatives in employment and social affairs related to the creation of a more integrated E.C. market. Both U.S. companies and E.C. industry generally have been supportive of proposals aimed at establishing E.C.-wide safety standards, reducing regional disparities, improving worker training and enhancing labor mobility. Concerns have been expressed over other initiatives, that would have the effect of establishing more rigid E.C.-wide industrial relations policies and practices.

(8) *Competition Policy*—Establishment of E.C.-level control over mergers and acquisitions, particularly large-scale multinational combinations, is seen by U.S. companies as potentially providing an expedited means of increasing E.C.-wide competition, while producing substantial gains for the E.C. through improved economies of scale.

(9) *Monetary Policy*—The E.C. has already agreed on the elimination of all controls on capital movements within the E.C. Currently under consideration are the establishment of mandatory coordination of monetary policies and possible creation of a single E.C. central bank and currency. These policies not only enhance the ability of U.S. companies to operate within the E.C. framework, but may also have a major impact on the E.C.'s international competitive status.

(10) *Potential Issues*—The report concludes by noting two other issues not now included in the EC–92 program, but which may have a major effect on U.S. companies when they are considered by the E.C. in the future. These are future rules regarding the opening of defense procurement within the E.C. and the adoption of common E.C.-wide export control policies.

[Committee Note: The full text of the NAM report was made part of the committee files.]

PREPARED STATEMENT OF CARLA A. HILLS

I am pleased to appear before this Committee today to discuss the revolutionary changes occurring in the European Community as it moves to complete it's internal market by the end of 1992. The EC 1992 program is an important development on the world economic scene—important for the Europeans and important for us. I know that many of you on this Committee have recently visited Brussels and other European cities and I'm sure that you share my assessment of the significance of EC 1992 for the United States.

Mr. Chairman, no other market is as important for American exporters or our investors as is the market of the European Community—not Canada, not Japan, not the newly industrialized countries of the Pacific. The market in the EC, when the individual country markets of the Community are combined—and that is the goal of the 1992 program—will be the largest industrialized market in the world. It is critically important for us that this $4 trillion market remains open to its trading partners and growing through the implementation of policies which promote, not frustrate, competitive forces.

The European Community and the United States exchanged over $160 billion in goods last year. Our trade position with the EC over the past two years has improved dramatically—from an annual deficit of $21 billion in 1986 to a $345 million surplus in January. U.S. firms' direct book investment position in the EC—already in excess of $130 billion—is growing rapidly as U.S. firms seek to position themselves to take advantage of new opportunities in the EC.

The context of the "EC 1992" initiative is industrial policy, accompanied by massive deregulation, on a continental scale. The "internal market" program is motivated not by bureaucratic zeal or Community officials' desire to create a United States of Europe; rather, it's motivated by European industrialists' perception that they need a single barrier-free home market in order to compete with the Japanese and, to a lesser extent, the Americans, in world markets.

This is an important point because companies and individuals that believe in the goal of international competitiveness do not—and almost by definition cannot—have as their interim objective a "Fortress Europe" that precludes non-European competition in the marketplace.

The 279 directive contained in the 1985 White Paper's are generally intended to foster competition in European markets. In the telecommunications sector, for example, the EC 1992 objective is to break the stranglehold on competition and public procurement now exerted by national PTT's. Competition in this sector is deemed important by the Europeans not only for the sake of suppliers of telecom equipment but also for the users of telecom services, who today are burdened by high-cost and inefficient telecommunications services. Real cross-border competition in financial services—with lower costs for the users of these services—will also affect users' competitiveness.

On April 28, I spent nearly an hour discussing a range of EC 1992 issues with EC Commissioner Sir Leon Brittan. He clearly stated his desire to make effective use of competition policy instruments in bringing about a European industry that is genuinely efficient and competitive in world markets. The need to avoid policies which discriminate against foreign nationals in this process is seen by Sir Leon and others as key to the program's success.

It is becoming less and less likely that the Community's initiative will fail halfway through—and this is good news. Even though there are some very difficult issues which remain, the momentum is strong and the progress to date is impres-

sive: 132 of 279 measures envisioned by the program have already been enacted and some 100 others have been drafted. If you have to bet whether they're going to make the 1992 deadline, bet they will.

American companies in nearly all goods and services-producing sectors stand to benefit from the EC 1992 initiative. Many of them are even better positioned to take advantage of 1992's opportunities than their European-based competitors. It is not only larger U.S. multinational companies with investments in Europe which stand to benefit, but also many smaller exporters that will realize the competitive benefits of lower costs and reduced, simplified regulation.

For all of these reasons, my office, and the interagency Administration network which we coordinate, have concluded that the EC 1992 program is in the U.S. interest and therefore something we should support. Our "global support" for 1992 is conditional and our view of "EC 1992" is colored by a framework of basic principles:

- American and third country firms must be permitted to enjoy the same business opportunities as EC companies in the "single market";
- "EC 1992" should reduce the level of protectionism in the EC and not substitute Community-wide restrictions for existing national restrictions (in areas such as automobiles)
- 1992 must contribute to multilateral liberalization by conforming to GATT principles as well as to new agreements reached in the Uruguay Round;
- Where multiple levels of guarantees governing the treatment of non-EC business now exist in individual Member States, and where the Commission is seeking to harmonize these divergent guarantees, harmonization should be at the most liberal, as opposed to most restrictive, level.
- The Community's internal market completion program needs to be carried out in a transparent fashion which permits an accommodation of foreign interests.

I said earlier that EC 1992 would bring revolutionary changes to our bilateral relationship, but it is also an evolutionary program as well and one where our perceptions change over time. As an example, our concerns in connection with the Second Banking Coordination Directive's "reciprocity" provision have abated somewhat with the redraft of that provision, while over the same period, our worry over the broadcasting directive's local content rule has grown significantly. Clearly, EC 1992 will be with us for some time and will continue to require active and ongoing monitoring and problem-solving activity on our part.

Let me turn now to a brief status report on where things stand on a number of key "EC 1992" issues.

RECIPROCITY AND NATIONAL TREATMENT

We continue to believe that unconditional national treatment should be the standard applied to foreign-owned banks. The Community's redrafted reciprocity language in the Second Banking Coordination Directive unfortunately does not go far enough in this regard. Setting aside the question of the unconditional national treatment principle, the practical implications of the EC's redraft is that U.S.-owned banks will not be discriminated against in their attempts to gain authorization to operate in the Community market. As I explained in my recent meeting with EC Commissioner Brittan, who has responsibility in this area, we continue to be concerned over how the EC may choose to implement this directive, particularly with respect to the conditions under which the Commission might propose market opening negotiations with other countries. But we recognize that the redraft represents a substantial effort to address our earlier-expressed concerns.

RESIDUAL QUANTITATIVE RESTRICTIONS

Assuming that the EC is successful in eliminating border controls between Member States, it will become physically impossible for these individual countries to enforce restrictions on imports into their markets (as many of them have done despite their entry into the Community). In some cases, rather than allowing these restrictions to fade away, European industry has begun to call for the translation of national protective measures in sectors such as autos into EC-wide measures. With over 1,000 product categories subject to such restrictions, there is a fear that major new, GATT-inconsistent trade barriers might be introduced by Brussels as a result of 1992.

Things are looking up, however, on this front. Recently, Martin Bangemann, the EC's Commissioner for the Internal Market, came out strongly against new protective measures in the autos sector. Given that five of the Member States currently restrict the importation of autos from Japan, it may be difficult for Bangemann to carry the day on this, but it seems clear that the Commission at least is no longer

siding with those who aim to make "1992" an excuse for increased Community protectionism. I might add that this was not the view taken by former EC External Affairs Commissioner Willy de Clercq with respect to autos.

Our position is that the "1992" package cannot be the excuse for new external trade barriers, and we have repeatedly made known our intention to challenge any new barriers in the GATT should they be introduced by the Community.

STANDARDS, TESTING AND CERTIFICATION

The importance of the EC's initiatives in the standards, testing and certification areas might be demonstrated in part by the two interagency working groups we have established to pursue the protection of American interests in "EC 1992". The Community's "new approach" to product standards—relying heavily on the principle of mutual recognition among Member States of the validity of national laws and regulations greatly simplifies access to the market.

However, where the Community's "essential requirements" to ensure the health and safety of products must be translated into a new EC standard, the unwillingness of regional standardizing bodies to admit of foreign participation in their activities gives us real cause for concern. Similarly, revised testing and certification approaches in the EC will necessitate detailed and time-consuming negotiations to establish a framework that will ensure that there is no negative impact on transatlantic trade arising out of these EC initiatives. Secretary Mosbacher's upcoming visit to Brussels will focus importantly on these areas.

RULES OF ORIGIN AND LOCAL CONTENT ISSUES

The rules of origin/local content area is extremely complex from a technical side and, partially as a result of this complexity, is often misunderstood in the "EC 1992" context.

Recently, we have taken the initiative with the EC on the need for us to work together—ideally with the Japanese and others in the Uruguay Round context—to develop a common approach to determining the origin of goods traded internationally. Only by arriving at such a common standard will we be able effectively to debate issues such as those raised by the Community's recently proposed regulation on photocopiers. Negotiating a multilateral understanding on origin rules is a necessary and useful exercise. Origin rules in and of themselves are generally not a problem in international trade. It is the uses to which they can be put, particularly in conjunction with so-called local content questions, that can create major difficulties for exporters.

Actually, there are no EC "local content" requirements in force today for goods. There is evidence, however, that the EC's anticircumvention measures in the antidumping area may have been interpreted so as to suggest that American content in Japanese goods under investigation must be replaced by EC content in order to avoid the imposition of antidumping duties. This is not what the EC regulation says and such a practice would be in clear contravention of the GATT and the Antidumping Code. We are working very hard to try to clarify this situation and end the confusion surrounding this alleged "local content" issue.

The only other area where "local content" seems to play a role in the Community today is in connection with firms voluntarily offering to meet locally-established local content requirements in exchange for receiving a subsidy or other tangible benefit. Such local content requirements are not sanctioned by the EC Commission and under certain circumstances are subject to legal challenge in the Community. Local content requirements applied by the British Government to the Nissan operation in the United Kingdom fall into this category. As an aside, it should be noted that, recent French statements notwithstanding, an automobile's "EC-origin" is determined through the use of the so-called "substantial transformation" rule and not through a measure of its "EC content". In the GATT Uruguay Round negotiations, the Community has indicated that it clearly shares our view that local content requirements are inconsistent with the GATT.

But what I have just said about local content requirements for trade in goods does not, unfortunately, hold for trade in services. In April the EC Council of Ministers reached what is called a "common position" on a proposed directive addressed to television broadcasting across EC frontiers. This directive is blatantly protectionist and prejudicial to our interests: it would require member states to reserve "where practicable and by appropriate means" a "majority proportion" of their TV transmission time for European works. This directive, if finalized, promises to discriminate against our industry. We in the Administration do not intend to let this matter

pass without a major effort aimed at removing the discriminatory local content requirement.

PROCUREMENT IN THE "EXCLUDED SECTORS"

The Community's drive to end the stranglehold on competition now exercised by the Member States in the so-called "excluded sectors" of telecommunications, energy, transportation and water provision is a critically important aspect of the "EC 1992" program. This effort has important implications for our bilateral telecommunications negotiations and for our more general effort to expand the coverage of the government procurement code in Geneva.

It is quite true that Commission officials with procurement responsibility are not opening the market for non-EC-origin products. Under the proposed measures, there is a preference margin granted to EC-origin goods, much like our own "Buy America" procurement preferences; however, the Community has plainly stated that it is prepared to exchange the "EC-origin" for "Signatory-origin" through negotiations pursued in Geneva. We have the opportunity to achieve a breakthrough in this important area.

"EC 1992" AND THE URUGUAY ROUND

"EC 1992" is not only having an impact on our government procurement negotiations, it is also affecting the overall Uruguay Round negotiations in a way that I would not have foreseen 12 months ago.

First, timing: There is no reason to believe that EC 1992 will make it difficult for us to successfully conclude the Uruguay Round negotiations on schedule at the end of 1990. With the Commission's progress made to date, and consistent with its own timetable, it should be possible to complete action on most of the "1992" legislative package at the Community level in 1990. Moreover, the EC has never suggested that it might require more time to complete the Geneva negotiations as a result of its possible preoccupation with the internal market.

Next, substance: "EC 1992" initiatives have frequently helped to advance the cause of the negotiations in Geneva. The Uruguay Round negotiations have positively influenced the EC in certain areas of "1992" activity. For example:

—Regarding protection of intellectual property rights, the Community position at the start of the Round was that it was willing to negotiate measures against trade in counterfeit goods but no more. Now the Community, in large part due to the 1992 intellectual property rights agenda, is willing to negotiate in Geneva on a much broader range of IPR protections.

—In the services negotiations, we believe that the emphasis in the Uruguay Round negotiations on national treatment has been helpful in restraining the Community from its earlier protective reciprocity approach in the banking directive.

—In the Round's standstill/rollback exercise, the Community has already tabled its willingness to eliminate a number of residual quantitative restrictions maintained by the member states in contravention of the GATT.

—In negotiations regarding the Standards Code's effectiveness, the EC's internal standards and testing/certification approach has enabled it to be more forthcoming in similar areas under negotiation in Geneva.

And there are other complementary areas between the two exercises. Over the past year, we have made our coordination of Uruguay Round 1992 issues more explicit, and we will increase this coordination between now and the end of the Round.

CURRENT ADMINISTRATION ACTIVITIES ON 1992

"EC 1992" has and will continue to occupy a central place in this Administration's international economic policymaking. This is only right. As I indicated in the beginning of these remarks, there is no other market in the world which approaches the importance for the United States of the European Community.

At the interagency working level, a sixteen-month-old task force on the EC internal market has been expanded to include representatives of agencies which had not previously been represented, such as the Small Business Administration. SBA's participation will enhance our ability to work with small and medium size exporters and investors in addition to the larger companies with which we interact on a regular basis. Our task force now has twenty different agencies and departments represented in its coordination sessions and its eleven working groups address—in a concentrated way—subjects as diverse as product certification and testing and television broadcasting restrictions.

We are working closely with a range of private sector groups to identify challenges to U.S. firms arising out of the program and the major areas of opportunity for the U.S. business community. In addition, the Advisory Committee on Trade Policy and Negotiations (ACTPN) task force on 1992, ably chaired by Larry Bossidy of the General Electric Corporation, is developing advice for the Administration on the role that the Government should play. We are looking forward to receiving the ACTPN report by June.

Finally, let me say that the Administration is devoting time and resources to the goal of informing the public in this country about "EC 1992". The Department of Commerce has been extremely active in private sector outreach programs, ranging from the operation of an information service to field office seminars to publications assessing the impact of EC directives on the business community. Other agencies have also contributed importantly to the public awareness objective.

To sum up, the outcome of "EC 1992" will have major implications for the way in which we conduct our business in the EC, for the economic health of the Community and our nation. We do not share all of "EC 1992's" objectives: we differ in our views of broadcasting restrictions; the degree of foreign participation which should be encouraged in standards development; and whether national treatment in financial services should be conditional. We will continue to have our differences with the Community. But where we have identified concerns and made them known to the EC to date, the Commission and its member states have generally been willing to accommodate our concerns. My colleagues and I have established a good working relationship with our counterparts in the new Commission and it is our hope that we will continue to be successful in gaining the Community's cooperation in this area.

RESPONSES TO QUESTIONS SUBMITTED BY SENATOR ROCKEFELLER

Question. Japan, obviously, has as much of an interest as do we in assuring that EC 92 will not result in the creation of new barriers in Europe. Are we systematically monitoring Japanese efforts to prevent the construction of new barriers through the EC directives? Also, are we watching closely how Japanese industry is changing its methods of operation in Europe to deal with 1992? Do we have anyone in our Embassy in Tokyo tasked with this? Anyone in our mission in Brussels?

Answer. Over the past year, U.S. and Japanese officials have consulted on EC 1992 issues on a number of occasions. When the U.S. and Japan have met formally in bilateral sessions, EC 1992 has typically featured on the agenda. We also meet informally in Washington, Brussels and Tokyo and there is a fairly regular dialogue between

Japanese Embassy officials here in Washington and USTR officials. One of the subsidiary working groups established in our interagency task force on 1992 is addressed to relations with third countries and is tasked with coordinating our approach on 1992 with the Japanese, Canadians and others. Japanese industry, whether out of fear or out of a sense of new opportunities, is reacting to EC 1992 with massive new investment in plant and equipment in the EC market. This "buying in" approach is consistent with the "globalized localization" strategy being pursued by Japanese industry worldwide. Despite massive capital flows of the past two years, Japanese industry today does not begin to approach the investment position of U.S. industry in the EC market.

There is no one individual to whom one could point in either our Mission in Brussels or our Embassy in Tokyo that would be charged with EC 1992 coordination with Japan; however, all of the officers in our economic sections at these posts would be expected to be prepared to have such a discussion with their Japanese Government counterparts.

Question. As you both know, I have been particularly concerned about the problems American companies have with the Japanese patent system. These problems are being dealt with in a number of fora at the bilateral, multilateral and international levels, and the activities in all these groups are interrelated in a complex web. One forum, which we call the "Trilateral" and the Europeans call the "club of 15", consists of the Japanese Patent Office, the U.S. Patent and Trade mark Office, and the European Patent Office with its 13 member countries. My question is: How will Europe 1992 impact the operations of the European Patent Office, if at all? I recognize this is a bit technical, so I don't expect an answer today. But I would appreciate your following up on this question in writing.

Answer. Membership in the European Patent Office (EPO) is not limited to the Member States of the European Community. Among others, Sweden, Austria and

Switzerland belong to the EPO. The EC is now working on a Community Patent Convention which would permit an applicant to receive a patent good in all the EC Member States, without having to apply to each national authority. But this convention would not change any of the procedures or the operation of the EPO. We are not aware at this time of any EC activity connected with 1992 which would have a direct impact on the EPO.

RESPONSES TO QUESTIONS SUBMITTED BY SENATOR RIEGLE

Question. The EC reportedly may abandon an earlier proposal to require reciprocity in banking market access. It now apparently intends to deny licenses only to banks from countries which fail to provide national treatment and effective market access to EC financial institutions. It also reportedly intends to seek negotiations with countries whose banking laws are determined to be less liberal than the EC's.

How do you expect U.S. financial institutions to be treated under this modified banking directive, if it is adopted?

Answer. Because the United States does not treat EC banks established in the United States less favorably than U.S.-owned banks, I expect that U.S. financial institutions which are—or become established in the EC market will enjoy commercial opportunities equivalent to those provided to EC-owned institutions under EC law and regulation.

Question. Do you expect that the EC will target the U.S. for negotiations?

Answer. It is difficult to foresee the extent to which the EC financial services market in 1993 will be perceived as more liberal than the U.S. financial services market at that time and how this perception might influence the Commission in its consideration of whether to propose negotiations aimed at liberalizing the American market. In recent discussions I have had with EC Commissioners Brittan and Andriessen, both were non-committal when asked whether the U.S. might be targeted for negotiations.

Question. Will the EC's switch to the more liberal standard of "national treatment" extend to insurance and investment services as well as banking?

Answer. The "Second Banking Coordination Directive" has long been regarded as the "flagship" of financial services directives to which the EC has attached "reciprocity" provisions. It is our understanding that, provided that it survives the EC legislative process, the more liberal formulation now found in the banking directive would also be substituted for existing language in the insurance and investment services directives.

RESPONSES TO QUESTIONS SUBMITTED BY SENATOR HEINZ

Memorandum for: Senator John Heinz
From: Carla A. Hills
Subject: The "Diffusion" Rule of Origin for Integrated Circuits in the European Community (EC)

At Wednesday's Senate Finance Committee hearing on "EC 1992" issues, you asked me about the position being taken by the Administration in connection with the EC's recent decision to the effect that the origin of an integrated circuit would be determined in accordance with the location of the plant where it undergoes the "diffusion" process. I responded that we are concerned over the general origin rules question with the EC and, more particularly, with the implications of the "diffusion" rule in conjunction with actual or alleged local content requirements.

The Rule of Origin Issue

Currently, there is no standard for determining origin which is agreed between the United States and the EC. This severely hampers our ability to complain in the event the EC arrives at an origin determination with which we wish to take issue. The Ricoh photocopiers case is a recent example of the problems which can arise out of ways in which a good's origin is determined.

In order to address the need to preclude pernicious origin rule determinations in the future, we have made negotiations on the origin rules issue a priority of ours in the Uruguay Round and have asked for consultations with the EC on the general issue.

The "Diffusion" Rule for Integrated Circuits

In general, there are three practical approaches for determining the origin of a good: "substantial transformation", "value-added" and "change in tariff heading".

The general rule in use in the EC is the "substantial transformation" rule, which is also the rule used for general customs purposes in the United States. For the purposes of our Free Trade Agreement with Canada, however, we employ the "change in tariff heading" rule.

In arriving at the "diffusion" rule, the EC decided that the "substantial transformation" from parts to the final product in integrated circuit manufacture occurred with the "diffusion" process and not with the final assembly as had earlier been the test. As a result of this decision, companies with assembly operations in Europe (but no "diffusion" capability) will no longer be considered to be producing EC-origin chips.

As an aside, you might be interested to know that the change in tariff heading approach which we use with the Canadians for FTA purposes effectively implements the same "diffusion" rule for integrated circuits in the U.S. and Canada because it is the "diffusion" process which changes the tariff heading for the product.

We have been approached by several U.S. manufacturers of integrated circuits and the American Electronics Association (AEA) about the diffusion rule and the more general problem. We understand the importance of this issue and as a result of these industry contacts, we have initiated our intensified dialogue with the EC.

However, the "diffusion" rule itself is not the trade problem here and the AEA—which supports negotiations aimed at developing consensus around the change in tariff heading approach—recognizes that the tariff heading approach yields the same result. The problem is the use to which these rules are actually or allegedly applied: local content.

Where is local content a problem?

Antidumping.—There has been some confusion over whether or not Japanese firms under anticircumvention (antidumping) investigations in the EC can only avoid the imposition of the dumping duties by replacing foreign content with EC "local content". The EC has assured us that this is not the case, and the EC regulation specifies only that a proportion of the good must be from sources other than the "dumper" (generally Japan) Nowhere does the EC regulation specify local EC content, and such an application of the law would clearly contravene the GATT.

Nevertheless, the Japanese companies involved in anticircumvention cases have begun to replace U.S. integrated circuits with EC integrated circuits. Furthermore, U.S. producers have become convinced they will have to perform diffusion in the EC if they are to continue to sell their products there. This strongly suggests that there are incentives for increasing the EC local content in items subject to the EC's anticircumvention measures.

We are attempting to get to the bottom of this issue. If EC officials are acting outside the scope of the EC antidumping regulations, we will take action to end their manipulation of the procedures. If the Japanese companies are not acting to replace U.S. integrated circuits at the EC's behest, then we want to know why they are behaving in this fashion.

Discriminatory Quantitative Restrictions.—The Community and its Member States do not impose discriminatory quantitative restrictions on the importation of U.S.-origin electronic products containing integrated circuits (although such restrictions are formally and informally maintained against Japan and other suppliers). As a result, the application of the "diffusion" rule might further disadvantage Japanese integrated circuit producers in this context, but it has no practical significance for American producers.

Government Procurement.—Under proposed EC directives in the so-called "excluded sectors" of government procurement, there is currently a proposal which would provide for a preference margin of 3 percent for EC-origin products comprised of at least 50 percent EC content (where the purchasing entity is offered comparable EC and non-EC products). Clearly, many of these products are integrated circuit-intensive, so the use of a U.S.-origin chip, as opposed to an EC-origin chip, might make it more difficult for a company to realize its objective of producing an EC-origin final—product. *However, the way to address this issue is to negotiate access to the EC procurement market—which is a major objective of ours in Geneva—in which case a U.S.-origin integrated circuit will have a status equal to that of an EC-origin integrated circuit.*

Tariffs.—Finally, the revised origin rule has implications for the dutiable status of both integrated circuits and products which might incorporate them to such a great degree that the origin of the product is largely determined by the origin of the—integrated circuits. *Again, the solution is to be found in the negotiation of the tariff barriers and not necessarily the way in which the good's origin has been determined.*

I hope that this memorandum has been useful in outlining our position on the EC's "diffusion" rule of origin and the more general issue of rules of origin in connection with local content requirements and the efforts we are making to address this situation.

PREPARED STATEMENT OF LIONEL H. OLMER *

Thank you, Mr. Chairman, for the opportunity to testify on Europe-19992 (EC-92) on behalf of the U.S. Chamber of Commerce. I have given the subject a great deal of thought based on my experience as a senior trade official in former President Reagan's first Administration and since then as an attorney involved in international business activities and as Vice Chairman of the U.S. Chamber's Policy Subcommittee on EC-92.

I reach two conclusions regarding EC-92: this historic process will have a fundamental impact on the world trading system and on the U.S. specifically; and no other issue places a greater demand for cooperation between the government and the private sector to assure that U.S. interests and rights are sustained.

The Chamber is persuaded that completion of EC-92 on terms consistent with the General Agreement on Tariffs and Trade (GATT) norms will offer substantial benefits to all parties. We will work hard to help to realize this potential.

One might have expected that the ubiquitous pronouncements from Europe regarding EC-92 would be met with uniform praise, awaited with anxious anticipation, and greeted with ringing endorsements by the private sector and governments around the globe. After all, it is not every day that invitations are warmly issued by what will be the world's largest trading bloc to take advantage of common technical standards, uniform business practices and solemn commitments to the principles of free trade. Indeed, optimism is warranted because economies of scale should be created once this market of 323 million people becomes a reality.

So why do we have the mixed reviews, rising apprehensions and spreading uncertainty? In part, I think it is because of differences between rhetoric and performance in the EC's policy statements and implementing measures that explicitly and implicitly distinguish insiders from outsiders and because of a growing perception of the primary motivations propelling Europe along this adventurous course. In my testimony, I will point out some of these differences; briefly comment on why EC-92 is so important; speak to the motivations; and suggest what may be an appropriate role for the Congress as EC-92 unfolds.

The current European market for U.S. business is enormous and growing. Exporters and importers, banks, insurance and data service companies, manufacturers with an overseas presence and those without, all are participants in a trade and investment account that total led more than one trillion dollars in 1986. Three-and-a-half million jobs are dependent on the activities of U.S. and European subsidiaries, branches, representative offices and joint ventures in the civil sectors of our interdependent economies, exclusive of banking.

Business and government leaders—and especially the Congress—are properly concerned regarding the future competitiveness of U.S. high technology industries—all the more reason why keen attention must be paid to EC-92. Last year, U.S. exports of electronics products and commercial aircraft exceeded 15 billion dollars; research and development and manufactures of informatics-related products inside the EC by U.S. subsidiaries at least equal led this figure. Moreover, it is evident that the EC has "targeted" high-tech competitiveness no less seriously than certain of our Asian trading partners and with substantially greater amounts of government subsidies.

The Chamber's Policy Subcommittee on EC-92 has expressed strong support for the completion of Europe's internal market, so long as the process is based on the following principles:

1. Economic welfare and social equity are more likely to be advanced by market-oriented, incentive-based economic policies that promote the free and unencumbered flow of trade and investment.

2. Open access by non-EC parties is an essential ingredient for the EC's efforts to foster ec .nomic dynamism.

3. National treatment—rather than sectoral reciprocity—should be the underpinning of our economic relationship.

4. Transparency in rule-making and timely and nondiscriminatory enforcement of rules for Europeans and non-Europeans alike are essential.

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* The views expressed herein are not necessarily the views of the law firm, Paul, Weiss, Rifkind, Wharton, and Garrison.

The signals from Brussels and other European capitals, at this stage in EC-92's implementation, suggest that strong private sector monitoring is needed and that U.S. government intervention may be required to achieve these objectives in actual practice. Examples of these negative signals are:

• *Rules of Origin and Local Content:* The EC has recently determined that in order to be treated as "European," foreign manufacturers of semiconductors will have to perform the process of "diffusion" in Europe. While many U.S. and Japanese chip producers currently have operations in Europe, few have diffusion facilities there. One U.S. company chief executive told me that this EC rule will require an investment in excess of 100 million dollars for this capital-intensive part of the semiconductor process in order for his company to sustain its market position.

• *Government Procurement:* The prospect of an opening for outsiders in the EC's collective 600 billion-dollar annual public procurement market is very encouraging. Yet pending directives would impose a 50% local-content requirement for non-EC companies and a 3% bidding price premium for EC firms.

• *Transitional Rules:* As political interests are balanced among the 12 member states and various EC industries, the legitimate interests of outsiders may be the first to be traded off. "Fortress Europe" is not a realistic outcome, in my view; both European governments and their private sectors know well how dependent their economies have become on international trade. But "selected protectionism"—proffered as temporary measures for import-sensitive sectors, such as automobiles—will be defended as necessary. For example, despite record profits, the EC's auto manufacturers are asking for the imposition of "voluntary" restraints on imports for a transition period of five-to-seven years. While aimed primarily at the Japanese, such restraints are likely to have a direct bearing on U.S. export opportunities as well.

• *Competition Policy:* According to U.S. Federal Trade Commission chairman Dan Oliver, recent EC antitrust determinations suggest the use of its competition policy as a protectionist device. For example, a new "block exemption" would prevent a mass-market franchiser like McDonald's from contracting with a single soft drink company to supply all of its franchisees. Oliver noted that this action appears contrary to the EC's common market objective, and questioned the coincidence that the companies currently most likely to be able to supply large European franchisers are companies whose parent entities are non-European.

• *Financial Services:* The EC Commission's Vice President for Financial Services and Competition Policy, Sir Leon Brittan, recently told an American audience in Washington, D.C. (according to an AP press report that I read in Asia last week) that "companies who wait until 1992 before setting up business in Europe may be too late." Although he added that the 500 U.S. banks already operating in Europe have nothing to fear, this statement appears to contradict the positive direction of the EC's modified "Second Banking Directive" of April 23 (which adopts "national treatment" rather than reciprocity as the test for market access), as well as positive statements made by Sir Leon during his recent visit to the U.S.

• *Standards Setting:* Contrary to a commonly held view, the EC Commission in Brussels is *not* setting technical standards for European products. Rather, it is proposing only "essential" health and safety requirements which will be translated into detailed specifications by Europe's private standards-setting organizations (e.g., the Committee for European Standardization, and the Committee for European Electrotechnical Standardization). Inasmuch as few outsiders thus far have been permitted either to participate in or to observe standards development activities, there is concern that the process could give rise to non-tariff barriers on imported goods.

The economic rationale for EC-92 is best detailed in a study funded by the EC Commission and published in 1988, popularly known as the "Cecchini Report." Entitled "1992, The Benefits of a Single Market," the study de-emphasizes the enormous dislocations that will be created in the near term if EC-92 proceeds as planned. Instead, in my view, the Report makes some heroic macroeconomic assumptions to sustain a rosy forecast about the scope of the benefits of an integrated market.

What the EC ultimately decides to do about its motor vehicle sector will be instructive, because that industry is enormously important to the overall economy. It has a ripple effect by which a dozen or more supplier industries, such as steel, glass, rubber, textiles and increasingly electronics, have an equal interest. (Some analysts calculate that by the year 2000, about $1,500 of the value of an automobile will be comprised of electronic components!)

The fight between France and the U.K. over whether Nissan autos manufactured in Britain and exported to France would be considered *Japanese* (and therefore subject to France's quotas on Japanese cars) if they had less than 80% European content had to be resolved by President Mitterand and Prime Minister Thatcher. The solution—that France would treat the U.K. Bluebirds, which currently have 70%

local content, as European for now on the understanding that the EC-content will be increased to 80% in a few years will not win either side an Adam Smith award in behalf of free trade. But at least it is a "solution" for those two countries. Meanwhile, Italy has reaffirmed its position that it will count the U.K. Nissans against its annual quota of 2,600 "Japanese" cars.

The deeper significance of the tension in the automotive sector lies in Europe's recognition of how far behind it has fallen in. manufacturing efficiency, *despite* its car industry's current profitability. According to industry experts, the Japanese produce an automobile with about 18 man hours, versus 24 for the U.S. and 37 for Europe, on average. Mr. Mitterand and Mrs. Thatcher (and I suspect the leaders of Italy's government) are seeking to ease the pain of their uncompetitive domestic industries.

I believe that the principal motivating force behind EC-92 is a fear of being left further behind in the race for 21st century competitiveness. The dominance of Japan and America in computers, telecommunications, semiconductors and commercial aircraft has been cause for Europe's treasuries to pump tens of billions of dollars into efforts to catch up. I expect this will continue. Moreover, if there is one absolute truth about "open competition," It is *not* that everyone will benefit, but rather that some must lose. And Europe's politicians have shown a decided disinclination in years past to suffer the consequences of telling constituents that fair competition is what makes for better products at cheaper prices for the benefit of people throughout the EC. That EC-92 will produce many losers is reflected sharply in the words of leading European businessmen, such as Carlo De Benedetti, former chairman of Imperial Chemicals, who said that the "next 10 to 15 years will be perfect hell," littered with the "dead and wounded" who will fall in pursuit of a common market.

I further believe that concern is warranted by the U.S. as to whether, given its drive to make EC-92 a success, Europe can simultaneously sustain support for the multilateral trading system and the current Uruguay Round negotiations. According to Mrs. Edith Cresson, the French government's Minister of European Affairs (and no stranger to international trade issues), "The U.S. and Europe should agree on a joint strategy to counter the economic menace of Japan." Well, at an earlier time in our commercial history this might have been dismissed as misguided or perhaps treated as a serious proposal by some. But in today's world, it is badly out of step with economic reality. For better or worse, Japanese investment in the U.S. and Europe (more than half a million jobs in Britain alone are dependent on Japanese investment in U.K. manufacturing), joint ventures, product and component dependencies, all reveal the interdependent character of world trade. We cannot "gang up" on Japan because it is not in our self interest—and this is true for Europe as well.

EC Commission Vice President Brittan aimed his alert not to wait until 1992 at U.S. businesses, lest they be too late. But I believe that his warning has meaning for the Administration and Congress as well. Both need to assert with forcefulness and conviction the view that, while the integration of Europe is welcome, it must not come at the expense of the American private sector, which has already paid for its continuing right of access in Europe through the opportunities granted over the past many years to European businesses in the U.S. market. In October 1988, the Senate called for a "bicontinental dialogue" on the implications of the single market program and enumerated certain objectives to guide the new Administration. Perhaps it is time to review the degree to which this dialogue has been implemented and to which the desired assurances have been obtained. I would encourage an effort to develop more specific objectives, a timetable for the Administration and a closer monitoring of the progress toward EC-92. Neither the business community nor the U.S. government can afford to wait until 1992 if the U.S. wishes to ensure an ability to take full advantage of EC-92's opportunities.

There is no substitute for close and comprehensive consultation between government and the business community in seeking to achieve these objectives, and the Chamber looks forward to filling a constructive role in this regard.

Thank you, Mr. Chairman, for the opportunity to testify before your Committee.

COMMUNICATIONS

STATEMENT OF THE AMERICAN INTERNATIONAL AUTOMOBILE DEALERS ASSOCIATION

SUBMITTED BY ROBERT M. MCELWAINE, PRESIDENT

URUGUAY ROUND NEGOTIATIONS AND POTENTIAL EUROPEAN COMMUNITY BARRIERS TO TRADE IN AUTOMOBILES

On behalf of our 10,300 American automobile franchises and their approximately 240,000 employees, the American International Automobile Dealers Association (AIADA) appreciates this opportunity to share with the Senate Finance Committee our concerns about the European Community's adoption of trade policies that would distort international trade in automobiles. We hope that you will encourage our negotiators to keep these concerns in mind throughout the Uruguay Round of Multilateral Trade Negotiations.

I. INTRODUCTION

AIADA represents Americans that sell and service imported automobiles. The livelihood of our members and their employees depends on free trade, in particular the free flow of automobiles across international borders.

We believe the European Community and the United States are on a collision course on automotive trade. The United States, in its continuing effort to keep world markets open, rightly rejected legislation that would have established domestic content requirements for U.S.-made automobiles. Elements within the Community, however, are now pushing for an EC-wide requirement for an 80 percent domestic content level in automobiles. Further, they have indicated that such an extraordinarily high content requirement would determine the country of origin of imports. Under such a formula, Hondas exported to Europe from the factory in Marysville, Ohio, Nissans from Smyrna, Tennessee, and Toyotas from Lexington, Kentucky, would be classified as "Japanese," even though as much as 75 percent of their content would be of American origin. They would then be subject to the quotas on Japanese automobiles the Community is expected to establish.

Such action would block one of the most promising developments in American exports in many years. The three Japanese automakers are planning to export up to 150,000 vehicles, collectively, to the Community every year. The value of these exports is in excess of $1.5 billion annually. This could substantially improve the U.S. trade balance.

We would expect the United States to retaliate against such unfair treatment and we would anticipate that the target for such retaliation would be Europe's substantial automotive exports to the United States. Our members--retailers of BMWs, Jaguars, Mercedes-Benzes, Porsches, and Volkswagens—would find their product unavailable, or priced out of the marketplace by punitive tariffs. More than 2,000 American businesses, employing 70,000 American workers, would be imperiled.

We believe it urgent that the United States make it known to the EC Automotive Committee, in the strongest possible terms, that the application of quotas to U.S.-made automobiles, regardless of the nameplate, will be regarded by us as an unfair trade restraint and that we will retaliate. In addition, our negotiators must remind their counterparts in the Uruguay Round negotiations of our concerns. The Community needs to be dissuaded from this policy before the tide of events sweeps it into such a short-sighted and ultimately disastrous course.

At the same time, we should attempt to dissuade the EC from adopting Community-wide quotas on Japanese automobiles to assuage those nations that currently operate such restraints. We should add here that our bargaining power over such a

demand would be greatly enhanced if the Japanese government were to end its costly and archaic "voluntary" export restraints on auto exports to the United States.

II. PRODUCT AT ISSUE

All motor vehicles that may be affected by EC-92 trade policies should be the subject of the Uruguay Round negotiations. Motor vehicles "principally designed for the transport of persons" generally are classified under HTS heading 8703. They are the principal focus of our concern. To a lesser extent, trucks also may be affected by EC-92 policies. Motor vehicles "for the transport of goods" are classified under HTS heading 8704.

III. BACKGROUND

When a country imposes trade barriers against the automobiles of another country, we frequently feel the impact here in the United States. In 1992, not just five, but twelve, countries may have in place some of the most rigid trade barriers yet against automobiles produced by Japanese manufacturers. If this occurs, not only will our members be hurt, but auto manufacturers and consumers in the United States will suffer as well.

We share the general concern in the United States about the possibility of a "Fortress Europe" emerging from the European integration process. For the world automobile industry, 1992 threatens higher import barriers and a shrinking European market for cars produced by Japanese manufacturers in the United States and in Japan. In 1992, national trade regimes will be replaced by Community-wide rules. Currently, tolerance for Japanese imports varies dramatically from country to country. For example, West Germany imposes no import restrictions on Japanese cars, while Italy imposes a quota restricting imports to less than one percent of its market—less than 3,000 units annually. Comparable community-wide rules could have a substantial negative impact in the United States.

The European Community is now in the process of identifying the common ground between those European governments that favor somewhat freer trade and those that seek to protect completely their domestic auto manufacturers. Recently, Martin Bangemann, the Community's new industry commissioner, recommended that existing national import restrictions be lifted and that they not be replaced with a community-wide quota after 1992. As the European Community struggles to define its united trade policy, we see two serious threats to an important sector of the U.S. economy. First, the Community appears headed toward adopting a minimum local content requirement as high as 80 percent as the basic means to determine the origin of goods. Second, notwithstanding Mr. Bangemann's announced position, there is a strong possibility that today's protectionist quotas will be extended Europe-wide. Low quotas combined with high domestic content requirements will constitute a virtual import ban on cars otherwise destined for Europe.

If the European Community adopts a significant minimum local content requirement, not only cars produced in Japan, but those produced in the United States as well, will be denied access to that market. Such a restraint effectively would constitute a quantitative restriction in violation of Article XI of the General Agreement on Tariff and Trade.

The trade feud that erupted last year between Great Britain and France over U.K.-made Nissan Bluebirds underscores the impact that local content requirements will have on Japanese cars in particular. Nissan operates a manufacturing facility in Sunderland, England. In late September 1988, the first Nissan cars were available for export to continental Europe. However, the Government of France (followed by the Government of Italy) declared unilaterally that it would treat these British-made Bluebirds as "Japanese" and thus subject to its 3 percent national quota. The Government of France argued that the British-made Bluebirds were "Japanese" automobiles because more than 20 percent of the content was non-European. The Government of France recently backed away from this position, but the Government of Italy still has not.

In our view, the initial French position directly contradicted a governing Community standard. In general, the European Community determines the origin of goods by looking to the location at which the "last substantial manufacturing operation" takes place. If the last substantial manufacturing operation takes place in Europe, the product will qualify as European and be permitted to circulate freely within the Community. The Community rule implies no minimum local content requirement.

When considered along with the Community's recent rulings on photocopiers and semiconductors produced by Japanese manufacturers, the Bluebird controversy un-

derscores an alarming trend among EC Member States. Through the Commission, the Community has determined that Ricoh copiers made in the United States are not U.S. products, but rather are Japanese products, and therefore are subject to existing dumping duties. With respect to semiconductors, the Community has decided that in order for them to be treated as a European products, the etching process—the costliest part of the manufacturing process—must take place in Europe.

Although the British Government has argued persistently that the Bluebirds are European and not Japanese, even it supports a minimum local requirement of 80 percent. In its agreements with Nissan, Honda, Isuzu, and Suzuki, the government has insisted on an 80 percent local content requirement. However, it allows manufacturers a period of time ranging from two to three years to reach the 80 percent level.

IV. IMPACT OF EC TRADE BARRIERS

If the European Community adopts an 80 percent local content requirement as advocated by France, Italy, Spain, and Portugal, the United States will be seriously affected. The factories of Japanese manufacturers in the United States will reach full capacity by 1992-93, when these factories should be producing more than 2.5 million units a year. To the extent production exceeds demand here, the manufacturers intend to begin exporting these U.S.-made automobiles to Europe and Canada. With an 80 percent local European content requirement imposed, exports from the United States would be foreclosed.

In addition to being opposed to such an arbitrary and illegal domestic content requirement, we also are deeply troubled about a possible EC-wide quota on imports. Currently, France, Italy, and Spain (which together account for about 40 percent of total European sales) are virtually closed to Japanese producers. Portugal and the United Kingdom also limit imports of Japanese cars. Whether the Community adopts Italy's one-percent quota or the United Kingdom's eleven-percent limitation on the Japanese share of their market, the effect will be very damaging. We are particularly concerned that the overall quota, whatever the applicable percentage, is likely to be limited to no more than a million units a year, the level established in 1985-86. Any car not meeting the 80 percent domestic content requirement would be included in the quota, even if manufactured in a member country.

Any trade barrier that effectively bars exports to Europe of automobiles produced by Japanese manufacturers either in the United States or in Japan will increase pressure on the U.S. market and, ultimately, will hurt U.S.-Japanese trade relations. Denied access to Europe, Japanese manufacturers in the United States would be forced to move their domestic production into the U.S. market in competition with Detroit. In any event, the European-caused distortion to trade will generate increased protectionist pressure within the United States to severely restrict imports of cars from Japan.

Further reductions in imports of Japanese cars naturally will raise the price of the product we sell. Once again, the American consumer will get stuck with the bill for this protectionist folly. Since 1981, the Japanese export restraints have encouraged Japanese manufacturers to abandon production of efficient, low-cost cars and, instead, to focus on high-cost luxury vehicles. Historically, when Japanese manufacturers raise the price of their automobiles, U.S. manufacturers have followed suit. As always, the consumer at the lower end of the market feels the squeeze.

V. CONCLUSION

Our members risk getting hit with a double whammy. Any action taken by a united Europe to close its markets could ultimately lead to reduced U.S. imports of both Japanese automobiles and European automobiles. We thus are raising concerns now with the hope that the U.S. Government will discourage the European Community from adding additional bricks and mortar to the fortress to shield European auto manufacturers from the thrust of foreign competitors.

We urge the Senate Finance Committee to encourage the Administration to take an active role in Europe's 1992 process, and to voice our concerns during the Uruguay Round negotiations. The European Community must come to understand that the application of quotas to U.S.-made automobiles will be regarded as an unfair trade practice, will trigger U.S. retaliation, and will undermine progress in the Uruguay Round on issues important to the Community.

**STATMENT BY AMERICAN PLYWOOD ASSOCIATION (APA)
RELATIVE TO IMPACT OF EC-92
ON U.S. WOOD-BASED STRUCTURAL PANEL INDUSTRY**

BACKGROUND

Overseas promotion by APA began in 1964 with trade missions to Japan and Europe and the staffing of European offices. Today, with assistance from the Foreign Agricultural Service, APA has representatives in four offices in Europe, one in Japan and another in the Caribbean. Over that period of time, exports have grown 35-fold, with a current value approaching one-third billion dollars. Much of the present activity has been concerned with gaining official government acceptances of our members' products - as well as gaining customer acceptance. Government acceptances are in hand for Denmark, West Germany, Holland, Sweden and the United Kingdom. APA members' products are also widely used without restriction in Belgium, Italy and Norway. The requirements and acceptances differ significantly from one country to another.

COMMON PRODUCT STANDARDS

One large benefit of EC-92 will be the uniformity of standards throughout the EC. At the present time, each country's own standards must be satisfied in order to gain approval of a product for use in building construction. APA requested acceptance of plywood in West Germany in 1975. The approval was finally granted in 1982 after much testing and study. However, because of the standards that were imposed, the approval is limited - applying only to factory-built housing - a very small market in Germany.

So, a common set of product standards throughout the EC would be very beneficial to the wood-based structural panel industry.

TRANSPARENCY OF THE STANDARDS-SETTING PROCESS

The EC intends to base European standards on those promulgated by the International Organization for Standardization (ISO) where they exist. However, because many of the standards that are needed do not yet exist as ISO standards, many new standards must be written. While the GATT Code requires that draft standards be made available for comment prior to promulgation this is too late in the process to effect important changes. The U.S. has been locked out of the

European standards activity (CEN/CENECEC) even to the extent of being observers. The APA would like to participate as an observer and would do so if permitted.

THE INFLUENCE OF EUROPEAN INDUSTRY

It is our opinion that the European Industry is very influential in setting CEN standards for wood panels. In the U.S., the standards setting bodies, ASTM, ANSI, etc., must have the committee membership balanced between producers, users and general interest to avoid dominance by one group. We are not aware of any similar requirement in CEN.

Those EC countries that do not produce panel products but instead import large quantities have minor roles in the standard setting process.

ACCEPTANCE OF TEST DATA AND CERTIFICATION

The above comments relative to product standards apply with equal validity to Test Data and Certification Programs. At the present time acceptance of APA data and certification in Europe varies from complete acceptance to no acceptance. A uniform set of standards with appropriate guidelines would be most helpful - provided, of course, that the standards are reasonable.

U.S. GOVERNMENT INVOLVEMENT

APA recommends: 1) that the government press for U.S. observer status in CEN/CENECEC meetings. This does not in itself solve potential problems with standards, but it does help in keeping abreast of problems as they develop. And 2) that the government press for reciprocity of test data and certification programs by mutually acceptable bodies worldwide.

STATEMENT OF THE BUSINESS ROUNDTABLE

The Business Roundtable is an organization of over 200 chief executive officers of U.S. companies representing a wide range of industries. The Business Roundtable believes that the integration of the European Community market is an historic and essentially positive undertaking. The United States should strongly encourage the progress of the 1992 Program. A stronger, unified Europe is in our long-term interest. Overall, the 1992 Program presents much more of an opportunity than a threat to U.S. business. The U.S. economy will benefit from a unified, market-oriented Europe. The European Community is a key market for U.S. products and services. In addition, a stronger Europe is likely to be more willing and able to bear its share of common defense and other security-related costs. We should not let the fear of a "Fortress Europe" cloud the positive aspects of the 1992 Program. The three questions posed by the Senate Finance Committee should be analyzed against this backdrop.

1. Will the 1992 Program Result in a "Fortress Europe" With High Protectionist Barriers?

The Business Roundtable is optimistic that the 1992 Program will not result in a "Fortress Europe" with high protectionist barriers. However, both the U.S. Government and the U.S. business community should continue to monitor closely the progress of the 1992 Program. We need to be vigilant in resisting any efforts by the European Community to include market restrictive or discriminatory elements in the Program.

Assessing the impact of the 1992 Program on the Community's trading partners is a difficult proposition. This is because the details of the Program are still evolving. The Community itself did not begin to focus on the external implications of market integration until late last year. More importantly, there is an ongoing debate within the Community concerning how the Program should affect its trading partners—and a consensus has yet to emerge.

In this context, the Roundtable worries less about the threat of overt highly protectionist barriers and more about the threat of subtle discriminatory features that are creeping into some aspects of the 1992 Program. While the U.S. Government and the U.S. business community have a great deal to gain from a dynamic and revitalized Europe, these reforms should not be achieved at the expense of the United States and the rest of the world.

The following areas should be monitored closely:

LOCAL CONTENT AND RULES OF ORIGIN

A variety of European Community trade policy developments indicate a movement towards local content requirements and new rules of origin. For example, since 1988 the Community has been using its antidumping laws to impose local content requirements administratively. The Community's new approach to defining rules of origin also has the effect of imposing local content requirements. In addition, some representatives from European business are urging the Commission to regulate inward investment, and, in particular, to impose local content requirements as a condition to investment.

Taken together, these developments are forcing non-European manufacturers, primarily the Japanese, to increase their investments in Europe. This could produce severe adverse consequences for U.S. competitiveness. For example, we could experience a shifting of capital investment from the United States to Europe, and the "designing out" of U.S. components to meet European rules of origin requirements. Japanese firms may be less likely to enter into supply agreements and joint ventures with U.S. firms. There are already indications that foreign customers, which supply the European market, have dropped U.S. component manufacturers in favor of Community sources in order to satisfy local content thresholds.

This broadening of local content requirements and unilateral formulation of new rules of origin could also seriously undermine U.S.-led efforts in the Uruguay Round—which generally have been supported by the Community—to discipline local content requirements and liberalize trade in general.

The lesson here is that we must examine not only the 1992 Program directives and statements issued by the Commission, but also other policy developments in the Community, in order to understand fully the impact of the 1992 Program on non-European firms.

RECIPROCITY AND NATIONAL TREATMENT

It seems likely that, under the 1992 Program, some form of reciprocity will be a condition for granting market access to foreigners. Reciprocity is a feature of the Second Banking Coordination Directive, the Life Assurance Directive and the Investment Services Directive.

The concept of reciprocity means different things to different people. To date, no precise definition of reciprocity has emerged from the Community. But there are some encouraging signs. The Community's statement last October on the external implications of the 1992 Program was the first indication that trading partners would not have to adopt "mirror image" legislation identical to that of the Community.

Even more recently, the European Commission agreed to modify significantly the reciprocity provisions in the Second Banking Directive. Rather than demanding "equivalent" treatment, the new reciprocity provisions are based on concepts of national treatment, effective market access and similar competitive opportunities. This formulation of reciprocity takes into account that certain trading partners, including the United States, have domestic laws which are non-discriminatory, but may be less liberal than Community laws. Although questions remain about application and interpretation, The Business Roundtable is extremely encouraged by this important development in the Commission's thinking on reciprocity.

PROCUREMENT POLICIES

Liberalization of government procurement is particularly important to U.S. firms: the European market has an annual value of over $500 billion. Many of the Community's directives signal a significant improvement over the current procurement system, particularly the proposal to extend competitive procurement to four new areas—transportation, energy production and distribution, water and telecommunications. The key issue here for both defense and non-defense related industries is to ensure that liberalization of procurement policies does not unfairly favor European (including European Free Trade Association) firms over non-European firms, or otherwise discriminate against non-European signatories of the GATT Procurement Code.

Another area of concern is a provision giving Community producers time for "industrial adaptation" to the 1992 Program. This could delay effective implementation of the Program's procurement initiatives and adversely affect Uruguay Round efforts to broaden the GATT Procurement Code to reach new sectors.

HEALTH, SAFETY AND TECHNICAL STANDARDS

The development of harmonized standards to determine what may be sold in the Community is an extremely important process. On the one hand, a unified approach to standards would help U.S. companies by easing the movement of goods and services within the Community. At the same time, there is the fear that new standards could create barriers to trade and discriminate against foreign-made items.

Another issue that needs to be clarified is how the Community intends to treat testing and certification procedures that are conducted outside its borders. Will self-certification suffice, or will third-party testing in accordance with Community criteria be required? The latter could substantially increase costs for U.S. exporters and delay their access to the European market.

Finally, it is crucial that U.S. companies be able to evaluate the ongoing standard-setting process. We are encouraged by recent indications that the Community intends to increase the transparency of the process.

QUANTITATIVE RESTRICTIONS

The 1992 initiative may involve the shifting of existing GATT-illegal quantitative restrictions, as well as voluntary restraint agreements, from the national to the Community-wide level. This broadening of quantitative restrictions could severely limit market access for U.S. companies. If Community-level quantitative restrictions are used together with strict local content requirements and rules of origin, they could restrict market access both for U.S. exports and products produced by European-based subsidiaries. Shifting quantitative restrictions to the Community level could also undermine efforts in the Uruguay Round to negotiate comprehensive rules on the use of safeguards.

Because the 1992 Program is still evolving, it is too early to state with certainty what the precise impact will be on U.S. exporters and investors. While no part of

the Program is, at present, overtly protectionist, the U.S. Government should remain alert to protectionism, as well as to more subtle forms of discrimination.

2. WILL THE 1992 PROGRAM DESTROY THE URUGUAY ROUND NEGOTIATIONS?

To a great extent, the answer to this question depends on the diligence of the United States in monitoring the linkages between the 1992 Program and the Uruguay Round, and the skill and vigor with which the United States pursues the GATT negotiations. Given the strong U.S. commitment to promoting progress in the Uruguay Round, it is critical to ensure that developments in the 1992 Program do not undermine the multilateral negotiations. To the extent that the European Community intends to "manipulate" the linkages between the 1992 Program and the GATT negotiations to its benefit, the United States should be in a position to do the same.

One concern is that the Community will take a harder line in developing the 1992 Program in order to influence the GATT negotiations to its advantage, particularly in those areas, such as services and investment, that are not yet covered by the GATT. Failure to understand and anticipate the linkages between the two initiatives will seriously impair the U.S. Government's ability to positively influence the outcome of both the 1992 Program and the Uruguay Round.

Some of the specific areas that require careful monitoring are:

- The application of the principle of reciprocity in the 1992 Program, which could potentially undermine the principle of national treatment integral to the GATT.
- The 1992 Program directives on banking, insurance, investment services and professional qualifications, which will have a direct impact on the services negotiations.
- The way in which the 1992 Program sets health and safety standards, which will affect multilateral efforts to harmonize standards.
- Measures adopted by the European Commission in areas such as services, investment and intellectual property protection, which are not covered by the GATT.
- Community procurement plans, and specifically the planned extension of coverage to the water, transportation, energy and telecommunications sectors, which relate to negotiations to broaden the scope of the GATT Procurement Code.
- European Community practices concerning local content requirements, which relate to negotiations on trade-related investment measures.

Closer coordination should be developed between the U.S. Mission to the European Community and the U.S. Mission to the GATT, to ensure that these and other linkages are identified and acted upon in a timely manner. If we highlight the 1992 developments in the Uruguay Round negotiations, the Community may feel more constrained when making its internal market decisions. This applies both to those 1992 initiatives which appear to be inconsistent with existing multilateral obligations, and those initiatives which may inhibit efforts to establish new multilateral rules in areas not presently covered by the GATT.

3. IS THE UNITED STATES MONITORING THE PROGRESS OF THE 1992 PROGRAM CLOSELY ENOUGH AND ARE WE PREPARED TO SPEAK OUT FORCEFULLY AGAINST OBJECTIONABLE FEATURES?

Over the past year, both the U.S. Government and the U.S. business community have made great strides in monitoring the progress of the 1992 Program, but our work is not over.

The most constructive course the U. S. Government can follow is to focus on influencing the direction of the 1992 Program through a comprehensive balanced dialogue with the European Community. This means actively supporting the positive aspects of the 1992 Program and speaking out forcefully against the objectionable features of the Program. As mentioned above, the Community itself is struggling with many of these issues. We should use this internal debate to our advantage. The Commission is accessible to U.S. companies and we are increasingly taking advantage of this accessibility to press our positions. Recently, we saw the success of presenting our position aggressively to the Community when the Commission modified the reciprocity provisions in the Second Banking Directive.

Both the U.S. Government and the U.S. business community should be prepared to make it clear to officials at the European Commission and in member-states that the 1992 Program should not become a means for adopting protectionist, discriminatory policies. Recognizing that the 1992 Program is an ongoing process, however, it is premature to consider anticipatory legislative or administrative proposals which call for retaliatory or mirror-image actions. In view of the opportunities the 1992

Program affords, it would be unfortunate if either the U.S. Government or the U.S. business community overreacted to developments in the 1992 Program.

Instead, both the Executive Branch and the Congress should seek the development of up-to-date, accurate information and analysis on the 1992 Program. The U.S. Mission to the European Community should be expanded so that the 1992 Program can be scrutinized in greater detail and in a more timely matter. This would not necessarily require additional resources. Economic officers assigned to other posts within the Community's member states could be assigned to Brussels to assist with the increased workload.

We also recommend devoting additional resources to the U.S. Government's outreach program on the 1992 Program for smaller U.S. companies, whose resources to anticipate and handle potential problems or to capitalize on opportunities are more limited than those of larger U.S. multinational companies.

The U.S. business community must also be more vigilant in protecting its interests. In particular, U.S. firms should be prepared to take an active role in the development of health, safety and technical standards. U.S. companies with operations in Europe should make efforts to participate in the European standards-setting process. U.S. exporters without a presence in Europe should make sure that their trade associations are actively monitoring the process and disseminating information to them.

CONCLUSION

The 1992 Program presents much more of an opportunity than a threat. In order for this opportunity to be realized, U.S. companies and the U.S. Government should work to promote the adoption of those measures which support the Commission's October 1988 position that the 1992 Program is intended to make Europe a "world partner."

STATEMENT OF THE CHEMICAL MANUFACTURERS ASSOCIATION

I. INTRODUCTION

The Chemical Manufacturers Association (CMA) is pleased to submit this statement on the European Community's (EC) program to complete its internal market by December, 1992.

CMA is a nonprofit trade association whose member companies represent 90 percent of the production capacity for basic industrial chemicals in the United States. In 1988, two-way chemical trade between the U.S. and the EC totalled over 9.4 billion, with shipments to the EC accounting for over 26 percent of total U.S. chemical exports. Given the large volume of trade between the U.S. chemical industry and the EC, the completion of the internal market and its ramifications are of great importance to the U.S. chemical industry.

As a proponent of free market access, CMA supports the underlying principles and basic objectives of the single European market. The initiatives encompassed by the plan will present substantial opportunities for U.S. based companies. However, at the same time there is a potential for elements of EC-1992 to be structured or applied in a manner which could discriminate against or otherwise disadvantage U.S. industrial interests. As both the pace and scope of implementing measures increase, it is imperative that the U.S. government and industry monitor the legislative and policy developments raised by the EC-1992 effort.

In the sections which follow, CMA provides a brief overview of its approach to the EC-1992 program, as well as its responses to the specific questions raised by the Committee (hearing notice dated April 6, 1989).

II. OVERVIEW OF CMA APPROACH TO EC-1992

The effects of EC-1992 are likely to include a significant increase in Gross Domestic Product (GDP) of approximately 5-7 percent per year; a 6 percent decrease in consumer prices; and the creation of 2-5 million jobs. These economic improvements will result from the removal of direct barriers to commerce, increased competition and efficiency, and the increase in demand from a combined market of 320 million people. In brief, the opportunities created by the EC-1992 program are significant, particularly for U.S. export industries.

Approximately 300 directives are planned for implementing EC-1992. These directives are generally designed to remove physical, fiscal and technical barriers to the free movement of goods, services, capital, and people among the member countries of the EC. These directives have the potential to adversely affect U.S. business if

they are developed and implemented in a manner inconsistent with overall free trade principles.

One area that will deserve special attention as the EC-1992 program continues is environmental regulation. Although the European Community already has adopted a large number of standards related to product performance, physical compatability, health, safety and the environment, additional standards could create problems for competing products of U.S. origin. One example of the potential problems encountered in such legislation was the European Commission's proposed directive regulating preparations (mixtures) of chemicals products. The directive would establish regulations for the classification, packaging, and labeling of certain mixtures. The original draft directive would have required excessive disclosure of confidential business information; interventions by both the U.S. government and the chemical industry were successful in promoting disclosure provisions which provided better protection for such information.

The U.S. chemical industry has two perspectives to consider in evaluating progress toward EC-1992. On the one hand, several U.S.-based multinational corporations have substantial production facilities in the EC. On the other, some CMA member companies only export product to the EC from U.S. production facilities. Depending on the product line in question, both perspectives may be important.

CMA expects that for U.S. companies with a significant presence in Europe, the impact of EC-1992 should be virtually the same as for their European counterparts. From the perspective of U.S. chemical exporters, the promise of a revitalized EC market can only be realized fully if U.S. firms are allowed to participate on an equal footing with their EC competitors. Again, however, with respect to EC-1992 initiatives, U.S. exporters share many of the concerns expressed by EC chemical firms.

CMA has developed a "watch list" of the EC directives adopted and/or proposed which potentially affect the U.S. chemical industry. A copy of that material is attached for the Committee's further information.

III. "FORTRESS EUROPE" AND PROTECTIONIST BARRIERS

CMA does not believe that the creation of an internal European market will result in a "Fortress Europe" of protectionist barriers. The alarm over the possibility of the creation of a protectionist Europe is best exemplified by the concerns over the concept of reciprocity. Some commentators expressed a belief that the concept of reciprocity required a rigid "quid pro quo." Early in the EC-1992 process, it was thought that the access granted American companies to European markets after 1992 would be based on the access European companies have to the identical sectors in the American market. In October, 1988, the European Commission issued a statement entitled "Europe 1992: Europe World Partner," which has done much to reassure the Community's trading partners that protectionism is not their intent.

The October statement announced that the EC will continue to adhere to its commitments under existing international agreements. In this statement the Commission also clarified what it meant by reciprocity. Reciprocity will not mean an exact "quid pro quo," but means instead comparable market access. This is in accord with the principles of national treatment as outlined in GATT Article III.

The Commission's statement has raised some concern over the status of companies operating under Article 58 of the Treaty of Rome, at least in the context of several proposed directives. Article 58 states that any company organized to do business within the EC is entitled to national treatment. Although the Commission made clear that Article 58 would continue to apply to established subsidiaries of non-EC owned companies, the status of newly established subsidiaries has been questioned. The application of Article 58 to new subsidiaries is an example of an area in which it is incumbent upon U.S. industry to work with the U.S. government (particularly the Office of the U.S. Trade Representative and the International Trade Commission) in addressing these concerns.

IV. EFFECT OF EC-1992 ON THE URUGUAY ROUND (GATT) NEGOTIATIONS

As noted earlier, the EC has stated that in implementing EC-1992, the Community will abide by its existing international obligations under the General Agreement on Tariffs and Trade (GATT). However, for areas not currently covered by GATT rules, such as services, the EC will reportedly seek to assure access to other countries on a "reciprocal" basis until new international rules and disciplines (GATT or otherwise) are in place. EC-1992 should therefore enhance the Uruguay Round of Multilateral Trade Negotiations, and indeed should increase the importance of the talks. The talks should be viewed as yet another arena in which to carry on discus-

sions between the U.S. and EC members regarding EC-1992 and to express the concerns of U.S. industry. Together with various U.S. governmental agencies, the U.S. chemical industry expects to use the Uruguay Round negotiations to urge the adoption of trade liberalization rules which could also be implemented in the European Community.

V. MONITORING OF EC-1992

CMA believes that it is imperative that the U.S. industry continue to monitor legislative and regulatory activity in the European Community. This is especially true given the broad scope and accelerated pace of the program. According to the U.S. Department of Commerce, 148 of the approximately 287 directives called for in the 1985 White Paper (the Cockfield paper), which identified specific measures needed to complete the internal market, had been adopted as of mid-February, 1989. Some 174 measures have either been formulated as proposals or for which a commitment has been made to draft. Increased cooperation between both industry and various governmental agencies is crucial to ensure that American views on proposed EC legislation can be made in time, with a positive impact.

It should be kept in mind that the EC legislative process is vastly different from that of the American political process. EC directives and regulations are not always published before being voted upon. Advocacy before the EC may in some instances require significantly different approaches to assure consideration of industry's views.

The cooperation procedures adopted in the Single European Act (SEA) now require two readings of proposals (by both the European Parliament (EP) and the Council of Ministers (the Council)), instead of the one reading under the earlier consultation process. After the Parliament adopts an "opinion" and the Council adopts a "common position" by qualified majority, the proposal is read a second time by the Parliament. At this time any one of four actions may be taken, including adoption of the proposal, rejection, or possible amendment.

These new procedures (which are considerably more complex than as outlined here) increase the opportunities for the interested public to lobby and monitor EC efforts. There are now three ways in which proposals may be amended. Also, under the cooperation procedure it is more difficult to block legislation, since a single member state no longer has the power to do so. Advocacy efforts must therefore begin early and continue throughout the relevant stages of the new procedures.

In addition, the European Commission is beginning to exercise its authority in the policy arena. For example, the European Commission recently proposed new Guidelines for the EC system of granting temporary duty suspension. Ambassador Carla Hills of the USTR recently conveyed her concerns about the proposed changes in the system to the European Commission. CMA strongly supported Ambassador Hills approach on this matter, and believes the issue is a good example of the steps required to conduct effective advocacy at the European Commission.

Duty suspensions are regularly granted in the U.S. and the European Community as a means of avoiding the added cost of custom duties (to producers and consumers) when a product is not produced by domestic manufacturers. Importers and consumers thus realize an economic benefit when a duty is suspended. Although the procedural means for obtaining duty suspensions vary from country to country, "uniqueness" (insufficiency or the absence of domestic production) is a key criterion applicable to all systems.

The proposed Commission criteria would deny duty suspension in any case where the imported product "is subject to an exclusivity contract which has the result of restricting the ability of Community importers to buy the products from third parties." Ambassador Hills and CMA are concerned that this requirement could discourage the import of chemical products into the EC under exclusive license or distribution agreements. Such agreements are commonly used by chemical manufacturers to assure continued protection of products for which patent and intellectual property rights have been granted, particularly between companies in Europe and their foreign affiliates.

In our communication with Ambassador Hills, CMA suggested that some of the procedural requirements imposed by the Commission's duty suspension criteria are unworkable, or at best, vague. For instance, it is unclear how EC importers are to document the lack or insufficiency of production in the EC. Importers would apparently be required to approach EC producers and document that they are unable to provide "customized products" required to meet particular specifications before approaching foreign suppliers. No procedure is apparently contemplated to allow applicants to challenge refusals to grant duty suspensions or even to be informed of the reasons for rejection.

The type of high-level involvement represented by Ambassador Hills' expression of concern is a prerequisite to effective representation and advocacy before the European Community. CMA is pleased to note the active involvement of the Senate Finance Committee on EC-1992 issues, particularly those raised during the Committee's recent visit to the EC. Agencies such as the USTR and the ITC need to be informed of potential difficulties with the EC-1992 program, so that these matters may be pursued in both bilateral and multilateral negotiations (such as the Uruguay Round). In addition, the U.S. chemical industry will be working through its individual companies and through the European counterparts of industry organizations and associations to address specific aspects of the EC-1992 program which may prove disadvantageous to U.S. industry.

VI. CONCLUSION

CMA appreciates the concern shown by the Finance Committee regarding the possible negative effects of EC-1992 for the U.S. chemical industry. While the possibility exists that specific efforts by the European Community may adversely affect U.S. industry, effective monitoring advocacy will mitigate these effects. CMA's major purpose in addressing the EC-1992 program is to prevent any adverse effects on U.S. industry. At this time, it is CMA's view that the economic benefits represented by an integrated European market will far outweigh any adverse effects which might result. Nevertheless, CMA will continue to monitor European legislative and regulatory developments, in order to better support the U.S. government's trade policy efforts.

Enclosure.

Working List of EC Directives, Adopted and/or Proposed
Potentially Affecting the U.S. Chemical Industry

CMA WATCH LIST AS OF April 10, 1989

SIMIS* Number	Directive Description	OJ No.	Date of OJ	Implementation Date(1)
	"L" Documents - Adopted			
14	Antibiotic residues	L 275	9/24/86	12/31/87
15	Control of residues	L 275	9/24/86	12/31/88
19	Maximum levels for pesticide residues in cereals and foodstuffs of animal origin	L 221	8/7/86	6/30/88
20	Amendment of Directive 79/117/EEC on the prohibition of certain plant protection products (ethylene oxide)	L 212	8/2/88	7/1/87
21	Proposal for Directive on the fixing of guidelines for the evaluation of additives used in animal foodstuffs	L 64	3/7/87	12/31/87
25	Amendment to Directive 74/63 on undesirable substances and products in animal nutrition (maximum pesticide residues in animal feedingstuffs)	L 304	10/27/87	12/3/90
28	Simple Pressure Vessels	L 220	8/8/87	7/1/90
33	General Directive on sampling and methods of analysis	L 372	12/31/85	12/23/87
34	Preservatives (modification)	L 372	12/31/85	12/31/86
35	Emulsifiers (modification)	L 88	3/3/86	1/1/85
37	Obligation to indicate ingredients and alcoholic strength	L 144	5/29/86	5/1/88 (permit) 5/1/89

*-Single Internal Market Information System prepared by the U.S. Department of Commerce as of March 15, 1989

(1)-Indicates date by which the 12 Member States are to implement national regulations that are consistent with directive adopted. Actual implementation date of Member States is not known at this time. Implementation dates earlier than date of official journal indicates modifications that have been made to earlier adopted directives.

SIMIS Number	Directive Description	OJ No.	Date of OJ	Implementation Date (1)
38	Simulants (plastic materials in contact with foodstuffs)	L 372	12/31/85	1/1/86
39	Proposal for Directive concerning the placing on the market of high-technology medicinal products including those derived from biotechnology	L 15	1/17/87	7/1/87
40	Proposal amending Directive 75/318 concerning the testing of medical specialties	L 15	1/17/87	7/1/87 Portugal 11/91
41	Proposal amending Directive 81/852 con- veterinary medicinal products	L 15	1/17/87	7/1/87
42	Council Recommendation concerning tests relating to the placing on the market of medical specialties	L 73	3/16/87	Non Binding Council Recommendation
43	Proposal for a Council Directive concerning tests relating to the placing on the market of medical specialties	L 15	1/17/87	7/1/87
45	Council directive relating to restriction on the marketing and use of PCB's (polychlorinated biphenyls)	L 269	10/11/85	6/30/86
47	Non-ionic detergents (modification of existing Directive)	L 80	3/25/86	1/1/90
48	Membership of the European Agreement on detergents	L 350	12/31/85	12/31/87
54	Directive of products misleadingly defined	L 192	7/11/87	10/1/88
75	13th VAT Directive concerning tax refunds to persons not established in the Community	L 326	11/21/86	1/1/88
76	17th VAT Directive concerning the temporary importation of goods other than means of transport	L 192 C 324 amendment	7/24/85	1/1/86 and Derogation
78	Liquid Fertilizers	L 83	3/29/88	3/89
80	Proposal for the extension of information procedures on standards and technical rules (amendment to Directive 83/189)	L 81	3/26/88	1/1/89
87	Classification, Packaging and labeling of dangerous preparations	L 187	7/16/88	6/30/89
90	Good laboratory practices non-clinical testing of chemicals	L 145	6/11/88	1/1/89
94	Protection of workers by banning certain chemical agents and activities	L 179	7/9/88	1/1/90

SIMIS Number	Directive Description	OJ No.	Date of OJ	Implementation Date (1)
100	Directive relating to flavorings for use in foodstuffs and to sources of materials for this production	L 184	7/15/88	7/1/90
101	Council decision to established inventory of source materials for preparation of flavorings	L 184	7/18/88	7/1/90
146	First directive to approximate the laws of member states relating to trade marks	L 40	2/11/89	12/28/91
	"C" Documents - Proposed			
3	Production and trade in medicated feeding stuffs	C 41	2/16/82	TBA
5	Personnel responsible for inspection	C 262	10/14/81	TBA
33	Flavorings	L 100	4/19/88	10/1/89
34	Extraction Solvents	C 312 C 77 C 152	11/17/83 3/23/85 6/10/88	36 mos. after notification
35	Preservatives (modification)	C 330	12/17/81 (Partially Adopted)	12/31/82
37	Obligation to indicate strength and volume of containers	C 312	11/17/83 (Partially Adopted)	1/1/85
38	Modified starches	C 31	1/2/85 (Proposal)	7/1/86
39	Food Additives (modification of existing directives)	L 131	5/27/88	6/30/90
40	Materials and articles in contact with food (amendment)		Adopted	See "L 132"
42	Food Labeling (amendment)		Adopted	See "L 134"
47	Price transparency in the prices of medicine and social security refunds		Adopted	See "L 138"
49	Secondary fertilizers	C 12	1/16/87 (Proposal)	Within 12 mos. of notification
51	Cosmetics - 4th modification to directive 76/768		Adopted	See "L 141"
83	Regulation on Community trademarks	C 351 C 230	12/31/80 8/31/84	TBA Proposal

SIMIS Number	Directive Description	OJ No.	Date of OJ	Implementation Date (1)
84	First directive to approximate the Laws of member states relating to trade marks		Adopted	See "L 146"
85	Regulation on the rules needed for implementing the community trademark regulation		(Proposal)	
86	Regulation on rules of procedures for the Boards of Appeal of the Community's Trademark office		(Proposal)	
87	Community trademark office regulation on fees	C 67	(Proposal) 3/14/87	3/14/88
88	Arbitration procedure concerning the elimination of double taxation	C 301	12/21/76 (Proposal)	January 1st on the second year after adoption
89	Common system of taxation of applicable to parent companies and their subsidiaries	C 39	(Proposal) 3/23/69	TBA
90	Common system of taxation of mergers, divisions and contribution of assets	C 39	(Proposal) 3/22/69	TBA
93	Proposal for Council directive instituting a process of convergence of rates of VAT and excise duties (This proposal replaces the standstill proposal on both VAT and Excise duties withdrawn by the Commission)	C 250	(Proposal) 9/18/87	12/31/92
106	Harmonization of the structure of excises on mineral oils	C 92	(Proposal) 10/11/73	TBA
110	Common rates bands for all harmonized excise duties on mineral oils	C 262	(Proposal) 10/1/87	12/31/92
113	Council Directive on minimum safety requirements for use by workers of personal protective equipment	C 161	(Proposal) 6/20/88	7/1/90
114	Council Directive for measures to encourage improvements in safety & health of workers at workplace	C 141 C 30	(Proposal) 5/30/88 2/6/89	1/1/91
115	Council Directive concerning minimum safety & health of workers at workplace	C 141	(Proposal) 5/30/88	1/1/91
116	Council Directive on Laws relating to personnel protective equipment	C 141	(Proposal) 5/30/88	1/1/90
118	Council Directive amending 77/93/EEC on protective measures against harmful organisms to plant & plant products	C 47	(Proposal) 5/4/88	1/1/89

SIMIS Number	Directive Description	OJ No.	Date of OJ	Implementation Date (1)
122	Proposal directives on the contained use of genetically modified micro organisms	C 198	(Proposal) 7/28/88	TBA
123	Proposal Directives which relate to environment of genetically organisms	C 198	(Proposal) 7/28/88	TBA
124	Green Paper on copyright and the challenge of technology	(88)172		Not Applicable
129	Amended proposal for a council directive relating to the transparency of measures regulating the pricing of medicinal products for human use and their inclusion within the scope of the national health insurance system	C 129	(Proposal) 5/18/88	TBA
136	Further modifications to emulsifiers, stabilizers, thickners for food	C 214	(Proposal) 8/16/88	7/1/89
139	Eighth amendment to 76/769 on restrictions to marketing dangerous substances	C 43	(Proposal) 2/16/88	
143	Legal Protection of Biotechnology Inventions		(Proposal) 10/17/88	12/31/90
144	Oligo-elements Fertilizers	C 304	(Proposal) 11/29/88	1/1/91
150	Amends Council Directive 75/442 on Waste	C 295	11/19/88	1/1/90
151	Directive on Hazardous Waste	C 295	11/19/88	1/1/90
153	Policy Statement and Draft Council Resolution on Global Approach to Technical Specifications and Certification		(Draft Proposal) 11/88	
160	Pesticide residues in Fruits and Vegetables		12/19/88	12/31/89

Annex 3 Documents - Committed to Propose

21	Proposal for the modification of directive 76/895 (maximum levels for pesticide residues in fruit and vegetables)
38	Pharmaceutical products completion of work eliminating obstacles to free circulation of pharmaceutical products
49	Proposal for a directive on the relationship of undertakings in a group

STATEMENT OF MOTOR & EQUIPMENT MANUFACTURERS ASSOCIATION

SUBMITTED BY CHRISTOPHER M. BATES, DIRECTOR OF POLICY ANALYSIS

The Motor and Equipment Manufacturers Association (MEMA) appreciates the opportunity to present its views to the Senate Committee on Finance regarding the likely impact of "Europe 1992" on the motor vehicle parts manufacturing industry.

Founded in 1904, MEMA is the oldest trade association in the U.S. motor vehicle parts industry. It is the only association devoted exclusively to representing and servin~ the needs of U.S. manufacturers of motor vehicle parts, accessories, and allied products.

The European Community (EC) is the third largest U.S. export market for motor vehicle parts after Canada and Mexico, with purchases rising from $.9 billion in 1987 to $1.4 billion last year. The percentage increase in U.S. exports to every EC country except Greece and Italy was greater than the 18% gain in total U.S. exports of motor vehicle parts from 1987 to 1988.

The United States, however, continues to run more than a $2 billion deficit with the EC in motor vehicle parts trade. U.S. parts imports from the EC reached $3.8 billion in 1988, up from $3.3 billion in 1987. This sectoral trade situation contrasts with the very significant progress made last year in reducing the overall U.S. trade deficit with the EC.

U.S. parts makers also have a large and growing direct investment position in Europe. Reliable data on the total book value of such investments is not available. However, survey data from the International Trade Commission's 1987 study of the industry show that annual capital expenditures by subsidiaries and affiliates of U.S. parts manufacturers in the 4 largest EC countries increased from $84 million in 1982 to over $200 million in 1986.

As these data show, our industry has a very important stake in ensuring that Europe remains a healthy market for U.S. exports, and that new trade or investment barriers are not erected.

U.S. parts manufacturers have mixed views on the implications of "Europe 1992" for their businesses. Some firms with manufacturing operations or a strong distribution and sales network in Europe are optimistic that further EC market integration will promote a healthier European economy and lead to new market opportunities. Others, however, question this view or have reserved judgment until the details of EC policy become clearer.

There is broad concern within our industry that U.S. parts exporters could encounter greater difficulties in selling to the EC in the 1990s. These concerns are based on:

(1) expectations that EC auto policy, while aimed at restricting market penetration by Japanese producers and their local affiliates, will indirectly harm U.S. export interests;

(2) the belief that harmonization of EC industrial standards and testing/certification policies will facilitate internal EC trade, but could discourage imports from non-member countries such as the United States;

(3) the likelihood that European parts manufacturers will become vastly more competitive regionally, and aggressive globally, due to the "Europe 1992" process.

There are several areas of EC regulation or policy which firms in our industry are monitoring closely as part of their strategic planning activities. These include: EC auto industry trade policy; EC technical standardization, testing and certification policies; customs and other border regulations; and competition (antitrust, merger and acquisition, and product liability) policies.

The balance of this testimony focuses on EC auto industry trade policy and technical standardization/testing/certification policy, which are likely to have the greatest direct impact on manufacturers in our industry.

EC AUTO INDUSTRY TRADE POLICY

While the specific terms of future EC auto industry trade policy are still under discussion, the general direction of the policy debate is reasonably clear.

—The EC is expected by most U.S. and European industry observers to negotiate a regional export restraint agreement with Japan to replace current member state limitations on Japanese auto imports. Any new EC-wide restraint is unlikely to be removed until EC auto exports to Japan increase to roughly half the level of Japanese exports to the EC.

—To encourage new vehicle assemblers entering Europe to make substantial use of local suppliers, the EC is expected to establish stringent rules of origin as a condition for free trade in finished vehicles among member countries. Japanese vehicle

producers already have read EC sentiment clearly, and several have announced plans to achieve 80% content in vehicles they assemble in Europe.

These policies, if implemented as expected, will put pressure on U.S. and other non-EC suppliers of original equipment parts to establish or expand their manufacturing presence in Europe, whether directly or through strategic alliances with locally-based manufacturers. A number of large and mid-size U.S. parts makers already have taken such steps to avoid "Fortress Europe" and take advantage of expected growth in regional demand due to internal market liberalization.

On the positive side, new opportunities may emerge for European operations of U.S. companies with experience in selling to Japanese-affiliated customers in North America. While assembly capacity for Japanese-design vehicles in Europe lags far behind that in North America, it is projected to reach 500,000 units or more by the early 1990s.

On the negative side, EC automotive trade policy could result in:

(1) diversion of some Japanese vehicle exports to non-EC markets, including the United States;

(2) discouragement of large-scale imports of U.S.-built, Japanese-design vehicles; and/or

(3) reduced long-term opportunities for U.S. exports of original equipment automotive parts if EC rule of origin requirements are set at an excessive level (a minimum of up to 80% is under discussion)

Although the EC is not proposing to raise its external tariff on imports from non-member countries, EC tariffs on both vehicles and parts are significant, and are higher than U.S. or Japanese tariffs. In conjunction with more stringent rules of origin for automotive products, therefore, EC tariffs are likely to discourage parts imports from the U.S. and other non-EC countries to a greater degree than in the past.

HARMONIZATION OF EC STANDARDS AND TESTING/CERTIFICATION POLICIES

Through regional standards bodies (CEN/CENELEC) the EC is seeking to harmonize member country standards for industrial products based on a new concept of "essential requirements," rather than detailed design standards. EC members would then be required to accept products exported to them by other member countries which meet these newly defined "essential requirements."

The EC has pledged to rely upon existing international standards (ISO/IEC) in developing these standards, where feasible. However, we believe this gives the EC considerable room for maneuver.

CEN/CENELEC also is drafting a proposal to establish an EC-wide product testing and certification regime. The intent is to develop a system of lab accreditation and third-party testing as a complement to manufacturers' own internal quality assurance and testing/self certification programs.

This approach offers the potential for additional EC regulation of products produced within the Community as well as those exported to it.

Moreover, non-EC manufacturers do not have adequate access to the EC standards development process, which is far less open and transparent than those used by ANSI, ASTM, and SAE in the United States.

Finally, the "mutual recognition" concept may not apply uniformly or automatically to products made outside the EC. The EC is likely to insist on reciprocal treatment from the United States and other non-member nations, particularly if EC-wide acceptance of foreign-generated test data or product certifications is our goal. Thus, U.S. exporters may derive only limited benefits from the new harmonization approach.

Because of these concerns, MEMA is working in cooperation with other interested groups to improve U.S. industry's access to the EC standards development process. We are encouraged by recent statements by leaders of CEN and CENELEC which suggest they are willing to work with ANSI and other leading representatives of the U.S. standards community to address some of these concerns.

IMPACT OF EC-92 ON THE GATT URUGUAY ROUND

The direction and pace of the EC's implementation of its single market program will have important repercussions in the GATT Uruguay Round negotiations.

On the most general level, concerns have been voiced that the EC will focus primary attention on the "Europe 1992" initiative and will not make an adequate commitment to the multilateral negotiating process. With the basic framework for the GATT negotiations now firmly in place, the Uruguay Round should now enter a

more active phase. By the end of this year, therefore, the United States should have a much clearer sense of the EC's commitment to GATT negotiations in Geneva.

The current debate over establishment of an EC-wide restraint on Japanese auto exports and regional rules of origin on automotive products will have a direct impact on the GATT negotiations on safeguards and non-tariff measures. The "safeguard" negotiations will include efforts to increase GATT discipline on "grey area measures," such as "voluntary" export restraints. The non-tariff measure talks are expected to include negotiations on a more uniform multilateral approach to rule of origin requirements.

MEMA, as an active participant in the USTR/Commerce Department trade advisory program, will monitor developments in both the "Europe 1992" and GATT Uruguay Round arenas to ensure that proposed policy decisions and negotiated agreements do not hinder export opportunities for U.S. motor vehicle parts manufacturers.

MEMA ACTIVITIES REGARDING "EUROPE 1992"

MEMA has enjoyed close liaison with counterpart associations and industry leaders in the EC for many years. It is now taking an even more active role in monitoring the progress of "Europe 1992," analyzing key developments, and reporting findings to members on a regular basis. Analysis of "Europe 1992 issues and related outreach to the U.S. parts manufacturing industry will remain a focal point of MEMA's international program activities in the foreseeable future.

To date MEMA activities in this area have included:

(1) collaboration with counterpart associations and industry leaders in Europe and Japan to gather information and gain a broader perspective on the "Europe 1992" process;

(2) participation in and information exchanges with various U.S. industry standards groups and broad private sector task forces considering the impact of "Europe 1992;"

(3) analysis of new EC Directives of interest to MEMA members as they are issued; and

(4) extensive outreach to U.S. auto parts manufacturers through participation in several industry conferences and direct reports to members.

A growing number of manufacturers in our industry are looking carefully at how "Europe 1992" will affect their market position in Europe. For exporters in particular, however, there are no clear answers regarding appropriate strategies at this stage.

EC implementation of new and planned Directives may vary significantly from stated intent and thus will require careful monitoring by both industry and government. MEMA believes *sustained* U.S. surveillance of the "Europe 1992" process is therefore essential to protect U.S. interests, particularly with regard to exports.

STATEMENT OF THE NATIONAL ASSOCIATION OF MANUFACTURERS

NATIONAL ASSOCIATION OF MANUFACTURERS,
May 25, 1989.

Hon. LLOYD BENTSEN,
Chairman, Finance Committee,
U.S. Senate, Washington, DC

Dear Mr. Chairman: On behalf of the National Association of Manufacturers and our Chairman Richard E. Heckert, I want to express our appreciation for the recent hearing that you held on the European Community Internal Market program (EC-92). On the same day that the hearing was held, NAM's international committees passed a resolution on EC-92. I would like to request that this resolution be added to the record of the hearing.

I would also like to comment on some statements made by one of the other witnesses, Mr. Matthew Coffey. In his testimony and discussion with the committee, he indicated that major problems faced by small exporters in the U.S. included uncompetitive U.S. export financing and differences in competition policies which may impede U.S. producers who seek to compete in the E.C.

I would like to call the committee's attention to the strong support provided by NAM in the past for the export trading company law, that reduced antitrust constraints on smaller U.S. companies and allowed them to cooperate more in export markets. And the NAM remains strongly supportive of increases in U.S. official export financing, the record of which has been extremely weak in the 1980s. We

have always made the point that this would benefit small U.S. manufacturers as well as large ones.

I would also request that you add this letter to the hearing record.

Yours sincerely,

STEPHEN COONEY,
Director, International Investment and Finance.

Enclosure.

NATIONAL ASSOCIATION OF MANUFACTURERS RESOLUTION ON THE EUROPEAN COMMUNITY 1992 INTERNAL MARKET PROGRAM

The plan to complete implementation of the European Community internal market by 1992, known in shorthand as EC-92, will have major effects on NAM member companies. Both U.S. exports to the European Community and the operations of U.S. companies with investments in the E.C. will be affected.

As indicated in its recent report, *EC-92 and U.S. Industry*, the National Association of Manufacturers believes that the overall impact of the EC-92 program will be to encourage strong and dynamic growth, in an increasingly deregulated E.C. market. The results, we believe, will be beneficial for industry in Europe, and for European workers and consumers. We also believe that if this program is successful, it will provide a positive stimulus to world trade growth.

But as this NAM report showed, U.S. industry has a series of specific concerns regarding the outcome of specific issues in the EC-92 process. Decisions on these issues could either enhance or reduce the opportunities for U.S. companies' trade and investment in the E.C.

NAM represents the full spectrum of U.S. industry. This includes the largest U.S. industrial companies, which may have major production facilities in Europe, in addition to exports into that market. NAM also has over 9,000 smaller manufacturing member companies, with fewer than 500 employees each, that typically service foreign markets through exports. This resolution has also been developed with the active participation of the NAM Associations Council, representing 144 cooperating sectoral trade associations. The major issues for U.S. companies as outlined in this resolution therefore reflect the full range of NAM members' concerns. These major issues are:

Technical and Environmental Standards and Certification—U.S. industry is encouraged by the "new approach" being taken to develop Europe-wide technical standards. Consonant with E.C. obligations under the GATT Standards Code, we expect that any new standards developed on a Europe-wide basis will be transparent and compatible with international standards. New Europe-wide standards should not create de facto trade barriers. Similarly, the establishment of an E.C. regime for product testing and certification should not lead to any discrimination against products made or services offered outside Europe. Where appropriate, there should be negotiations for mutual recognition of testing and certification. procedures.

Public Procurement—U.S. industry is encouraged by the strengthening of existing E.C. rules on the opening of member government procurement and by the proposed extension of E.C. rules to the sectors presently excluded from GATT or E.C. discipline. We hope that the E.C. would also initiate discussions as soon as possible looking toward inclusion of these sectors in a more effective GATT Government Procurement Code. We also must express concern about the possible world trade impact of several provisions in the excluded sectors directives, including the local content rule, use of transitional measures and treatment of non-E.C. suppliers based on "equal access."

Reciprocity—The European Commission has stated that intra-E.C. market opening initiatives should be extended to non-E.C. producers only insofar as E.C. trading partners provide equivalent access to their markets for E.C. producers, and insofar as market access rules are not already determined by GATT obligations. It has also indicated its willingness to negotiate this question of reciprocal access in multilateral as well as bilateral forums. In recent revisions proposed in the draft Second Banking Directive, the E.C. also declared that it would adhere to a national treatment standard as the basis for reciprocity. NAM supports U.S. negotiations with the E.C. in all available forums, with the primary goal of strengthening an open, multilateral world trade system. In any case, we expect that the E.C. will continue to apply national treatment to U.S. exports as established under Article III of the GATT, and we hope that national treatment will be the basis of reciprocity in all areas where it is applied by the E.C.

Rights of U.S. Companies—NAM members are concerned that some proposals in the EC-92 progam could include a qualification of the general principle of national treatment of U.S.-owned companies in the E.C. as established under Article 58 of the Treaty of Rome.

Rules of Origin, Local Content and E.C. Trade Policies—Completion of the internal market may result in the replacement of national import quotas, whether formal or informal, with E.C.-wide measures. Any effort to do this should be consistent with the GATT. Only in that way can the United States be sure that its GATT interests will be considered and that appropriate consultations will take place. Moreover, there is an ongoing development of E.C. rules of origin of traded goods and evolution of local content rules that determine whether goods are of E.C. origin, for the application of specific antidumping penalties. NAM members are seriously concerned that the evolution of such policies could lead to development of general local content rules, which have previously been opposed by both the United States and the European Community in the present GATT negotiations.

Sectoral Trade Issues—The NAM is particularly concerned with the future development of E.C.-wide common commercial policies and other sectoral initiatives regarding automobiles, telecommunications, information technology and, as recently announced, aerospace manufacturing. Such policies may include new restrictive quotas, local content rules and direct subsidization of commercial research, development and manufacturing production. Certain aspects of proposed policies in these areas have broad implications for general trade policy.

Intellectual Property—NAM members strongly support the enhancement and completion of a Europe-wide system of protection of trademarks, patents and copyrights. We believe that this will strengthen international intellectual property protection.

Social Dimension—NAM members with investments in the E.C. are strongly interested in the issue as to whether EC-92 should be accompanied by new initiatives in employment and social affairs, and what type of initiatives would be most effective under the EC-92 program.

Competition Policy—NAM members believe that establishment of E.C.-level control over mergers and acquisitions, particularly large-scale multinational combinations, can expedite the development of improved cross-border efficiencies and economies of scale within the E.C. Such an E.C.-wide policy, however, should replace existing national approval authority for such mergers within the E.C., and not merely add an extra approval procedure to existing national competition policy controls.

Monetary Policy—NAM members with business operations and transactions in the E.C. are encouraged by the decision to eliminate all controls on capital movements within the E.C., and by consideration of other measures designed to reduce the costs and difficulties of intra-E.C. financial transactions.

Potential Issues—NAM members are especially interested in future proposals which may be developed regarding establishment of an E.C. system of export controls of strategic products and technology, and reduction of defense procurement barriers within the E.C.

The NAM supports U.S. government consultations with the E.C. and, where appropriate, negotiations, on the issues above that are directly relevant to U.S. trade interests. Such discussions could be on a direct bilateral basis or in the GATT. In particular, NAM reaffirms its support for U.S. participation in the GATT Uruguay Round, as well as in the strengthening and expansion of GATT codes on non-tariff measures.

Furthermore, NAM calls upon the U.S. government to strengthen the support that it provides U.S. exporters in Europe. The Department of Commerce, the Office of the U.S. Trade Representative and the State Department have so far done a commendable job in identifying and disseminating information on EC-92 issues. It is our view, however, that more resources need to be devoted to this task, especially by strengthening the U.S. and Foreign Commercial Service.

This resolution will also be presented directly to the Delegation of the Commission of the European Communities. More detailed policy positions on the issues listed above may be developed, as E.C. policy proposals are themselves developed more fully.

(Adopted by the International Trade Policy Committee, International Investment and Finance Committee, National Association of Manufacturers, May 10, 1989)

STATEMENT OF THE NATIONAL CONVENIENCE STORES INC.

SUBMITTED BY V.H. VAN HORN, PRESIDENT AND CHIEF EXECUTIVE OFFICER

Mr. Chairman and members of the Committee, I am Pete Van Horn, President and CEO of National Convenience Stores Incorporated based in Houston, Texas. I am here today not only on behalf of my company, which employs approximately 6,000 workers in the state of Texas, but also on behalf of the National Association of Convenience Stores, of which I am a former Chairman of the Board. NACS is a trade association representing 2300 convenience store companies operating 54,000 stores and providing over half a million jobs.

Although NACS represents convenience store companies of all sizes, I'd like to take a few moments to profile the typical NACS member. According to a 1987 survey, 60 per cent of the 2300 NACS retail members are companies with 10 or fewer stores. Those companies own an average of just over four stores and employ an average of approximately 30 employees.

Fully 88 per cent of NACS retail members are companies with fewer than 50 stores. Those companies own an average of roughly 10 stores and employ on the average fewer than 100 employees.

Given those numbers, I feel secure in saying that few, if any, industries have felt the impact of Section 89 as harshly as the convenience store industry since the law took effect on January 1. On behalf of the industry, I want to thank you for holding these hearings, and we hope the Committee recognizes that changes in Section 89 are imperative.

The purpose behind the law was, as NACS understands it, in two parts. Congress believed that the bill would encourage employers to extend their health and life insurance benefit plans to more employees and not limit coverage to higher-income workers. The bill also had a revenue-generating purpose, as tax revenue would be generated from discriminatory benefit plans as well as from plans that do not meet the new qualification rules for tax-free status.

After fewer than five months of operating under the law it is not clear that it effectively serves either purpose. Indeed, NACS believes that the two goals were mutually exclusive from the beginning. If the law succeeds in inducing employers to offer benefits to more employees, benefit plans will become non-discriminatory and will generate no revenues for the federal treasury. On the other hand, if employers continue to eliminate benefit plans entirely to avoid the costs and uncertainty of discrimination testing, tax revenue will increase, but so will the number of uninsured Americans.

The convenience store industry is concerned over aspects of both the nondiscrimination tests and the qualification rules of Section 89. Although there seems to be broad support for changing the discrimination testing, we are concerned that the qualification rules will be left alone. We echo the comments of many other business groups that have objected to Section 89, and we would like to explain the effects of the law on our industry.

The convenience store industry does not operate on a high profit margin. Any added costs of doing business are either passed on to the consumer or, if absorbed by a company, result in the elimination of unprofitable stores and the jobs they created.

Section 89 imposes substantial costs on the convenience store industry. Simply determining whether a covered benefit plan discriminates in favor of highly-compensated employees can cost even a small company $10,000 or more. That cost will be duplicated for each separate plan a company offers. As the law says that even a slight difference in benefits provided under a plan can have the effect of treating one plan as two or more, the costs imposed by Section 89 on small companies are far more disproportionate to the purposes it serves. Many smaller companies will not be able to survive the costs imposed by the law.

It is obvious from my opening remarks concerning the size of the average convenience store company that NACS is concerned as an association about the impact of Section 89 on small businesses. We do not believe, though, that the unfairness of the law is limited to smaller companies. Large convenience store chains also are affected by Section 89 in ways that hurt their ability to complete in the marketplace. Larger companies have more employees and may offer a greater variety of benefits than small companies. As a result, their costs of discrimination testing are magnified.

In addition, many convenience store chains operate in more than one state or more than one geographic region. Section 89's penalties for not offering comparable benefits to lower and higher income employees fails to take into account regional

difference in costs of living and other economic considerations. In order to compete for workers in some parts of the country, a chain may have to offer costly fringe benefits to prospective employees. Penalizing the same chain for not offering similar benefits to workers in other parts of the country where competition for workers is not as high, while not penalizing local food retailers which also may not offer any benefits, can pose an almost insurmountable competitive disadvantage on the larger chain. The result would be to force the larger chain out of some markets and to eliminate jobs from economically disadvantaged regions.

Other federal laws allow for regional differences in compensation. The Davis-Bacon Act, for example, requires federal construction contractors to pay their employees no less than the wages that are prevailing for similar work in the same "city, town, village, or other subdivision" in which the work is to be performed. Similarly, the Walsh-Healey Government Contracts Act and the Service Contract Act require other federal contractors to pay employees no less than the wages that are prevailing for similar work in the same "locality." The failure to take that into account in Section 89 imposes substantial hardships on large chains and their employees.

The most devastating impact of Section 89 has been the decision of many companies to discontinue their employee benefit programs entirely rather than face the uncertainty and potentially disastrous tax liabilities of the law. Obviously, this approach takes benefits away from lower income employees who may not be able to afford to buy their own, and defeats one of the purposes of the law. Further, there is no guarantee that even higher-paid workers will use the additional income to purchase health insurance. The result will surely be an increase in the number of uninsured Americans.

The only way to resolve completely the problems created by Section 89 is to repeal it in its entirety and start on a clean slate. Section 89 has so many fundamental complexities and inequalities that any effort to amend it short of a complete repeal would be meaningless and would only add to, rather than subtract from, the severe problems it creates. NACS favors a complete repeal of Section 89, and would be willing to work with Congress to develop a workable alternative.

The qualification rules, although not as complex as the non-discrimination rules, are probably more inequitable. The effect of those rules is to tax all benefits received by even low income employees through no fault of their own if their employer made a mistake in implementing the plan. A failure to comply with the qualification rules will result in the taxation of all benefits received under the plan. An employee earning $13,000 per year at a company which provides benefits to lower-paid workers may find that every dollar received in benefits is taxable income. The Internal Revenue Service regulations establish limits, based on income, that any individual will be required to include in taxable income, but those limits appear nowhere in the statute. NACS believes that the qualification rules are too harsh, too burdensome, and unnecessary to serve the law's purposes.

The bills introduced to date in the Senate to amend Section 89 fall far short of providing the necessary relief from the burdens imposed by the law. Both of those bills—S. 595 and S. 654—leave intact the vast majority of Section 89 and merely carve out minor changes in its provisions. H.R. 1682 also proposes only minor changes in Section 89.

Short of a complete repeal, NACS must agree with the approach taken by Mr. Rostenkowski in the House. His bill, H.R. 1864, proposes to rewrite completely the discrimination provisions of Section 89. Although NACS does not agree with the provisions in Chairman Rostenkowski's bill imposing an excise tax on employers for plans that fail to satisfy the qualification rules, and although NACS would like the opportunity to work with the Congress in developing the final bill, NACS is in agreement that a total revision of the discrimination rules is necessary to make the law workable and less burdensome on employers. If that is done, NACS believes Section 89 will no longer induce employers to discontinue health benefits in favor of higher salaries for high income employees, and will achieve some of the purposes of the original bill without imposing undue costs on employers.

Thank you, Mr. Chairman and members of the Committee.

STATEMENT OF THE NATIONAL FOREST PRODUCTS ASSOCIATION

INTRODUCTION

The National Forest Products Association is a national trade association representing over 700 companies and organizations with forestry operations in every

state. Our members are engaged in timber growing, harvesting, processing, manufacturing, and distribution. The wood products industry employs over 700,000 people, and in 1988 had sales of an estimated at $70 billion. Exports of solid wood products account for 8% of all U.S. production, double of what they were just ten years ago.

Major improvements in manufacturing productivity since the early 1980's have made the industry very competitive in the world market place, gaining the U.S. forest products industry impressive positions in many world markets. The United States is the largest producer. and exporter of softwood plywood, the second largest producer of softwood products, and the largest producer of commercial hardwood roundwood. We are the third largest hardwood lumber exporter and fifth largest exporter of softwood lumber.

In 1988, the United States became a net exporter of wood products for the first time since 1980, registering a $98.145 million favorable trade balance. Of total wood exports, softwood products made up 81% and hardwood products made up the remaining 19%. Softwood logs comprised 39% of exports, softwood lumber 21%, hardwood lumber 12%, wood chips 5%, and softwood plywood 5%.

The U.S. wood products industry has become increasingly concerned about the European community's EC plan to create a barrier-free market by the end of 1992. EC legislation dealing with standardization may have a profound impact on U.S. exports since harmonization directives may be framed so as to hinder the entry of U.S. products into the European market.

In 1988, our industry exported $905 million in wood products to EC countries of which 92% was in the form of processed wood products such as lumber, veneer, plywood, cardboard, particleboard, and other panel products. The largest volume products were hardwood lumber (28%), softwood lumber (26%), softwood plywood (19%), and hardwood veneer (10%) of total exports.

NFPA EC-92 Action Plan Summary

NFPA has been working with the U.S. Department of Commerce, Department of Agriculture, and regional product associations to monitor these developments and analyze the impact for U.S. forest products. The blueprint for action that NFPA has developed includes four steps:

1. to determine exactly what standards, codes, and regulations affect the wood products industry;
2. to evaluate these standards, codes and regulations;
3. to determine how the U.S. industry can best influence these standards, codes, and regulations; and
4. to determine if benefits of EC integration will be extended to non-EC countries, favoring timber producers in Europe through standards which accommodate their products and discriminate against American products.

The U.S. forest products industry's primary obstacle at present is timely access to the work of the EC standards committees, and the working documents produced by these groups at a point in the procedure in which a meaningful response can be made. The United States Trade Representative (USTR) and Commerce have established procedures to address problems that arise from the EC-92 harmonization effort, and have asked industry for advice on problem areas. The industry would like to respond to government requests, but has been unable to do so because of a lack of information. Somehow we need to gain access to the CEN committees and their working documents. Once these are in hand, we can then evaluate their impact on our industry and advise our government of any problem areas. NFPA plans to continue working with Commerce and USTR to insure that our industry is kept abreast of developments in the European Community.

Recommendations to the U.S. Government

(1) NFPA recommends that at a minimum, the U.S. government press for U.S. participation, or, second best observer status, in CEN meetings, allowing our industry to respond to problems as they develop.

(2) In addition the U.S. government should encourage the EC to make working papers available in a timely manner, and develop a program for responding to problem areas identified in draft codes and standards.

(3) We would also recommend that the government press for reciprocity of test data and certification programs by mutually acceptable bodies worldwide.

Background: Elements in the Action Plan

IDENTIFICATION

On July 1, 1987, the Single European Act came into operation. This calls for the completion of a single market for the European Community by December 31, 1992 to be achieved through the issue of regulations and directives.

Regulations come into effect immediately, and most often address important issues which require immediate action. A directive must be implemented within all European Community countries in a fixed period of time.

One such directive is the Construction Products Directive which aims to eliminate barriers to trade in the construction industry caused by differing national rules and regulations, while maintaining acceptable levels of health and safety. The broad policy requirements of the Construction Products Directive will be achieved through the use of CEN developed codes and standards specifying the use and supply of building materials, including timber. The EC is the main contractor of CEN and has given it the task of developing a complete set of standards to be used in the new legislation to appear in 1992.

The CEN has evolved as the main regulatory body affecting the forest products industry within the EC. CEN is the world's largest regional standards group, with members from both *EC and European Free Trade Alliance (EFTA) countries.* These include in the EC: Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, and the United Kingdom; and in the EFTA: Austria, Finland, Iceland, Norway, Sweden, and Switzerland.

The directives issued by the following CEN committees will impact the U.S. wood products industry:

CEN/TC 33—technological tests for doors, windows and shutters
CEN/TC 38—methods of tests for wood preservatives
CEN/TC 91—particleboard, formaldehyde determination
CEN/TC 103—adhesives for wood and derived timber products
CEN/TC 112—wood based panels
CEN/TC 124—timber Structures
CEN/TC 127—fire safety
CEN/TC 175—grading standards for non-structural timber

Design codes being drafted for Europe are called EUROCODES. EUROCODE 5 is the design code for timber, and will be supported by standards being drafted by CEN/TC 124.

Phyto-sanitary regulations are another area with the potential for impact on U.S. wood products exports. The Commission of the European Communities Council Directive 77/93/EEC set up a Community plant health regime to harmonize prohibitions and restrictions applicable to imports of plant and plant products to prevent the introduction or spread of harmful organisms.

The list of product categories covered by harmonization is growing and the U.S. industry needs to monitor formation of new committees and draft directives being developed by existing CEN bodies as well as those which are a result of 77/93/EEC.

The U.S. government has pressured the EC to make draft directives available to the U.S. industry for comment. Starting this month, the European Community is scheduled to begin releasing draft standards on a monthly basis to U.S. firms through international standard-setting bodies.

EVALUATION

NFPA plans to establish an industry committee to provide technical expertise to evaluate and analyze the various Eurocodes as they are developed. This committee will include technical support staff from regional product associations, NFPA's Market Support Council, and wood products companies to review technical materials, recommend a coordinated industry response when appropriate, and serve as a conduit for gathering and disseminating information.

ACTION

While the United States is prohibited from direct participation in CEN committees, the EC has directed CEN to adopt specifications developed under the auspices of the International Standards Organization (ISO) whenever possible. NFPA has been successful in influencing international standards development as it relates to fire testing through its participation in ISO working groups on fire. With the ISO representing one of the few organizations where the U.S. has direct input, the in-

dustry could consider expanding its participation to other ISO committees related to timber.

Once the U.S. industry reaches agreement on how the new standards will impact the European import market, information can be supplied to appropriate individuals and strategies developed for discussions between relevant United States and EC government agencies.

EFTA DETERMINATION

It is clear that the six EFTA countries will have certain links to the EC standardization process which are not open to other countries. The countries are important in the global timber industry and are one of the U.S. industry's main competitors in Europe. Standards for obligatory use by the EC are prepared by CEN through majority voting.

While no other countries are in as favorable a position as EFTA, evaluation of the standards should reveal any comparative advantages which might then be addressed in bilateral or multilateral fora.

EC-92 Issues

1. The potential benefits of common EC product standards to U.S. exporters:

The adoption of uniform product standards and codes within the EC could benefit the U.S. wood products industry provided that the standards are reasonable and do not contain provisions that impede the acceptance of U.S. products. It will be necessary to obtain and analyze the standards to make this determination. NFPA has not been able to do this to date because it does not have access to the work of the CEN committees.

2. Transparency of the EC standards setting process:

The EC has stated its intent to base European standards on those promulgated by the International Organization for Standardization (ISO) where available. ISO standards are still being developed in several key areas which could impact U.S. wood products' acceptance. In the absence of completed or exact ISO standards, CEN may adopt new and potentially conflicting standards to fulfill its mandate by 1992. The U.S. wood product industry actively participates in the ISO, but in spite of U.S. requests has not been allowed to participate in European standards activity (CEN) nor has it been given observer status.

3. Desirability of unofficial American observers in European standards organization:

Direct observation of the proceedings at CEN meetings would give the U.S. the ability to respond quickly to detrimental proposals. Representatives from the U.S. wood products industry are eager to participate and would encourage the EC to allow such participation.

4. Role of European industry in setting EC-92 product standards:

The European industry appears to be very influential in setting CEN standards for wood products. As mentioned, EFTA countries have special links to the EC standardization process not open to other countries by virtue of their direct participation in CEN. These countries are also among the U.S. timber industry's main competitors in Europe.

In the U.S., the standards setting bodies, ASTM, ANSI, etc. must have the committee membership balanced between producers, users, and general interest to avoid dominance by one group. We are not aware of any similar requirement in CEN.

5. EC willingness to provide for mutual recognition of test data:

At this time it is unclear whether the EC will accept U.S. data and certification. Ideally, the uniform testing requirements being developed under the auspices of the ISO would be adopted by the EC. However, a complete set of ISO tests may not be available in time to fit the EC-92 schedule of harmonization. It is also unclear whether testing in the U.S. in compliance with CEN standards will be acceptable to the EC.

STATEMENT OF THE UNITED STATES COUNCIL FOR INTERNATIONAL BUSINESS

Basic Elements of the United States Council's Position on the Single Market

The E.C.'s program to complete its internal market by December 31, 1992, will be of enormous consequence to Europe, the world economy as a whole and to the U.S. economy and American companies. The United States Council supports this initia-

tive and believes that it will result in a more open and dynamic market which will benefit U.S. companies ready to take advantage of the opportunities it will offer. The E.C.'s single market program is the acceleration of a process that began in 1957, with the signing of the Treaty of Rome which established the European Economic Community. Then as now, the goal is to create a common market free of restrictions on the movement of goods, services, people and capital. Both the U.S. Government and American business have consistently supported this goal, stressing the importance of creating a dynamic European economy, and recently, of emerging from the stagnation that pervaded Europe in the 1970s and early 1980s.

As long as this is achieved through deregulation and growth, it is up to U.S. business to take advantage of the market opportunities afforded. However, U.S. companies would be opposed to "harmonization" at the E.C. level which resulted in more burdensome regulation or bureaucracy and to measures that resulted in discrimination against firms of non-E.C. origin investing in or exporting to the Community.

A. THE U.S. STAKE

U.S. business is interested in the Single Market initiative because of the impact it will have both on the European marketplace in which it operates and on the environment for trade and investment worldwide. "1992" is one of a number of major developments, including the Uruguay Round, the U.S.-Canada Free Trade Agreement, and implementation of the U.S. Trade Act, that make this a time of unprecedented opportunity for creating an open world trade and investment system. It is also a time of great risk, if any of these developments are perverted, and if protectionist tendencies should prevail.

American business and the U.S. economy have an enormous stake in the Community. According to the National Association of Manufacturers and the National Planning Association, the E.C. is the largest recipient of U.S. exports and investment. The E.C. accounts for 25% of U.S. exports ($60.6 billion in 1987). This is slightly greater than exports to Canada, and far greater than to Japan, other East Asian countries or Latin America.

In addition, a full 40% of U.S. foreign investment is in the E.C. (about $122 billion in 1987). In 1986, U.S. affiliates in the E.C. employed 2.5 million people and their sales were estimated at $430 billion. In some sectors, they represent a substantial portion of the market. In the pharmaceuticals, sector, for example, sales by European subsidiaries of [illegible]

American based firms represent 27% of the market, which is greater, for instance, than German companies' share of this market. Moreover, these investments play an important role in U.S. exports. It is estimated that in 1986, $18 billion of $53 billion total U.S. exports to the E.C. were accounted for by exports to U.S. subsidiaries.

B. OPPORTUNITIES AND CHALLENGES

U.S. companies emphasize the opportunities offered by a single European market, in terms of lower costs, increased demand and potential economies of scale.

Elimination of border controls would reduce costs associated with delays in transporting goods from one country to another. Already, for example, the E.C. has adopted a Single Administrative Document that replaces some 70 different forms required at border crossings. It is estimated that this will reduce transportation costs for companies within Europe by 7%, as well as reduce required inventory stocks. Transportation costs should also be reduced as the road, sea and air transport service markets are liberalized.

Harmonization or mutual recognition of national regulations and standards for goods and services would mean that a product would have to comply with only one set of requirements, rather than twelve, to be marketed freely throughout the E.C. This should in many cases allow U.S. companies to more efficiently serve their European customer base.

In addition, U.S. firms earning licensing fees and royalties in Europe, or which have trademarks to protect, will benefit from new intellectual property regulations that extend high standards uniformly across the E.C.

Growth in the E.C. resulting from integration will mean greater market opportunities for American companies. The "Cecchini report, commissioned by the E.C. anticipates that approximately 5% will be added to E.C. GDP in the medium term, as a result of reduced barriers, with a net increase of about 1.8 million jobs. While some consider these forecasts optimistic, E.C. GNP already rose 3.7% last year, following steady 2% growth over previous years, and more new jobs are being created than at any time since the 1960s.

The principal challenge for U.S. business will be a more competitive business environment in Europe. The impact of integration on U.S. business will vary among industries and individual companies, depending on how well they are positioned to face increasingly competitive European firms. U.S. companies invested in Europe early and have often done business on a Europe wide basis to a greater extent than their European counterparts. It is the intention of the 1992 program to increase the competitiveness of European firms through greater use of the market. Already, European companies are posing new challenges to American firms in a number of areas, not only in Europe but in the U.S. and in third markets as well.

Many U.S. companies, with experience trading and operating in the U.S. market and throughout Europe, are well equipped to meet this challenge and to take advantage of the opportunities discussed above.

C. CONCERNS

At the same time, business is concerned about ways in which discrimination against foreign-based firms could be introduced into this process. While we believe that the overall direction of the program is towards market liberalization, potential difficulties lie in the details of the numerous individual pieces of legislation in the program. Specific concerns have been expressed by the U.S. Council on E.C. measures, as summarized in Part II of this paper.

There is concern, for example, that European standards and regulations on specific goods and services, as well as testing methods and certification procedures, could be established which do not take account of broader international standards or which create new obstacles to imports.

Business would also be concerned if European-wide standard setting resulted in increased regulation or more burdensome bureaucracy. Further, incomplete or divergent national implementation of E.C. Directives could result in the maintenance or creation rather than the dismantling of trade barriers within the Community.

Also, European firms under new competitive pressures could be favored over those based outside the Community through the maintenance of subsidies, discriminatory public procurement practices, and restricted access to E.C. research and development programs.

There have also been concerns about the use of the concept of reciprocity in E.C. legislation. It is not clear if the E.C. will interpret this as requiring national treatment or "mirror legislation" of third countries, in order for their firms to have access to the E.C. market. Also, although reassurances have been received about its meaning as included in proposed measures in the financial services sector, it is as yet unclear how this might apply to other areas.

There are concerns about the impact on U.S. exports and on U.S. markets of application of local content requirements, and how the E.C. will address at the Community level national quantitative restrictions being phased out.

For companies with establishments in the E.C., the Treaty of Rome (Article 58) guarantees that firms established in an E.C. member state shall be treated as member state nationals under Community law. For U.S. companies, it is important that no qualification is made to this general principle in the context of specific 1992 measures.

Pressures for protection will be exerted by certain European business quarters, though on the whole, they seem to take an open, liberal approach.

Also, fear of Japanese competition may lead to measures affecting U.S. interests. The E.C. Commission has identified three major sectors in which problems are expected: automobiles, electronics and textiles. They have also identified two smaller ones: sewing machines and motorbikes. It remains to be seen in what additional sectors problems will be encountered.

CONCLUSIONS

The U.S. Government should continue to support the E.C.'s efforts to integrate its market. At the same time, it should ensure through negotiations at the bilateral and multilateral levels that discriminatory measures are not introduced in the process of integration, and that the E.C.'s market remains open to investment and trade from outside the Community.

We believe that a key element of ensuring that this process results in an open E.C. for U.S. business is to strengthen broader international commitments to liberalization, particularly in the context of the Uruguay Round of GATT negotiations on lowering of tariffs and non-tariff barriers, including agreements on services, intellectual property, and investment, and on rules of origin and local content, as well as

the improvement and extension of the GATT Agreement on Government Procurement.

We are pleased to see that agreement has been reached on continuing negotiations on the items not agreed at Montreal, allowing the negotiations to proceed.

Last, it should be recognized that any measures taken by the U.S. Government which could be construed as protectionist, for example, certain aspects of the Trade Act, or "Buy America" legislation, could provoke protectionist reactions at this critical moment in liberalizing the system both in Europe and globally. This makes achievement of liberalization on a multilateral basis all the more important.

STATEMENT OF THE U.S. SEMICONDUCTOR INDUSTRY ASSOCIATION (SIA)

The Semiconductor Industry Association (SIA) is pleased to have the opportunity to submit written testimony for this hearing on "Europe 1992."

The Semiconductor Industry Association, which represents U.S.-based semiconductor manufacturers, was created in 1977 to coordinate industry energies in solving international trade problems. In particular, SIA has focused on finding solutions to problems involving unfair trade practices and unequal access for American semiconductor products in world markets. SIA's main concern continues to be public policy issues that affect the industry's ability to remain competitive internationally. However, the range of SIA activities have expanded to include a broad spectrum of industry topics, such as occupational health, safety, and environment; industry statistics; public communications; and industry-oriented publications. The industry's interest in fostering competitiveness through cooperative ventures has led to the creation of a basic research consortium, the Semiconductor Research Corporation (SRC) and the formation of SEMATECH. SIA's most recent initiative is an exploration of ways to stimulate reentry by U.S. manufacturers into production of dynamic random access memory semiconductors (DRAMs), a critical sector in which the U.S. industry has been decimated, due in large part to unfair Japanese trade practices.

SIA member firms represent over 90 percent of the U.S. industry. A list of member companies is attached.

In response to the Subcommittee's request, SIA's testimony will address some of the industry's concerns with regard to the 1992 "single market" effort in Europe. We would emphasize that this is a very preliminary assessment; we don't know enough yet about the policy directions that Europe appears to be taking to reach any firm conclusions as to what the ultimate effects of the 1992 effort will be on U.S. companies operating in Europe. However, there have been a number of recent actions taken in Europe which have had negative repercussions for U.S. companies, and these events have caused us to take a closer look at what is happening in Europe and to be concerned about some of the signals that the Community appears to be sending in the electronics area.

The European market is a very important market for U.S. semiconductor and electronics producers. Europe as a whole is one of the world's largest markets for semiconductors. Total semiconductor consumption in Europe in 1988 amounted to $8.253 billion. U.S.-based semiconductor producers were the largest suppliers to the European market, with sales of $3.697 billion (44.8% of the total European market). This compares with U.S. sales in 1988 of only $1.934 billion in the Japan market, which is now the world's largest semiconductor market (Japan's consumption of semiconductors was $18.108 billion in 1988, of which the U.S. share was 10.68%). Clearly, the United States industry has a strong interest in maintaining access to the European market, our largest export market, and we would be very concerned if we thought that the Community was trying to emulate the Japanese "closed market" model.

As you are aware, the much-heralded 1992 "single market" effort is an enormous legislative undertaking which is being implemented through increased centralization of authority in the hands of the EC Commission. Almost 300 directives will be considered as part of the EC effort to create a unified internal market of 320 million consumers. To date, we understand that the Commission has enacted some 100 directives. Among the objectives of the 1992 effort are to improve the competitiveness of EC firms, particularly in strategic sectors such as electronics; and to promote job creation through increased investment in Europe.

The creation of a single EC market certainly has the potential for many positive gains. However, the 1992 effort has also raised concerns as to whether the political and economic tradeoffs involved in that effort may result in increased barriers to non-EC companies' access to that market and/or increased pressures on non-EC

companies to shift jobs, investment and technology to Europe to maintain their market presence.

One objective of the 1992 effort—to improve the competitiveness of EC firms—is nothing new in the electronics area. The EC has a long history of protection and promotion of EC electronics production. Concerns about the European industry's international competitiveness and EC dependence on foreign suppliers in critical information technologies have led to the use of policy tools which have been quite effective in increasing the competitive strength of EC producers. We estimate that over $1 billion/year is spent by the Community on government-subsidized microelectronics research and development and joint manufacturing efforts. These efforts have resulted in, among other accomplishments, a European 1-megabit DRAM capability. These same concerns have also led to European calls for a better "balance" in areas such as semiconductors, as European producers continue to lag foreign producers in share of their own market. The European Electronic Component Manufacturers Association (EECA) has been forthright in calling for subsidies, maintenance of the current tariff level on integrated circuits (ICs) "realistic" duty suspension procedures, "equitable" European origin rules, and similar policy measures aimed at improving the competitive position of European ICs vis-a-vis foreign chips.

In furtherance of its efforts to promote European electronics production, the European Community has erected a number of barriers—both tariff and nontariff—to imports. The EC has high tariffs on electronics products compared with the other major electronics-producing nations. For example, while the United States and Japan have eliminated duties on semiconductors and computer parts, the EC maintains tariffs on both—14% in the case of semiconductors.

More worrisome than tariffs which, although they are a trade barrier, are at least transparent and less distortive than most other forms of protection, are non-tariff barriers. Most of SIA's concerns in connection with 1992 have to do with what appears to be a trend toward increased use by the EC of non-transparent, non-tariff means to achieve policy objectives related to protection and promotion of European electronics industries.

This apparent trend has begun to manifest itself recently in the form of a number of initiatives which on their face may not seem to be objectionable—many can be justified for non-protectionist reasons—but which in their operation, or in their *interaction with other measures,* have had the effect (intended or not) of imposing competitive disadvantages on non-EC companies.

For example, on February 2, the EC adopted a new rule of origin for integrated circuits (ICs) under which the origin of the semiconductor is to be determined by the location of "diffusion" operations (wafer fabrication). Therefore, to obtain EC origin, a semiconductor will now have to contain a die (the silicon "chip" itself) fabricated in the EC. Prior to this change, assembly operations in the EC sufficed to bestow EC status on ICs. This change in the EC's rule of origin for integrated circuits makes it more difficult for foreign-based companies to obtain EC origin for their products. Other restrictions require (or are interpreted, correctly or incorrectly, to require) a specified percentage of "EC content," the effect of which is to create disincentives to buy semiconductor components from non-EC suppliers—unless they have sufficient investment in the EC to achieve EC origin for their products.

Of particular concern are situations where restrictive measures (e.g., local content rules imposed in connection with quotas, procurement preferences, etc.) are applied to end products containing semiconductors. Such rules may appear innocuous in isolation, but in combination, they can and do operate to create incentives for downstream product manufacturers to buy European, rather than non-EC origin, components. A number of such restrictions currently exist, both at the national level and at the Community level. At the national level, examples of such restrictions include quotas imposed by several countries, including Italy and France, on imports of Japanese automobiles that contain more than a certain percentage of foreign content. There are reports that such quotas may also be imposed at the Community level. The fact that these quotas are being administered to require certain minimum levels of EC content (80% in France) to escape the quotas has an impact on U.S. suppliers of semiconductors, for whom the rapidly growing automobile end-use market is a very important market. The automotive semiconductor market in Europe was about $591 million—approximately 7% of the total European semiconductor market—in 1988. Clearly, restrictions that create incentives for manufacturers to purchase European semiconductors in place of U.S. semiconductors to avoid automobile quotas put U.S. companies at a competitive disadvantage.

At the Community level, such restrictions include special origin rules for a number of consumer electronics products which require a minimum percentage of EC content for the product to obtain EC origin (e.g., 45% for radio and TV receivers

and tape recorders). Similar rules are being considered for VCRs and photocopiers. These EC content rules become important when combined with quotas, high tariffs, screwdriver assembly dumping duties or other restrictions on these downstream products, because a manufacturer can escape such restrictions by adding more EC content to its product. Again, this creates incentives for producers of these goods to replace U.S. components with EC-origin parts.

We have received reports that an EC content requirement is effectively being applied in certain dumping cases involving assembly in Europe through the EC's "screwdriver assembly" regulation. The purpose of the screwdriver assembly regulation is to avoid circumvention of antidumping duties through establishment of low-value-added assembly operations in the Community. However, problems have arisen with the way the rule apparently is being applied in combination with other EC content requirements on subassemblies to create pressure to include certain minimum amounts of EC content in the EC-assembled product. This result is not required by the screwdriver assembly rule itself and is contrary to GATT principles. The practical result, however, is that several U.S. companies have already been dropped by Japanese customers in favor of EC sources. Semiconductor vendors are also now being asked to disclose the location of diffusion operations in sales proposals, as well as to indicate what their future plans are to "Europeanize" their product lines.

A recent example will illustrate the problem. A Japanese printer manufacturer told its U.S. supplier that to avoid dumping duties on its printers assembled in Europe under the EC's "screwdriver assembly" regulation, it must "design out" U.S. semiconductors so that boards going into its printers will count as EC-origin rather than Japanese origin. To obtain European origin for the boards, Japanese manufacturers are apparently being told that there must be at least 45% European content in the boards. By replacing U.S. chips with European chips, the European content of the boards can be raised to 45%, and the Japanese manufacturer thereby increases its total non-Japanese content in the finished product to over 40% and avoids the "screwdriver" dumping duty. Note that this is accomplished without actually reducing the number of Japanese parts—Japanese content levels are maintained as U.S. chips are replaced with European chips. The loser in this equation, obviously, is the U.S. supplier.

SIA is concerned that there will be an increasing number of restrictions such as those we have described, with adverse consequences for U.S. exports, in connection with the entire "Europe 1992" initiative. There is a proposed EC directive on telecommunications procurement which would establish preferences for products containing 50% or more EC content (and permit discrimination against products that do not). Furthermore, there are various other EC initiatives that appear to be shaping up more as "industrial policy" measures (i.e., measures intended to force investment in Europe or promote EC industry at the expense of non-EC companies) than market-liberalizing measures.

In conclusion, what many U.S. companies see occurring—and sales have already been lost—as a result of these recent initiatives, is the prospect of a domestic content/manufacturing requirement for electronics products sold in Europe. A domestic content policy—which both the EC Commission and the U.S. government are on record as opposing—would put pressure on U.S. companies to increase significantly their manufacturing investments and technology transfers to the EC, regardless of whether competitive considerations would support such decisions, in the face of discrimination against their products if they do not. U.S. companies would feel forced to respond by transferring jobs, technology and investments to Europe. Those decisions would have important adverse implications for the U.S. economy and the U.S. industry's global competitiveness.

While it may be premature at this juncture to conclude that a "Fortress Europe" is being built in the electronics sector, the trend is not promising—we cannot afford to let it happen. Close scrutiny and further analysis of these developments is clearly warranted. We intend to keep a watchful eye on regulatory developments in Europe and urge you in Congress to do the same.

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