

**THE ADMINISTRATION'S INTERNATIONAL  
TRADE AGENDA**

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**HEARING**  
BEFORE THE  
**COMMITTEE ON FINANCE**  
**UNITED STATES SENATE**  
**ONE HUNDRED EIGHTH CONGRESS**  
SECOND SESSION

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MARCH 9, 2004  
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**TUESDAY, MARCH 9, 2004**

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

The hearing was convened, pursuant to notice, at 10:00 a.m., in room SD-215 Dirksen Senate Office Building, Hon. Charles E. Grassley (chairman of the committee) presiding.

Also present: Senators Snowe, Kyl, Thomas, Baucus, Graham, Jeffords, and Lincoln.

### **OPENING STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM IOWA, CHAIRMAN, COMMITTEE ON FINANCE**

The CHAIRMAN. We welcome everybody here. Senator Baucus and I are happy to convene this hearing on the President's trade agenda to look at accomplishments and challenges facing the Bush Administration. We welcome you, Ambassador Zoellick. This is a very important time in U.S. trade policy.

Just a few years ago, as you recall, Congress empowered President Bush, through the passage of trade promotion authority, to negotiate trade agreements, with the idea that trade strengthens our U.S. economy. Today, Congress has implemented two free trade agreements under this procedure. Three more are at our doorstep: the Central American Free Trade Agreement, U.S.-Australia, and U.S.-Morocco.

Each of these agreements carries substantial benefits to the U.S. economy. Negotiations continue to create a Free Trade Area of the Americas, and hopefully to conclude a new round of trade talks in the World Trade Organization in the near future.

There are also a number of bilateral negotiations under way that will require our continued attention. In my mind, we are now at somewhat of a crossroads of U.S. trade policy.

While we have made some progress in leveling the playing field with our foreign competitors through the passage of U.S.-Chile and U.S.-Singapore agreements, there clearly remains a lot more for Congress to do.

With enough political will, Congress could—and I repeat, could—implement as many as three free trade agreements this year. Congress is likely to see even more free trade agreements ready for implementation next year.

However, Congress could be considering a new World Trade Organization agreement in the not-too-distant future, and this is most important. This negotiation is clearly where we get the most bang

for our negotiating buck, especially for interests that Senator Baucus and I have of agriculture.

Of course, next year Congress will face the issue of whether to extend the trade promotion authority for an additional 2 years. Implementing these agreements and extending trade promotion authority are going to be tough choices.

It's going to take a lot of political courage. Unfortunately, we don't have as much of that as we used to have in the sense that trade is much more controversial than it has been for a long time. This also is an election year and we have some presidential aspirants determined to make trade and trade agreements and economic whipping boy.

Now, this may be very good politics—not all over the country, thank God, but in some areas of the country. But regardless of where it is practiced, it is disastrous economic policy. That does not mean that we should discount workers' concerns about trade and their role in the world economy, but at the same time we should not pander to these fears for short-term political gain.

I was surprised to learn last week that some of my colleagues made a political decision to load up the FSC/ETI JOBS bill with all kinds of political message amendments designed to stoke workers' fears about the economy.

I hope they will reconsider this approach when we return to that bill after our spring recess. Sanctions are in place and American manufacturers need a shot in the arm. American manufacturing's future is too important to be a playing game of politics.

I said earlier we are at the crossroads. Political leaders can play on people's fears, throw up barriers to trade, seek to isolate America from the global economy, or we can do what we did in the 1980's, rise to meet the real challenges of the world economy.

I know President Bush and the team leader, as Ambassador Zoellick is, is not going to run from these challenges. My message today is very simple. If we are going to sustain the prosperity of this country's experience over the past 50 years, we must remain steadfast in our support for negotiating more open markets than we presently have. We simply cannot allow our economic policy to be guided by politics up here.

Mr. Ambassador, we have a lot of important issues to discuss, and I thank you for being here and for your testimony.

I now turn to Senator Baucus.

**OPENING STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR  
FROM MONTANA**

Senator BAUCUS. Thank you very much, Mr. Chairman. Thank you, Ambassador Zoellick, for appearing before us today.

Mr. Chairman, you have given us a pretty comprehensive overview of trade policy on many issues that we face, and I deeply appreciate that. I know that all those listening do as well. I think that the primary focus today should be on one issue, and that is jobs. That, I think, should be the primary goal of our trade policy, that is, to keep and create jobs.

Some might have other goals. I disagree with that. I think that our primary goal in trade policy and trade agreements, and enforc-

ing trade agreements, should be the creation of jobs and retention of jobs.

In the last 3 years, we have lost about 3 million jobs in this country. Some of those are moving overseas. Increasingly, the jobs moving overseas are higher-paying and higher-skilled jobs.

Every day now, it seems that there is news on the subject of offshoring. We all hear it in the press, see it in the press, and hear it from our colleagues in Congress, and most importantly we hear it from our constituents, manufacturing plants moving to China, call centers moving to India.

Even jobs in State employment offices are not immune. In some States, unemployed workers have to call someone overseas to find out what their State benefits are.

There has been a lot of debate on whether this is good or bad in the big economic picture. Let us face it, offshoring jobs has people worried, and legitimate worries of the American public cannot be dismissed.

There is no silver bullet. There are lots of pieces to the offshoring puzzle. Tax policy, education, health, research and development, to name a few. But today we should talk about trade, about how to use our trade policy to create and keep good jobs here at home.

I believe it is a question of priorities. First, we need to reexamine how we choose partners for free trade agreements. I remember when we were debating fast track and the trade agreement of 2002, all of us here in the Congress, in the business community, the White House, we were all talking about exports, about competitiveness and economic growth. In short, we were talking about jobs.

But somewhere along the line that goal got hijacked. Instead, as the General Accounting Office recently concluded, foreign policy considerations now dominate this administration's selection of trade partners. That is a mistake.

I do want to commend you, Mr. Ambassador, for continuing to push forward on the WTO Doha Round. The collapse of the new round in Cancun was a serious setback and we need to continue to make WTO a priority.

But I also agree that the WTO cannot be the only game in town. We need to move ahead on different fronts as well and particularly we need to negotiate free trade agreements. But we are now negotiating a number of agreements that will have very limited effects.

I want to be clear. I welcome more open trade with any country willing to make a comprehensive commitment. But negotiating those agreements takes a lot of resources and our negotiating resources at USTR are not unlimited, as you well know, Mr. Ambassador.

American workers, farmers, businesses deserve the most bang for their buck. They deserve trade deals with commercially significant markets that will generate job growth at home.

Second, enforcement. Negotiating free trade agreements is not the only way to get market access. A case in point is India. We all know that India is benefitting enormously from the offshoring of service sector jobs from the United States.

But the United States is not getting anything in return. Why? Because India has such a closed market and India is certainly one

of the leading countries holding back progress toward greater market access in the WTO.

The administration's proposed solution is to negotiate a free trade agreement with a country next door to India, Sri Lanka. Total U.S. exports to Sri Lanka last year were about \$143 million. So, after we expend lots of negotiating resources and wait out a 10- to 15-year implementation period, we might have free trade with an economy that has a current commercial worth to the United States of \$143 million a year.

By contrast, American businesses in 2002 lost more than twice that much, that is, \$342 million in retail revenues just from software piracy in India. India has made commitment under the WTO TRIPS agreement to protect intellectual property rights, but what are we doing about enforcement of that agreement?

How can we spur innovation and create jobs at home if we let people overseas steal our intellectual property rights, \$13 billion worth of software alone in 2002? Would our limited resources not be better spent combatting piracy than negotiating agreements with tiny markets?

I think we need to reassess our priorities, and that is why, today, I am requesting that the GAO conduct a review of how we enforce the more than 250 trade agreements that the United States currently has on the books.

This study, which will be completed in the year 2005, will help Congress and the administration better assess how well we do at enforcing trade agreements and how to allocate our resources to achieve the best possible results. By best results, I mean, first and foremost, jobs, because that is what Americans need.

Third, we must ensure that U.S. companies can compete on a level playing field. But we should reject the notion that we must lower standards in this country to compete. Instead, we must look to raise standards in the countries we trade with.

The Trade Act of 2002 made tremendous progress in this regard, but we must continue to race to the top. When it comes to standards on labor and the environment, incredibly, the debate in the last 3 years has been about what this administration, what this Congress, not our trading partners, will accept.

Our trading partners will accept higher standards in order to gain prestige and access that a trade agreement with the United States gives them. I know that. I have met with trade ministers. I have talked with them about these issues.

But we do not negotiate with them, we negotiate with ourselves. We negotiate about what this administration and this Congress will accept, not what other countries will accept. I think we have got to do better.

In any event, Mr. Ambassador, I look forward to working with you and this committee as we focus on priority issues in this year's trade agenda. I hope we can be efficient and keep our eye on the ball, namely, how we keep more jobs and create more jobs in the United States of America. Thank you.

The CHAIRMAN. Mr. Ambassador, whatever lengthy statement you have, we will be glad to put in the record and have you give any sort of summary you want to give right now, and then we will go to questions.



**STATEMENT OF HON. ROBERT B. ZOELLICK, U.S. TRADE  
REPRESENTATIVE, WASHINGTON, DC**

Ambassador ZOELLICK. All right. Thank you very much, Mr. Chairman, Senator Baucus, and Senators Thomas and Jeffords.

First, I just want to start by thanking the members of the committee for their advice and support over the past year, and over the past 3 years. As I think all of you have mentioned, we certainly recognize that the benefits of trade are a highly contentious subject, this year of all years. My written testimony covers this in greater detail, and I do not presume to cover it this morning.

As I told Senator Baucus yesterday, other than a few asides in a speech he gave recently at Brookings, I thought he outlined a number of the challenges quite well. So what I thought I would do, Mr. Chairman, would be to just give you a little overview on where we are on getting to your questions, based on these slides that I think you have in front of you.

As the first page mentions, our strategy is to try to expand trade, to try to create growth, opportunity, development, and fairness through a series of multiple initiatives. On the trade front, as both the Chairman and Senator Baucus mentioned, we are trying to move on multiple fronts to be reinforcing globally, in the hemisphere, and bilaterally.

Along with that, the full commitment about enforcing law and agreements, as I will discuss in a moment, but also the need to help those that lose jobs along the way. This committee led a very important process in joining with the Trade Act of 2002 in expansion of the trade adjustment assistance. Last year, that provided some \$1.3 billion of assistance, with about 200,000 eligible workers.

That includes a new pilot program, an alternative trade adjustment assistance. And as the President proposed in the state of the Union, to complement that with a program of JOBS for the 21st century to help link our community colleges with job creation.

But by moving on multiple fronts, frankly, we need to help all Americans. We need to help our exporters. We need to help people who have adjustment for jobs. We need to help consumers, workers.

By moving on multiple fronts, we can exert leverage to open the playing field and have a more level playing field. U.S. barriers are relatively low. Our average trade-weighted tariff is about 2 percent. So every time we open up a market with a free trade agreement, frankly, we bring others down a lot more than we do ours. And it certainly strengthens America's hand in other markets.

One thing that I know that probably everybody on this committee, at least those here now, agree with, is given the fact that we are now in a stage of an economic recovery, the absolute worst thing we could do would be to turn to economic isolationism.

On the next page, what I note is that after the Trade Act of 2002, where I had the chance to work with both Chairman Grassley, Chairman Baucus before that, and many members of this committee, you had the confidence to extend trade promotion authority, and we have been trying to put that to good use.

As Chairman Grassley mentioned, we both completed and passed the Singapore and Chile Free Trade Agreements last year. We launched and completed a free trade agreement with Australia. We launched and completed a free trade agreement with five Central

American countries, and this very week we are trying to finish adding the Dominican Republic to that.

We launched and completed a free trade agreement with another moderate Arab-Muslim country, Morocco. We have launched free trade agreements with the Southern African Customs Union in Bahrain, and we have announced intention in the second quarter this year to begin with the Andean countries, Panama, and Thailand.

Now, as part of this, we have also advanced the Enterprise for Asean Initiative, which is an effort to try to give a road map for countries in Southeast Asia about how they can move towards free trade agreements, and do the same with the Middle East, which is obviously an area of both economic and strategic importance to the United States.

And also, in Miami this past year, we established a framework for the Free Trade Area of the Americas to try to move that towards concrete results and create incentives for progress.

As the Chairman and Senator Baucus mentioned, in the case of the global negotiations where there is the biggest benefit, the meeting in Cancun was obviously a disappointment. But it is our belief that 2004 need not be a lost year. Let me turn to that, next.

Now, the challenge in the WTO is, you have got 148 economies that you have to bring to a consensus about opening markets for agriculture, goods, and services, trying to boost growth and development.

Now, at Cancun, in the run-up, we did something that was very important. Many of you asked me about this in prior hearings. We finally solved this knotty problem dealing with developing countries and access to medicines for public health crises.

But going beyond that, frankly, a number of you were down there with us. Some countries wanted to posture. They wanted to pocket the proposals. That is not an approach we will take. We are willing to open markets and cut our subsidies if others will, but we will not do it alone.

The so-called Singapore issues, topics like competition policy, distracted from the core agenda. These were not really our issues. These were ones pushed by the European Union, Japan, and Korea. And it was very clear that we are going to have to bring around both developed and developing countries together on agriculture, and that means some cuts from all parts.

Nevertheless, there is a reassessment that has taken place in the months after Cancun. I think that the draft frameworks that were presented there could provide the basis for good work.

So in January of this year, I actually sent a letter to my ministerial colleagues to try to bring a little catalyst for this negotiation. About a week or so ago, I just came back from traveling some 32,000 miles and seeing about 40 of my different colleagues. I think there is a new energy and possibility.

Now, the core, as Chairman Grassley mentioned, is agriculture. We have to be able to eliminate export subsidies for agriculture, and that is primarily a challenge for the European Union.

We need substantial cuts in trade-distorting domestic subsidies. As you know, and you have backed us, and the Agriculture Committees have backed us, and the agricultural constituencies, we are

willing to cut our subsidies if we can get the European Union to cut much closer to ours and get market opening, get market opening not only in Europe and Japan, but also in many of the major developing countries.

We need to combine that with a good package on manufactured goods. Going to the point that Senator Baucus made, a number of developing countries still have some very high tariff levels, so we want to try to use a formula, frankly, that brings their tariff levels down further.

We want to combine that with some sectoral initiatives because there are areas where we could go zero-for-zero for a number of sectors, and increasingly important, a number of non-tariff barriers. This is really important for some of the industries, like autos.

We also need to get more and better offers in the services area, which, as you know, now covers some two-thirds of our economy. What we have suggested, is to drop all the Singapore issues but trade facilitation, because that is the one that is critical to get products through ports and Customs systems and express delivery.

So I do not think this will be easy, but our hope is, frankly, to try to target by this summer the agreement on the frameworks that we were not able to get at Cancun.

But the key steps—and I will be happy to discuss this with you further—are getting the EU, Japan, and others to move off some of those Singapore issues other than trade facilitation and get the EU to agree finally to eliminate export subsidies.

On the Free Trade Area of the Americas, this is a negotiation that was kind of a discussion for some 6 or 7 years. So in the course of Miami, since we are involved in 34 countries, we finally agreed on a framework that I believe has a shot at pushing us forward, and that is to have a common set of rights and obligations for all countries. This would focus heavily on market access benefits, but also a higher level of commitments for those countries that are willing to go further.

Now, as we mentioned, we have a two-track approach to this. We are simultaneously proceeding with free trade agreements with countries in the western hemisphere. And if you look at the number down there, these bilateral free trade agreements are really discussed sort of as a gold standard because they include intellectual property, services, anti-corruption, environment and labor provisions.

And the countries we have already negotiated agreements with or have in the pipeline would now cover some two-thirds of the GDP of this hemisphere, not including the United States.

In terms of other regional initiatives, one of the items that I know we will be working with the Congress this year is on the question of the extension of AGOA, the African Growth and Opportunity Act. This is a trade preference program. It is a one-way program. It has been a very important success.

In the past year, the sub-Saharan African countries, just moving into the trading system, now exported some \$14 billion worth of trade to the United States, and that is a 55 percent increase in a year of slow growth without much in the way of increases. There is a question about whether we can extend that and deal with some of the provisions that expire.

Similarly, in the area of the Middle East, every day you open the newspapers and you read about the security and the questions of democracy and development in the Middle East. So what we tried to outline is a step-by-step program that customizes for the stage of development for countries in the Middle East.

We now have free trade agreements with Israel, with Jordan, and in the past couple of weeks completed one with Morocco, and we are working on one with Bahrain. So if you look at the map, you have got one in the Magreb in North Africa, you have got a couple now in the heart of the Middle East, the Levant, but also Bahrain in the Gulf.

And these become important models because, as we made this announcement, we are now bringing countries to the first level of work with us, what we call trade and investment framework agreements. We now have those with Algeria, Egypt, Saudi Arabia, Tunisia, Yemen, Kuwait, and over the next couple of weeks, Qatar and the United Arab Emirates want to sign with us.

In addition, we have some countries that are not even members of the WTO yet, like Saudi Arabia, so we want to try to focus them and getting them in the first stage.

We have a similar approach with Southeast Asia. That is a big market for the United States. We now have a free trade agreement with Singapore. The second quarter of this year we will begin one with Thailand. That is a very important market for both manufacturers and the agriculture community.

Frankly, we hope that will be a model for the countries that we have these TIFAs with, Indonesia, Philippines, Brunei, and now Malaysia is also interested in signing.

So if you look at the bilateral agenda, we have Singapore and Chile done. These are good models. Of course, each has to be customized. We also have Australia done, which we launched in March, completed in less than a year; the five Central American countries; as I mentioned, adding the Dominican Republic, Morocco; five countries we are negotiating with in the Southern African Customs Union, Botswana, Lesotho, Namibia, South Africa, and Swaziland; Bahrain, and then, as I mentioned, the Andeans, Panama, and Thailand.

And to go to one of the points that Senator Baucus mentioned, when you add these agreements together, they account for the third largest export market to the United States and the sixth largest economy in the world.

Now, people often ask, and I know I have discussed this with Senator Baucus, well, what about other countries? Well, let us kind of look at the list. NAFTA, our free trade agreement partners in North America, cover about 35 percent of U.S. trade.

Now, then you look at the next biggest trading partners and you have got the European Union, which does not want to negotiate a free trade agreement with; Japan and Korea are very big, but they will not open up their agriculture market, and knowing the two gentlemen in the center of the dais, you know we would never do a free trade agreement without opening up agriculture markets; China is a big player, but right now we have got to focus on WTO implementation.

So as you look at the remaining countries, the free trade agreements that we have done or have in process cover 35 percent of the exports of the remaining set. If you include the Free Trade Area of the Americas, you actually are up to 50 percent.

So part of the challenge is, and this is a topic Senator Baucus and I have discussed, is that I cannot force someone to negotiate a free trade agreement that is not willing to move to free trade. But what we can do, is create a dynamic where they start to see their neighbor having free trade and they start to realize what they are missing.

Now, let me talk about some of these in particular, since they, I hope, will be before the committee later this year. Australia is our first free trade agreement with a developed country since Canada.

The National Association of Manufacturers and the Chamber of Commerce have dubbed this a manufacturing FTA because it would achieve immediate duty-free treatment on 99 percent of U.S. manufactured exports.

We already have about 150,000 jobs with our exports to Australia, and exporters now estimate this would gain us about \$2 billion in additional exports, and about \$2 billion in national income.

I know I worked on a number of items. In particular, Senator Thomas and I managed to get soda ash down to zero, and I know it is something we talked about.

It expands markets for services and farmers. All U.S. farm exports are duty-free from day one. This includes some important benefits for pork producers that I know Senator Grassley has always had his eye on, and I just saw a report from the Pork Producers Council that looks at just a few of the agreements we have done this year and notes that they should produce an added value of \$3.50 a hog. So, you can see these things are starting to add up.

Of course, we had some sensitive agricultural market issues with beef, dairy and sugar. As you know, we did not include sugar. In beef, we had a very long phase-out with various safeguards, slow quota increase. We tried to take care of the dairy people as well, because we did not touch the tariff.

We just increased the quota basically about \$40, \$50 million of imports a year. Their key item, they mentioned for us, was not changing the tariff.

I worked with Senator Kyl on this pharmaceutical benefits system, which I know we may want to talk about a little further, but I think is an important development. I appreciate his help; he went to Australia on this with us. And even though this was a developed country, we included environmental and labor provisions, as we do in all these free trade agreements.

Now, CAFTA. I know this one has been more controversial, but look at the starting point. Today, under the Caribbean Basin Initiative, which is a one-way preference agreement, U.S. tariffs on Central American goods are low, and indeed almost 80 percent of their goods come into the United States duty-free and we do not get anything in return.

So one of the benefits of CAFTA is, we get a two-way street. As you see, with CAFTA, more than 80 percent of U.S. manufactured goods would be duty-free on day one. Frankly, that is a tall order

for a number of these developing countries. I am really pleased with the courage they have in opening markets.

More than half of the current U.S. farm exports would be duty-free immediately. So what does this mean for you, in reality? It means beef, cotton, wheat, soybeans, fresh vegetables, processed goods, wine. We also got good openings in terms of pork, poultry, rice, corn, dairy, dry beans, and vegetable oil

Now, in exchange we did open our sugar market very modestly, but I want you to know what modestly means. The amount of opening that we gave in terms of our added sugar quota amounts to 1 day's production in the United States.

The increased access amounts to 1.2 percent of U.S. production and, after 15 years, that rises to the number of 1.7 percent. We did not touch the tariff. It does not affect the sugar program.

In terms of textile and apparel, another very important issue, we use the yarn-forward rule that the Congress developed in a lot of these preference agreements. And what this means is, we open duty-free if they use either U.S. or local yarn.

Now, we added some provisions called cumulation provisions that will allow people to use certain woven fabrics from Mexico and Canada if they allow us to do the same.

The reason why this is very important, is that if you look at this market, what it is really going to be competing with is not one another, it is going to be competing with China.

The question is whether we can create an integrated North and Central American market to be able to compete. We added very strong anti-circumvention provisions.

As you look at the agreement, you will see that, when we do this in the past, we sometimes allow a certain amount of fabric from third parties to come in. It is called TPLs. In this case, we only did that for Nicaragua for a limited period of time, just because of the nature of its apparel industry.

We have very strong IPR standards and protections, very important for our knowledge industry, a point that Senator Baucus mentioned. We are opening all service sectors, including telecommunications and insurance. A key issue with these countries, they had a lot of limits on your distribution, who you could do business with, and we cleaned all those up.

Very important anti-corruption rules, good governance rules, strong transparency. Frankly, the labor and environment provisions go beyond Chile and Singapore. And here I want to thank Senator Baucus and his staff, because they worked closely with us. We added some citizen petition rules that, frankly, had not been in other agreements.

We could go into them in detail if you want, but they allow development of a factual record, allow follow-up on items. We have environmental cooperation agreements and we have added some milestones in monitoring, and we added an appeal to the investor state issue.

One last point on these countries. A number of you were in the Congress 5, 10, 15 years ago and you remember the debate with Central America with civil wars and guerrillas crossing borders and killing one another. You now have five fragile Central Amer-

ican democracies working together and they are looking to the United States for a chance.

They already have a relatively open market. But why do they want to open their market the rest of the way? Because they want investment. They want to integrate. So, I urge you to look at this, because I believe it has got economic benefits, but it also, frankly, does have political benefits.

Central America is a region we often ignore, to our peril. Then when we turn our head, something breaks, out and the next thing you know you have got blood being spilled and that is not in America's interest.

In the case of Morocco, this package is the best-ever developing country package we have on market access: 95 percent of the goods are duty-free on day one. We get to expand some good export opportunities for U.S. agriculture. That is, frankly, what took us another couple of months on this agreement. We wanted to make sure we took care of wheat, beef, and poultry.

We have broad openings of service markets and they see this is in their interests because they want to create a regional hub. We have got new protections for U.S. investors, strong IPR and anti-corruption rules, again, labor and environment working with the ILO.

And, as I mentioned, in a world where we are trying to encourage moderate Muslims, tolerant societies, this is a very important development, and a courageous one on their part.

I know there is a large focus on China these days, appropriately so. So on the next page I just gave you a few key facts. U.S. exports to China grew some 75 percent over the past 3 years, even as exports to the rest of the world declined because of slow growth. It is now our sixth largest export market.

But the key point we have emphasized, I think, together, is that its implementation of its new WTO rules cannot slacken. China must open its market for U.S. trade if our openness is going to be maintained. That means complying with WTO obligations on agriculture, IPR, and not misusing tax rules or standards.

Now, China's response has been positive in some areas. They have addressed some systemic problems. We have record gains in soybeans, about \$2.9 billion of soybean sales. One of the reasons soybean prices are as strong as they are is because China is a big purchaser. The same with cotton exports. They are up almost 400 or 500 percent, up about \$750 million.

In addition to solving some of the problems, China has now solved the biotech approval problem from soybeans, cottons, corn and others to come. They have made some openings on financial services and motor vehicle financing, which is a booming business.

They have added some purchasing missions on the manufacturing side, but what we have stressed is that one-off purchases are not enough. We have got to have systemic change.

In April, next month, Don Evans and I will be meeting with an elevated dialogue with one of the vice premiers, Wu Yee, to try to focus on some of these issues. And, as we have demonstrated in the case of textiles and will do with others, we are committed to try to use the safeguards that are part of the WTO agreement and enforcement rules to insist on compliance.

More generally, as both the Chairman and Senator Baucus mentioned, monitoring enforcement is really the day-to-day work of what we do at USTR. I have a morning staff meeting where we go around the world and we focus on, what are the specific steps we can do to try to open markets.

Now, I just noted here a few examples, because probably they are useful for you to have: successful cases against the dairy market in Canada; pork with Mexico; apples with Japan; IPR and patents with Argentina; autos with the Philippines; pending cases we have with Mexico with rice and telecommunications. This is one that we have already won and it has not been publicly released.

The industry calculates this is about \$500 million, so you can see these do have pay-offs. In the EU, we now have panels formed on biotech. This is the geographic indicators. I know the Chairman has had a leading role in this and I know, Mr. Chairman, you were asking me recently, they have just formed the Biotech Panel. So, we hope that they have the hearing on that this spring and hope for a decision by the end of the year.

The same with textiles. We have got a lot of sensitivity on our textiles here. The Egyptians, who are a bigger textile producer, were not playing fair, so we brought an action against them. We worked with Kent Conrad, who is not here right now, on wheat with Canada.

But what I also want to emphasize to you is, this is just part of the set of tools. Let me give you a very practical example. Just last week, we managed to re-open the beef market after the BSE problems in Mexico. That is about \$589 million sales. That is big sales for our beef industry.

Now, how did that come about? Well, it came about with Ann Veneman talking with her counterpart, the agriculture minister, but, frankly, me also spending a lot of time with the former foreign trade minister about why they needed to follow the sanitary and phytosanitary rules, good science, and the fact that lack of beef and poultry was now increasing protein prices in Mexico. So, this is just an example of the type of thing that, frankly, we do as our bread and butter.

Now, there is another side to this. Here, I want to, in particular, thank the Chairman and Senator Baucus for helping us with this FSC issue. We cannot be a scofflaw. Frankly, we lost that FSC case after a number of rounds almost 2 years ago.

Now you are going to start to see the EU increase taxes on American exporters unless we get that repealed. That is a fact of life. You cannot stop it, I cannot stop it.

We can try to fight these cases as long as we can, but we are going to have others like this. We have got the Byrd amendment, which we are in arbitration on the amount. The 1916 Act, which is an old antitrust act that has now been used against the company, and that will open up retaliation.

We have got some small ones that would not be hard to change. Section 211 basically deals with blocking trademarks. We almost won the case, but there is one little change that has to be made. And another one on hot-rolled steel, where all we have to do is get a slight change in Department of Commerce authority. So, frankly, it helps us get others to follow the rules if we follow the rules.



Looking ahead, as I think everybody on this committee has mentioned to me at one point or another, it is clear that, given the economic uncertainty in this country, we need to help people manage through change.

One thing is sure. Economic isolation will not work. That will just kill jobs and opportunities. Americans, given the dynamism in this economy, can be big beneficiaries of openness and global growth and development. It means more choices.

It means more jobs that you will see created over time. It means lower prices, and it means higher-paying jobs. Our export industries pay, on average, about 13 to 18 percent higher than other jobs.

So, we need to use the WTO negotiations, our free trade agreements, other trade initiatives to try to level the playing field, spur growth and development. As I mentioned, our trade barriers are already relatively low. Something that I spent a lot of time with, I am sure would help this committee, is we have got to get U.S. businesses to explain some of this to their employees.

There are a lot of people benefitting from this out there. There are about 6.5 million jobs created through in-sourcing, foreigners who are investing in the United States. I have got the list of your States that have got some pretty sizeable job creation. But you do not hear much about that. You just hear about the other side.

We need to combine this with monitoring and enforcement of agreements, targeted use of safeguards, reliance on the unfair trade laws, and following the rules ourselves.

As both the Chairman and Senator Baucus mentioned, the other side of this is, if you are going to have an economy that can adapt for change, you have got to help people starting with good schools, you have got to help people with worker retraining possibilities, portable pensions, and lower taxes so people can save their own hard-earned dollars.

The key to America's success as an economy has been our flexibility and our dynamism, but that requires helping people adjust to change.

One more point, though. That is, a world where poor people lose opportunity is not a world where the United States will prosper, either. In a world where people have lives of destitution and they do not have a chance to improve themselves, that will not be a world where the United States, frankly, prospers. Over the past decade, trade has helped some 140 million people around the world lift themselves out of poverty.

So, thank you, Mr. Chairman. I would be pleased to answer your questions.

The CHAIRMAN. Thank you very much.

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

The CHAIRMAN. We will have 5-minute rounds. The order, as of now, would be: Grassley, Baucus, Thomas, Jeffords, Kyl, Snowe, and Graham.

The first question comes out of frustration because there is a lot of out-sourcing. Maybe there would be disagreement about the economic impact of it, but a job loss is a job loss, so it gets everybody's attention.

The frustration comes from the fact that, right now, it is a big political issue, so that affects all of us who are political leaders. You hear Senator Kerry and Senator Edwards making very strong comments about it.

Then I suppose the frustration does not come from their comments. The frustration comes from the fact that when you read and hear what their answer is, everybody can agree. For instance, one program I saw, their answer was, well, we have got to do more job retraining. I do not think any of us are going to disagree with that.

But I do not see, from people that are complaining about it, a silver bullet. I do not think there is a silver bullet. But, yet, it is a frustrating sort of thing when these things are brought up.

I do not have a single town meeting where there is not something brought up about out-sourcing. I had an opportunity to read an article by former Secretary of Labor Robert Reich, where he spoke about the necessity for retraining and acceptance of the fact of life, that the markets work this way and you have to respond to the markets.

So, all of this is very common sense to me. But the solutions that people have, including what I might have, would not be a silver bullet, but I hope that my response is a little bit more commensurate with the rhetoric I use compared to what some of the candidates for president are using. So, this is the environment we are in, so I would just explain that environment, the frustration I have.

But look at India, as an example. They have tariffs on poultry, 108 percent; tariffs on textiles, 55 percent; tariffs on equipment, 51 percent. Now, I do not know whether workers expect government to pass some law saying a job cannot leave the country or whether they are really asking for the equality that comes through trade agreements to level the playing field.

I think the latter works, but we do not do a very good job of selling the latter, and we leave people with the impression that we can pass a law and say that Company X cannot export a job if they want to.

So my question to you is, how do we address workers' concerns about out-sourcing and international trade? More fundamentally, how would we achieve more reciprocal trade relationships with countries that are problems? I guess I would highlight India, because it has gone from manufacturing to China now to concerns about IT jobs in India, as an example.

Ambassador ZOELLICK. Thank you, Mr. Chairman.

I certainly know out-sourcing is a very serious concern, and I think it deserves a serious discussion. I will maybe just start it today because I know it is one that is going to go on. It is a challenge, I think, because what you see are two sides of the same coin.

On the one hand, you see developments in technology and service industries that offer some tremendous opportunities, and the United States has been very quick at taking advantage of some of those opportunities. But it also involves change, and that can mean difficulties for people.

As I think both of you have said, any time somebody loses a job, the key is to try to help them get back on their feet. It is not only an economic question, it is a question of dealing with families and

anxiety. But I think the challenge is, how do you help people in a way that does not hurt and kill other jobs?

The United States is a major exporter of services. We have a \$60 billion surplus in terms of exporting. As the President always reminds, we only represent 5 percent of the world's public. If we want to have 95 percent of the market, we need to keep open for others.

The interconnections are much stronger than people think. U.S. companies with foreign affiliates now account for about 58 percent of our exports, so the companies that do business overseas are also exporting overseas.

It is clear that economic isolationism will not work. I think one has to be very careful about bureaucratic interventions that will increase prices for people. Obviously, the focus is opening new markets and to let entrepreneurs create jobs, and also, frankly, make the United States more attractive foreign investment.

I mentioned, you have got 6.5 million jobs created in this country through foreign investors through in-sourcing, and you certainly do not want to take bureaucratic steps, or taxes, or other things that stifle that opportunity.

Along with it, I think, as this committee has focused in passing the Trade Act, you have tripled the trade adjustment assistance. The President announced a JOBS for the 21st Century program that would link community colleges more closely with local sourcing needs and suggested about \$500 million for that. And, fundamentally, I think from all, whether a policy or political side, you just cannot rest until you have got growth that creates jobs for all people.

Now, particularly on India, Mr. Chairman, I was just there about 2 or 3 weeks ago. Actually, there was an article in the Wall Street Journal, I think, yesterday that talked a little bit about this. The point that I emphasized to the Indians is, if we are going to remain open for them, it has got to be a two-way street.

Now, India has historically been a very closed economy. It has been one of the most closed economies in the world. But it is changing, so there are players in India that start to see the interest in the international economy.

Our exports increased last year about 21 percent. It is up to \$5 billion. One of the things that I initiated about a year ago was to create an Office of South Asia in USTR, because I had a sense that this was going to be an emerging issue and it was something that I wanted to have a full-time person try to focus on how we could develop some networks to help open that economy.

We have had two good ambassadors there, Ambassador Blackwell, who has come back to Washington, who has been working on Iraq, and David Mulford, who many of you know is at the Treasury. I have spoken to them because part of the key will be creating allies within India to support openness and create business alliances.

One of the points about India that I think we can continue to work on, Mr. Chairman, is while they have high bound tariffs under the WTO, they have been bringing down their applied tariffs. They are still too high, but they are much lower. If you look

at what India does, it often brings those down in budget resolutions or budget acts.

In some ways, it is almost easier for them to take them unilaterally than in terms or part of a negotiation. That is an area where I think, again, we need to try to target where we have some particular export needs and see if they can try to lower tariffs.

The last point is on the Doha agenda, which we have all talked about, it has been no secret, India has been one of the more difficult players. The more we can send a message to India that, frankly, they also have to step up to the plate to try to make this successful in manufacturing, in goods, agriculture, and services, the more critical it would be.

I would just say one last point, because this relates and connects to your out-sourcing point. What I said to the Indians when I was asked about the out-sourcing issue, is that it is a complicated issue here.

Obviously there is a balance of interests, but frankly the Indians have absolutely no right to complain because they do not belong to the government procurement code in the WTO, which sets an obligation in terms of if you are going to have certain procurement procedures. Frankly, they are not that liberal on the services side.

So, it is a good example of, if countries around the world that are emerging economic powers want to get the benefits of the system, they are going to have to contribute to the system.

The CHAIRMAN. Thank you.

Now, Senator Baucus?

Senator BAUCUS. Ambassador Zoellick, I want to associate my remarks with the Chairman with respect to jobs and opening markets in India and just using our trade policy a little more aggressively than we have in the past. I also want to thank you very much for highlighting the need to get the FSC/ETI replacement legislation passed.

Penalties are accumulating daily and I am quite surprised, frankly, at the lack of sense of urgency in this Congress to get that replacement legislation passed so American companies are not paying those penalties on products going over to Europe. I thank you for indicating how important it is that Congress pass that legislation.

I would like to discuss with you the TAA, Trade Adjustment Assistance, program. As you well know, it does apply to persons who lose their jobs, their manufacturing jobs, on account of trade. It gives those people the ability to buy health insurance.

Do you support extending that to service workers? That is, people who lose their service jobs on account of trade?

Ambassador ZOELLICK. Well, Senator, as you and I have discussed, I think you have been a very important leader on this one and this may be another area where you are showing some important leadership.

I think that is something that we should examine very closely, as you and I have discussed. I have tried to do a little checking about what coverage there is now. I think there may be some coverage if some of the service workers were part of the group that falls through the certification process or their job is sufficiently re-

lated, or I think the Department of Labor is now looking to see, if they are in a support capacity, whether that could qualify.

But I do not know if that is enough. Now, frankly, one needs to look at the cost aspects of this as well. But my personal view is, as I said before, one way or another, through this program or others, you have got to help people adjust if you are going to require change.

Senator BAUCUS. I would hope that you would take a good, long, hard look at this. This is very bipartisan in this effort. Senator Coleman and I have introduced this legislation. There are 22 co-sponsors on the bill at this point.

I think it is one area that we could help address this question of offshoring, out-sourcing, however it is called. There are obviously lots of other reasons, lots of other points here, but that is one where we can help. We can help those people who are displaced.

Second, is with respect to legislation that Senator McCain and I have introduced. As you well know, it is the effort to give trade preferences to Mideast countries.

The fact is, almost every FTA, at least a lot of them, have come from countries that were one trade preference countries, that is, you give a country preferences that helps graduate them up to potential free trade agreements.

I know the President has talked generally about a free trade agreement with respect to the Mideast. You mentioned the Mideast in your comments. The administration supports the goal of trade preference provisions, as well as the Andean Trade Preferences Act.

It just seems to me that this is another part of the world where we can grant trade preferences at the discretion of the President. It is not unilateral. At least, it is not mandatory, it is discretionary, and also if countries meet certain conditions that we all think are very appropriate.

Is this not a good idea? It is a step-up toward a potential free trade agreement either with the region, or with a lot of countries in the Mideast. I mean, it is more than TFAs and BITS and all these other agreements which help a little bit, but do not have a lot of commercial effect.

Ambassador ZOELLICK. Well, I think it is a good initiative, Senator, and I compliment you and Senator McCain for doing it. I think it is an important part of the world and we are both trying to work on it together. I would certainly be pleased to discuss with you how best to do it. You have got some sensitive topics in there.

But there are two cautions that I would urge that we try to think about. One, is at Cancun—and I know you backed us there—one of the difficulties we ran into, is some of the developing countries that have preferences then started to be kind of difficult when we wanted to lower overall tariffs because they were losing the benefit of their preferences. So, that is an item I think we need to make sure this does not work against us on that side.

The other part of it, and the reason that, frankly, we have been trying to use the combination of TFAs and free trade agreements, is wherever I can I like to get reciprocal access. I would like to open those markets, not just have it be a one-way street.

As you know, and you helped us pass this again as part of the Trade Act of 2002, we have some preferences for these countries under the Generalized System of Preferences for all developing countries. We, as part of the President's initiative, are trying to work with countries to help them take advantage of it.

But if I had my druthers, Senator, frankly, I would want to try to open up the markets two ways. As I mentioned with Central America, a number of these countries have about 77 percent of their goods come in duty-free, and I would rather be able to kind of equalize that.

So, I found the initiative to be a positive one and I want to try to encourage those of you who take the courage to do these things. So, we should try to work on how to work around those issues.

Senator BAUCUS. Of course we want to move toward reciprocal agreements. That is clear. But sometimes you have to take a couple of steps to get there, and preferences is an approach which, in some respects, has also worked.

In Cancun, it was the FTA countries that were also impeding progress, that is South Africa and most of the CAFTA countries. I understand that GOHA has helped U.S. companies.

Ambassador ZOELLICK. I think it has. I think it has created a basis for free trade agreements. So I think the question is getting that balance and deciding kind of the focus of our capital and energies here.

Senator BAUCUS. Thank you.

The CHAIRMAN. Thank you, Senator Baucus.

Now it is Senator Thomas' turn, then Senator Jeffords.

Senator THOMAS. Welcome. We have been talking a lot about India. As you know, we worked together for a long, long time to get that temporary restraining order lifted on soda ash. So, I appreciate that.

You mentioned Mad Cow disease in Mexico. What is the prospect and outlook with respect to the Pacific countries, Japan, China?

Ambassador ZOELLICK. Well, I raised this when I was in Japan as well. I finished this long trip. I was there primarily for the WTO. An interesting thing is happening in Japan. They are now running so short of beef, that one of their favorite meals, beef pot, they do not have the beef to be able to bring in. And Australian beef is too stringy. So, you are actually getting some consumer response.

Senator BAUCUS. Where is the beef? [Laughter.]

Ambassador ZOELLICK. Yes. Where is the beef? That is right. It is here, and we have got to get it there.

The Japanese, after they had their Mad Cow outbreak, required testing of every animal. As you know, our cattlemen believe that is too much of a step. So, one of the things that we hope to try to do, is by opening the Mexican market to help try to show others that they really need to follow the sound science standards.

Now, Secretary Veneman and others of the administration are looking at some follow-up steps in terms of feed and other actions based on her international report. We will take that back to the Japanese and try to press them to reopen that market based on those steps.

Senator THOMAS. I see.

Ambassador ZOELLICK. And Korea will, I think, follow very closely to Japan.

Senator THOMAS. Those are best potential markets, no question. Someone talked to me at home the other day about steel, the cost of steel had gone up considerably and a lot of the junk steel, or the wrecked cars and this and that that result in steel are going to China from this country. What do you know about that?

Ambassador ZOELLICK. Well, I can say the President's safeguard worked. It gave the industry a time to restructure, and now you are finding steel prices going up. One of the reasons they are going up, and this is the other side of the global economy with China, is China is buying a lot of steel. We sold about \$1.1 billion of iron and steel to China last year, and about 60 percent of it is scrap.

So what you find, Senator, is if you are in the mini mill industry that uses scrap as your raw material, you are worried about your increased cost of prices, so you are raising prices. So, New Core and others have raised their prices some 30 percent.

If you are in the integrated business it is much better because you do not have that as your overall material because you make the inputs for your integrated rolled steel.

Frankly, I think, as we have seen, it would in some ways be an oddity if, for a couple of years, we put barriers on steel in this country and then we put barriers on what we export in terms of steel.

So, I think that really what we have seen with the steel industry as a whole is its return to health, and I hope they treat their customers reasonably so that, in the next cycle, their customers will also treat them reasonably.

Senator THOMAS. This is a broad question. We work on all this, and you do great work, and all this sort of stuff. But, yet, our trade deficit, balance of trade, continues to be stronger every year. Is that just the nature of things? Are we always going to import much more than we export?

Ambassador ZOELLICK. Well, Senator, the trade figures are driven primarily by relative growth, who is growing more. If you are growing more, you are buying more. So even though we are not pleased with the condition of our economy, when you grew 4 percent last year and much of the world is growing slower, you are buying more. It is also caused by exchange rates.

You know there has been some adjustment in exchange rates. It is also caused by, frankly, the investment flows to the United States because the money that comes into the United States is, in a sense, financed by—it is the other side of the trade equation.

What is striking when I looked at these numbers, is that if you look at the manufacturing trade deficit in recent years, 82 percent of the increase in our manufacturing trade deficit is caused by lower exports, not increased imports. That would be consistent with the idea that you are not having enough global growth.

So, this is the other side of the growing China and India situation. As they grow more, they will buy more, which should help us reduce this if we can get their markets open.

It is possible to get a zero deficit. We did it in 1990–1991 with the recession. But I am not sure that is the way we want to approach it. Or if you go back and look at the 1930's at the time of

the Great Depression, we had a trade surplus. So the surplus or deficit numbers, while they are indicators, I am not sure should be the prime goal.

The prime goal should be growth, creation of jobs, productivity, higher wages for people. That should be our goal. I think in this context what we really need to do is try to get others to grow more and then open those markets so we can sell to them.

Senator THOMAS. Thank you.

The CHAIRMAN. Senator Kyl?

Senator KYL. Thank you, Mr. Chairman.

I want to thank you for your testimony, in particular mentioning the work that was done with the Australia Free Trade Agreement and the bilateral discussions that you had there, and the breakthrough made with respect to pharmaceuticals.

I hope that is not only the first such breakthrough with Australia specifically because there is more work to be done there, as you know, but also with other countries, particularly the OECD countries that, like Australia, have similar pricing constraints that end up shifting the burden of R&D for new drugs to the consumers here in the United States.

We are considering the budget right now, which is one of the places where an effort is being made to address this issue in a different way, by treating the symptom rather than the cause, which you attempted to do in Australia, treating the symptom by allowing importation of drugs from Canada.

There will also be legislation or amendments offered to have this government actually try to set prices, involve ourselves in price control, on pharmaceuticals because the cost is too high. We all recognize the cost is too high. But one of the ways of addressing the causes is to get the other countries of the world to help bear part of the burden of the R&D that is so critical to this.

So, my hat is off to your team and the work that you did in at least beginning to address this with Australia. We do not need to discuss it here, but I know there is much more work that needs to be done in further discussions with the Australians.

My question with regard to this is, what efforts do you think we will undertake next with respect to some of our other trading partners to not only do what the Australians have done, but to move beyond that and begin to get directly into the pricing issues in such a way that they can actually better support the R&D efforts that will benefit not just their own people, but everybody around the world.

Ambassador ZOELLICK. Well, again, Senator Kyl, I want to thank you because I know you went a long way to Australia to kind of help us on this and talk to a number of the key ministers, and I think it helped create a good, fair result.

As you said, I think the heart of this question is the prices that people in America pay here and the challenge of those high prices. On the other hand, we have the best health care system in the world, and part of that is because we have the development of a lot of life-saving drugs, that as you look around the world, are not available to other people because they use various methods where they are trying to ration, in a sense, their drugs overall.



Obviously, part of this is going to be dealing with the needs at home and things like the Medicare prescription drug bill that people here worked very hard on. The companies, I know, are focusing on discount cards, which I think is going to be very important dealing with some of the seniors and other concerns.

On the trade side, we have been trying to develop our ideas with the help of you and others. Part of it is to focus on making sure that there is open access to life-saving drugs, and some of this is even tariffs, Senator Kyl, making sure that people do not have those barriers.

For those that have State-run health care systems, I think the challenge that we have is, how do we emphasize the principles we can all agree on to move forward: high-quality health care, making sure that if they are going to set prices in some ways that it is a transparent system, people know the basis of the rules, to make sure that those rules, as we do in the Australia agreement, include recognition of the role of innovation and the role of R&D, have review processes for those rules.

As you said, in the case of Australia, we have some ongoing working groups, both with specialists, but also a broader group of medicine working group. What some people always focus on, and I know we have had this discussion with you, it is not a question really of raising prices.

It is a question of kind of distribution of those prices. Like, one of the things we learned in Australia was, because of the pricing system they had, generic prices were higher than they are relative to the research-based prices.

Senator KYL. Since the yellow light is on already, my question was, are we going to pursue these same discussions with other countries and what would those countries be? I also wanted to be sure and mention that the medical device industry is every bit as important here in terms of innovation as the pharmaceuticals, and will you be including those items in your discussions as well?

Ambassador ZOELLICK. Yes. In fact, we had discussions with the Japanese just this week or last week on a deregulation initiative where we are trying to get faster turnaround for both drugs and medical devices, actually, which is an important market.

I think the focus is primarily on the G-8 countries, but this is one that we have talked about with some of my colleagues that work on the G-8, how we can work on it together, and to deal with the sensitivity here, which you and I know is we do not want to be seen as just trying to push to raise prices, we want to be seen for trying to get better treatment for R&D and innovation.

The other point which I know you and I have worked on as well, is that we need at the same time to emphasize that for poor, developing countries, this does not undermine at all what we try to do to make sure that they have access to HIV-AIDS drugs, the compulsory licensing. We work very hard to try to put that problem to rest and I think this is really more a question of kind of burden-sharing among developed countries.

Senator KYL. Thank you. We will want to pursue every opportunity that we can with these other countries.

I thank you, Mr. Chairman. Also, I want to just make a pitch, that I hope we can deal with CAFTA this year. It is very, very im-

portant and I would certainly hope that we can do whatever we have to as a committee to see that that is done.

I know the USTR did a lot of work on that and I appreciate the President having brought it up and provided the essential notice for us to move forward, and I hope we can. Thank you.

The CHAIRMAN. Thank you, Senator Kyl.  
Now, Senator Snowe?

Senator SNOWE. Thank you, Mr. Chairman. Welcome, Ambassador Zoellick. I want to focus on the issue of China. Obviously, I think one of the compelling issues with respect to China was when Congress granted the permanent normal trade relation status to China, is that they would become a member of the World Trade Organization and then abide, and be obligated to abide, by the rules of the international trade agreements.

Obviously, as we have seen, certainly in my State, but across the country, that the manufacturing sector has been significantly disadvantaged, without question, and continues to be disadvantaged.

We have obviously been wrestling with a question about, how do we address, frankly, I think, egregious practices on the part of China with respect to deliberately under-valuing their currency. It comes at our expense, jobs, the cost of goods, and so on. They have been able to under-value parts of their goods 15 to 40 percent.

So, as you know, Senator Bunning and I sent you a letter to which you responded in February with respect to initiating a 301 investigation of the currency trade practices of China.

In your response, you indicated that the WTO is to set rules for governments regarding trade policies rather than to examine exchange rate policies. I know the administration is taking the issue very seriously. The President has made some very strong statements, Secretary Evans, Secretary Snowe, and so on.

But I think the question is what we are prepared to do now. It is my understanding that the World Trade Organization could have an obligation if we initiated 301. We found violations of Article 15 of GATT with respect to exchange policies and that that could come before, I guess, their deliberative body, or dispute resolution body, rather. I know the National Association of Manufacturers is intending to file a 301.

So what will be our position on that and why can we not pursue this more aggressively? Because I do think it is critical. There is just no question, there is a cause and effect.

The time has come for China to abide by the same rules that every other member of the international trading organization is complying with. So, I think it is important for us to do what we can to indicate that we are serious.

I mean, we just cannot allow this to create a vacuum, opened, for years on end because in the meantime we are losing jobs and we are losing companies, to the detriment to, I think, Americans.

Ambassador ZOELLICK. Let me just start, just for a moment.

Senator SNOWE. So I would like to know, on WTO. I mean, it is my understanding that it states under Article 15 that WTO members "shall not, by exchange rate action, frustrate the intent of the provisions of this agreement."

So, clearly, if there were violations, that it could come before the WTO. I am just wondering, at what point are we going to be aggressive in pursuing this issue on behalf of workers and industry in America?

Ambassador ZOELLICK. Well, Senator, I think we have been pretty aggressive with China on a lot of items. That is one reason why our exports are going up 75 percent when our exports around the world have actually declined over the past 3 years.

And, while obviously you get some huge gains in the agriculture community, it is not just agriculture. Our electric machinery exports went up 21 percent last year, so that is integrated circuits, telecommunications, parts, so on, and so forth.

I asked the chairman of GM, since I know they are doing a lot of investing there, does this also allow you to sell there? They sent me some information that, over the past 3 years, they had sold over \$1.4 billion of components and parts and 15 percent of the Lansing River plant now goes to make Cadillacs that they sell, or Buick Regal sort of kits that they manufacture. So, there are some important manufacturing benefits.

On the currency issue, it is a point, as you mentioned, the President has stressed, Secretary Snow has emphasized, Secretary Evans and I have emphasized. There was a Treasury team that was just there over the past week as a follow-up effort.

The report that I got—but we can check with Secretary Snow—is the Chinese realize that they are going to need to move to flexible exchange rates and open their capital account, which is what they have to do to do that.

Their question that they are trying to figure out is exactly how to do it without creating a crisis in their banking system, because if you have got open capital flows and you have got a weak banking system—and they have got a very weak banking system—you could unleash a problem that frankly means China is not buying from anybody. So, that is part of the transition that we are trying to work with them on.

I have urged that they take some interim measures to show that they are going to start to solve the problem. If they cannot deal with that problem right away, Senator, emphasize the fact that we need to have a two-way street in terms of other things that we sell in the meantime.

On the case itself, I am always a little reluctant to talk in kind of an open session about sort of litigation prospects, for reasons you would understand. But you read language there. There really has not been a case brought like this.

One of the questions we would have to ask ourselves is, right now, China globally is in a slight deficit, so its exchange rates deal with its global position, not just the U.S. position. So does that mean that it is frustrating its position?

And one thing I know for sure, Senator, is the first case we bring against China, which could be soon, is not one that I want to have a risk on. So, we can talk a little bit more about the pros and cons of that case, but there are some others that I have emphasized where I think it is much more clear. For example, their tax policy with semiconductors is discriminatory, and if they do not fix it, very soon we are going to bring a case.

Senator SNOWE. Thank you.

The CHAIRMAN. Senator Graham?

Senator GRAHAM. Mr. Zoellick, thank you very much for your always thoughtful comments.

I would like to start with a comment and then go to a question. My comment goes to the issue that you have just been discussing with Senator Snowe. In my opinion, in a number of areas, the United States is losing its national sovereignty.

What is one of the major foreign policy questions we are facing? Proliferation of weapons of mass destruction. North Korea is a significant concern. What is one of our biggest domestic financial issues? How do we finance this enormous and hemorrhaging national debt?

In both of those issues, we have turned to China for a substantial part of the solution. They are leading the multi-party efforts to negotiate with North Korea. They are, I believe, now the third or fourth largest purchaser of U.S. instruments to finance the \$1.5 billion every day of our National debt.

Now, how in the world are we going to deal with China on a specific trade issue or their balance of payments and currency exchange when we have got to look to China to reign in the North Koreans on weapons of mass destruction and pay a significant amount of our escalating national debt.

That comment, to me, raises the reality that these issues are not isolated boxes, that they are interrelated, and they relate to America's ability to exercise significant influence over a whole range of issues.

I would suggest that our policy with regard to Korea and our policy relative to our own fiscal affairs are substantially diluting our ability to have that influence on important economic and trade issues. That is my comment.

My question is, I have been concerned about this question. How does the United States of America, with its much higher than world average standard of living, compete in a global economy where the lowest unit cost of production has become almost the Holy Grail?

I have asked that question of a number of people and I have consistently gotten three answers. One, that we have got to continue to make a significant investment in innovation, that what saved us for the last 20 years was that we were the first in line on the computer telecommunications revolution and that we now need to be the first in line on whatever the next major economic lift will be in the world's economy.

Second, we have got to have the best-trained workforce in the world in order to be the most productive. Third, we have got to continue to make an investment in our basic infrastructure, such as our transportation system, so that it contributes to our productivity and is not a drag on our productivity.

The first question is, do you agree with those three priorities for maintaining America's standard of living while being competitive in a global economy? If you do agree, I would be interested in your assessment of how well we are doing on each of those three areas.

Ambassador ZOELLICK. Well, Senator Graham, that is what they call a big question.

Senator GRAHAM. And you are a big thinker and you are here to talk about the administration's international trade agenda, and those are certainly issues that need to be central to our trade agenda.

Ambassador ZOELLICK. They are excellent questions, Senator. I am trying to figure out how to answer it succinctly. All three of the points you mentioned go to productivity. The reason why that is key, is that when you look at wages around the world and you look at where people decide to invest, it is not just a question of wage rates. It is a sad case to use now because of the problems with Haiti, but people for years have said, look, if it were just a question of wage rates, everybody would invest in Haiti. But they do not.

So why do they invest in the United States? That, frankly, is one of the reasons why you have got the capital inflow to this country. And going to your point about China, where I would differ a little bit, and this happened in the 1980's, too, they are not buying those treasury bonds out of favors to us, they are buying it because it is a liquid security and they get the return.

Senator GRAHAM. No, it is not a favor to them, it is a favor to us. Here we have got a currency which has just degraded 30 percent in the last couple of years and they continue to buy that currency.

They are the ones who are doing us the favor, just as they are in dealing with North Korea. Therefore, our ability to influence the Chinese on issues that are important to our trade policy is substantially diluted, in my opinion.

Ambassador ZOELLICK. Well, Senator, this is where I beg to differ a little bit. The Chinese, or any other country, when they buy U.S. treasuries, they are not saying, let us do a favor to the United States.

They are doing it because it is a liquid security, and in this case, as Senator Snowe mentioned, it might even keep the dollar up because they are buying the dollar. That is why the Japanese are buying U.S. securities.

So when people act like, oh, well, they have got leverage over us, they really do not because they are deciding to buy that security versus euros or others about what the best investment is and what their overall interest in terms of exchanges, in terms of whether they are going to hold dollars, which bids up the price of dollars, for something else.

But to go to the point about the productivity, the connection is as follows. One of the reasons that you have the big trade deficit in this country is you got a lot of capital coming into this country. It is the flip side of the trade deficit. That is because it is a good place to invest.

Now, when people invest in the United States, whether they do it in treasury securities or whether they do it in stocks and bonds, that, depending on how you spend that money, helps build your long-term productivity.

So when you look at the American workforce, they are by far the most productive workers in the world, much more than in Europe, much more than in Japan. That is why you can pay higher.

Now, the other side of that challenge, and this is what you see in the papers today, is as the productivity numbers go up, which

on the one hand we should be happy about, people will also say, yes, but as the person produces more, you do not create as many jobs.

So, at some point over the next couple of months you will start to see some change of that, and I believe you will see more jobs created. A few years from now, people will be very pleased with the productivity increases.

But to go to the core elements, I do believe we need to focus on education and schools, basics, but also, as we talked about here, retaining is fundamental if you are going to have a flexible economy.

You also mentioned innovation, so whether it is an R&D tax credit, or obviously from my point of view, having lower taxes so that companies can decide how to allocate their capital. Third, in terms of infrastructure, that is one of the aspects that makes our society more productive than others.

Now, you also see you can overdo that. Japan is a country where they pour tons of money into putting concrete on every river, and building bridges and roads that do not go anywhere. But those three elements are certainly elements that lead to productivity in the United States and they are part of our long-term development.

Fundamentally, it comes down to having well-educated, creative people in an economic system that allows them to use their ideas and the fruits of their labor. What is a challenge for us, and this is the exact thing that is happening right now, is that a more flexible system like that causes more upheaval for people and that creates anxiety, and that is why some of the things we have talked about on the trade adjustment side are going to be important if you are going to keep an open economy.

Senator GRAHAM. Excuse me, Mr. Chairman. I have concluded. But maybe you could just answer this with three letters, from A to F. How do you feel we are doing on innovation, preparing the American worker for greater productivity, and improving the state of our infrastructure?

Ambassador ZOELLICK. Senator, I am not trying to duck. As you know, I will give you a fair answer to your question if I know something. I am wary of a very generalized statement about that just because I think that, in terms of innovation, I think the information technology industry that I have talked to has emphasized the importance of some things on the tax side that would probably encourage it.

But the greatest thing we could do is not overload them with a whole series of new regulations and taxes that kill the rewards of innovation.

I would say the United States remains the best place to have innovation in the world. But, as you said, Senator, it is something you can never rest on because there are a lot of people out there who are eager to catch up.

In schools, I have long felt that schools in the United States—I am always amazed we produce some of the good people we do because I do not think that the standards in schools have been what they should be. But I am not an expert on that.

I think the President's Leave No Child Behind is the fundamentals. If you cannot read, write and do math, you are not going to make it in the modern world.

Now, I also think there are some important elements in areas like community colleges. I know this is a big area in Florida. I was in rural Illinois not long ago visiting a Caterpillar plant and I was there at a lunch with the head of the local community college.

I was very impressed by how they are connecting with the businesses in the local community to try to figure out how to create jobs that relate to the changes in the workforce. So, I think those are all the aspects that, in a bipartisan fashion, we are going to need to focus on together.

The CHAIRMAN. Thank you, Senator.

Senator Lincoln?

Senator LINCOLN. Thank you, Mr. Chairman.

Thank you, Mr. Zoellick. We appreciate you being here.

Just a few comments I would like to make for the record, Mr. Chairman. Throughout my career, first in the House and now in the Senate, I have been a strong supporter of open trade policies and I have carefully tried to review the trade agreements and other trade initiatives, such as the trade promotion authority for their costs and their benefits.

In every instance, I feel like I have given my support. I have supported these agreements because I recognized how important they are, not only to agricultural products, and I am an agricultural producer so I tend to be a broken record on, and employers in my home State of Arkansas, but also to our Nation's economy overall, as well as what I think the American people are interested in seeing in the future in terms of having the safe, abundant, and affordable food supply that they are assured of, and know fully well how safe it is.

I have supported these agreements because these benefits also stretch beyond their mere economic justification. It is about more than economics. Open trade is about opportunity, and through trade we can bring hope and stability, I think, not only to ourselves, but also to the most unstable regions of the world.

We always have to balance that. I appreciate the fact that you work very hard at that, Mr. Zoellick. I think you really do, in trying to balance this thing out.

Through trade we can, and we must, demand that our trading partners make dramatic improvements in labor and environmental standards if we are truly committed to a level playing field that will allow us to realize the full benefits of free and fair trade.

I know that in talking to workers oftentimes about the jobs that are being lost out of our State, they begin to list the cost of doing business, the cost to industry in our country.

I hope that we will continue here to work at a better rate of providing industries in this country an ability to be competitive and not giving them only their labor category as the area where they have control over in terms of squeezing down their costs to be more competitive, but also hope will come from the other direction in making sure that the countries we are competing with are willing to meet us at that table and be as far and progressive as they possibly can be towards their workers.

Based upon these facts, I do remain a very strong supporter of open trade. While I am a strong supporter of open trade, I am also a very strong supporter of American workers. American workers,

he and she that are out there, are really the most productive, the most efficient, and most dedicated workers in the world.

As the government they pay for out of their hard-earned wages, I think we have to do right by them. We here in the Congress have got to work hard to make sure, and I appreciate the fact that we have a good working relationship with USTR and that you do strive to do that.

But the joblessness that American economic policies have sparked here at home, I think it is impossible for us to let them go and recognize, in our discussion today and going forward in what we have to do—even in the last decade when the economy was much stronger and unemployment was much lower, there was uncertainty in some sectors of the American job market. The conditions have only become more pronounced, I think, with the recent recession and the sluggish economy that we face today.

Virtually no sector is unaffected and it is unreasonable to assume that we will become a Nation of executives managing workers offshore. I do not think we can survive that way. There is no sustainability in that.

Virtually every week brings new job losses in Arkansas, plants closing, layoffs, companies going out of business. That can be attributed to offshoring of jobs. And since the year 2000, my small State has lost more than 30,000 manufacturing jobs.

There is a lot of anxiety out there and we need to work to allay those anxieties and the ones that are there before us. Clearly, we need to do a better job of ensuring that American workers remain competitive in this globalized economy, and I hope that we can.

But I do think it requires a more comprehensive, multi-faceted solution that takes everything affecting job creation and job loss into account, including the rising health care costs and energy costs, just to name a few.

We have a great opportunity before us here in the Congress to do something about that, and I hope that we will. It would certainly, I think, make your job a lot easier in the things that you have to do.

It requires that we emphasize the importance of investing in our workforce in order to ease the uncertainty and concern. Senator Graham has talked a good bit about that in terms of innovation and the education and skills that we need to be able to be providing our workers to be globally competitive.

In the environment, job training, education, trade adjustment assistance, these are the most important tools for helping today's displaced workers transition into good-paying, productive, and sustainable workers. I hope we can continue to work together to make that happen.

I appreciate the Chairman holding this hearing today so that we can discuss what is needed and get some sense from Ambassador Zoellick of how the administration plans to cope with these needs, as well as the negotiations that you find yourself in in the many trade agreements that we are looking to bring to closure.

But before I close, Mr. Chairman, I would like to just make one final point in regard to the Continued Dumping and Subsidies Offset Act, what is commonly referred to around here as the Byrd amendment, which everyone is familiar with.



As you are aware, Ambassador Zoellick, I am very supportive of that provision in our trade law and join with an overwhelming majority of my Senate colleagues in expressing disapproval of the administration's position to repeal it. I hope that there will be further discussions and continued work on what we can come to in conclusion there.

Like all of our trade laws, I believe that this provision helps to ensure our ability to defend against proven instances of unfair trade, enabling us to keep jobs here in America, Mr. Chairman. I strongly encourage you to reconsider your position on that.

I think it is going to be a vital part of our trade implementation in the future and I hope that we can work together to come up with a solution that I think is going to be beneficial to all.

So, thank you, Mr. Chairman, and a special thanks to you, Ambassador Zoellick, for all of your hard work and your willingness to work with me when I do tend to be a broken record. Thank you.

The CHAIRMAN. Ambassador Zoellick, I and Senator Graham have some more questions we would like to ask you. As you know—

Ambassador ZOELLICK. Could I just say, Mr. Chairman, for Senator Lincoln, before the two of you came, I mentioned at the start how much I appreciated the help, not only over the past year, but over the past 3 years. You two have both been very supportive of us.

We have tried to be responsive to the interests that you have had. Cotton exports to China are up almost 500 percent, so there is a plus, some of the work that we did together on those issues. I know it is not easy. One of the things I mentioned and complimented Senator Baucus on, was that this committee played a key leadership role in adding to the trade adjustment assistance with the Trade Act. Last year, there was about \$1.3 billion of that covering some 200,000 people, which I think is critical.

On the Byrd Act, Senator, just let me share with you one caution. We have been found in violation of the WTO rules on that act and we are now contesting in an arbitration how much other countries would be allowed to retaliate.

There are about seven or eight countries lined up. They are seeking amounts of about \$150 million, could be higher. We obviously are contesting those amounts. The one thing we are going to have to be sensitive to, is if those countries retaliate, well, then exporters in America are going to feel the pain of that.

Now, you may ask, why did they find that? The antidumping and the countervailing duty rules are rules that are supposed to create an offset. If somebody subsidizes X amount, you are allowed to make up the difference.

What that law does, as you know, is then say, we will give that amount to the party that we believe brought the action. The difference is supposed to be made up and cause a fair price for the seller, but if on top of that you give the money to the person who brought the action, you are really getting a double hit.

I would just, in part, also mention, particularly from your State where you have got a lot of poultry production, these antidumping rules are increasingly getting used against the United States.

As you probably know, on all our agreements now, we cannot just talk about poultry, we have got to talk about the leg quarters and others because of the different price structure.

So not only is it something that can hurt our exporters in terms of tariffs, but it could hurt particular exporters. So, I know it is a sensitive topic and I know it is one that is deeply felt, but we could keep the discussion going if we could.

We are arguing against the number, but the other countries have said, well, the amount we should use is the amount that has been given back to people, which is roughly \$150 million, could be another \$80 or \$90 million.

We have argued that it should be, if any number, a lower number because you should focus on trade effects. That arbitration should be done sometime in the middle of this year. But I am just saying, this is the other side of it, which, as in the FSC act, we face retaliation if we are violating the rules, and then some of these exporters—could be in some of your States—get hurt.

The CHAIRMAN. I want to ask about questions of sanctions that we are facing right now, and that is the sanctions that the European Union are putting on us. You know that they are on a wide range of U.S. agriculture and manufactured goods.

They are 5 percent now, and are going to increase one percent a month for the next 12 months. There are some who would suggest that these sanctions are so low that they do not matter. Mr. Ambassador, they suggest that sanctions will have no impact, given the recent devaluation of the U.S. dollar.

So in regards to the European sanctions against the United States on FSC/ETI, what is your view? Do you agree that sanctions do not matter?

Ambassador ZOELLICK. Well, no. Clearly it adds to the costs for our exporters. You have got about \$3 billion worth of American exports that are now subject to an extra tax of 5 percent.

So, many of you work with your State governments about sales taxes, and if you want to add on an extra tax of 5 percent, or 6 percent, or 7 percent, or 8 percent because it is going to go up 1 percent a month, it is clearly going to affect the sales of American businesses.

So, again, I know you and Senator Baucus and others have had a thankless task, but as soon as you can get that repealed and something in its place, American exporters will be much better off.

The CHAIRMAN. In regard to the Doha Round, obviously I am interested in a successful completion there. American agriculture has waited too long for access to the world's markets. I hope we see progress in the next few months on a negotiating framework for agriculture.

One concept that concerns me is the continued calls by countries, and I think Brazil is the most outstanding for special or differential treatment. My point is, it simply does not make sense to allow major economically competitive agriculture exporting nations, and Brazil is surely that, to get the same treatment as, say, some struggling nation like Ethiopia.

In fact, if that is the result of the negotiations, I am not sure that they would receive any Congressional support. What steps are you taking to address the complex issue of special and differential

treatment to make sure that, at the end of the day, U.S. agriculture is not seriously disadvantaged, like some special provisions for a developed nation agriculturally like Brazil is?

Ambassador ZOELLICK. Well, Mr. Chairman, we made the exact point that you made. Indeed, in this letter that I sent to my colleagues in January, I stressed that if we were going to be successful in agriculture, in cutting some of our domestic subsidies and opening our markets, because our tariffs are already relatively low compared to others, we were going to have to get increased access to major developing countries.

As you said, what I have emphasized is this does not mean poor countries in Africa, it does not mean poor Caribbean countries. It means some of the major players, for example, in Latin America, Southeast Asia, and other very important markets that we are trying to target through free trade agreements, but we would like to get them all, frankly, in the Doha negotiations.

A point that we have tried to make with some of the poorer developing countries is that we can actually express more sensitivity for them if everything we apply to them does not apply to a Brazil or an Argentina.

There is some recognition of this in the WTO through special treatment for what are called least developed countries, the poorest countries. But, frankly, I think it is a point that is going to have to be pursued further in the WTO because, as I have warned some of my partners in major developing countries, we are not going to be able to sustain open markets in this country unless we get some markets opened elsewhere, and that includes some major developing countries that frankly, over the past years, have taken very few cuts.

It is not only a question in agriculture, Mr. Chairman, it is going to be in manufactured goods as well. So, that is how we are going to have to strike the balance, for those that are truly in need versus those that are truly in need versus those that are competitive.

The CHAIRMAN. On the question of something Mexico is going to American agriculture, I would like to ask you about—and this would be a follow-up on the hearing that we had last September on barriers that Mexico is imposing on our products. We have had several different Senators express the same concern.

But of particular interest to my State of Iowa, Mexico continues to maintain a de facto ban on imports of U.S.-produced high-fructose corn syrup through its tax on soft drinks containing this product.

What efforts are you making to see that Mexico continues compliance with its NATO and WTO obligations concerning this, and other products? By the way, I sent a letter to the President—maybe too late—last Thursday or Friday asking that he bring this up with President Vincente Fox.

I do not know that he did, but I just want that for the record that I at least asked the President to do that. I presume you were not involved in those talks last weekend.

Ambassador ZOELLICK. No. I was busy opening up the beef market there, Mr. Chairman.

The CHAIRMAN. Good. Thank you. Go ahead and answer my question.

Ambassador ZOELLICK. Well, first, I want to compliment you, Mr. Chairman. With the hearing you had and others, you helped give us some additional leverage to make some headway on a lot of agriculture products with Mexico.

In addition to beef, we had success in removing the antidumping order on live swine, which is very important to your State and others. We solved a problem with dried beans and poultry. I think we are close to solving something with apples, and we have stopped them from an investigation so far on pork. On rice, we have not been satisfied and we are bringing a WTO action on rice.

On high-fructose corn syrup, frankly, I have told my Mexican counterparts that we consider the tax they have discriminatory and I believe, at least it is my hope, that we will be bringing an action very soon, Mr. Chairman.

The CHAIRMAN. Senator Graham? And does Senator Lincoln have a second round?

Senator LINCOLN. No, sir. I could just submit my questions.

The CHAIRMAN. All right. Yes.

[The questions appear in the appendix.]

The CHAIRMAN. Then when you are done, Senator Graham, we will adjourn.

Senator GRAHAM. Well, that will help contribute to brevity. [Laughter.] Again, I have a comment and then a question.

I had asked if you would be willing to try to evaluate our status on these three issues of innovation, education, and infrastructure. I will take a shot at it. I think the private sector deserves an A. They continue to make a significant investment in innovation and that is a key to their individual success and our collective success.

I am afraid I will give the Federal Government a C-, and I will pick out one specific area which many people have suggested will be the follow-on to telecommunications and computers, and that is various applications of biomedicine and genetics.

We have, in these areas, erected some of the regulatory barriers that you suggested, often driven by ideological, rather than scientific, standards. We have reduced our Federal commitment to medical research and development. This is true in many areas.

One area that I am particularly stressed about is, as part of the general reductions in services for veterans, one of the most hard-hit areas has been the medical research that the Veterans Administration has historically provided, which has been, incidentally, some of the most productive research that the Federal Government finances.

The ability to put pure science and immediate clinical application together for the benefit of the 10 percent of Americans who are veterans has not only benefitted that 10 percent of the population, but has had a national and international value, and that is a program which we are now retreating from.

In terms of education, to me the big issue in education is the fiscal crisis of the States. The States and local governments pay about 94, 95 percent of the cost of education and they are literally in crisis in my State so bad that there are proposals to cut the 12th grade out of a standard public school education in order to save

money. The Federal Government has substantially contributed to that crisis of the States, and therefore I would give it a D on that.

But the worst grade is for infrastructure. We just passed a transportation bill in the Senate a few weeks ago which, if nothing else, does one thing. It guarantees that our American transportation system, both highways and public transit, will be worse at the end of 5 years than it is today.

That follows a strong precedent because the one we passed in 1997 assured that it would be worse at the end of that period, and it is, and the one that we passed in the early 1990's had the same assurance.

So, for the better part of 15 years, the Federal Government has had a policy of disinvesting in transportation, which has resulted in an increase in both congestion and a decrease in the level of maintenance of our roads and bridges.

I happen to know something about the status of infrastructure in Iowa because I spent about 6 months getting a seminar in that. I will not attempt to state what the facts are there, but I am certain our Chairman is well aware of it. So, I would give us an F in that category.

So if we are serious about having a strategy that is going to help us balance a high U.S. standard of living versus a competitive global economy, we are not doing a very satisfactory job. That is the end of my comment.

Now, the question. Senator Kyl raised the question of pharmaceutical pricing and specifically talked about the Australia trade agreement, which has had the effect of injecting more marketplace in the Australian pharmaceutical distribution system.

Has there been demonstrated that there is a correlation between greater market forces in foreign countries and a reduction in pharmaceutical prices in the United States?

Ambassador ZOELLICK. That is a question that I have asked some of the pharmaceutical companies myself, because, as you know, they are in a larger competitive environment. One of their concerns is whether they will have R&D paid for at home or abroad, and how it affects their prices.

It is a subject that I do not think there is a clear answer to yet, Senator Graham. I think that is why, in my answer to Senator Kyl, I mentioned that my own sense of this problem is that you have to look at it in a multifaceted approach.

I think there are going to be things, again, as this committee and others did, to try to help people pay for their prescription drugs under Medicare. I have talked with the companies about the discount card approach, which would be a way of trying to cut prices.

Again, what I hasten to emphasize, because many people, I think, misstate this, I do not see our mandate as trying to increase people's prices elsewhere in the world. I see our mandate as trying to give a fair return to innovation and R&D and have a transparent and open system.

And as I just alluded to, the more one gets into this, in each country, obviously, the system varies a tremendous amount, particularly if they have State-run health care systems.

But some of the changes, at least, we are urging people to look at could lower their costs of generic prices because they have com-

parator systems between prescription drugs that are unpatented and ones that are not, and the comparators actually pull up the generic price.

So when you deal with other countries' health care systems, as with people dealing with ours, one has to have a lot of care here. You want to be constructive. You do not want to be destructive in the process.

Frankly, some people will also point out, we have various prices that are set as part of our government pricing systems as well. But I do think it is a legitimate subject for discussion and debate because Americans do pay a larger share.

Senator GRAHAM. Well, why I think this is so important, is trade is like every other negotiation. If you are selling your house or bargaining for a car, is it is a series of trade-offs. I will facilitate getting a better mortgage if you will pay me \$10,000 more for my house, kind of thing.

Here, we have made a decision that we are going to emphasize trying to open up Australia's pharmaceutical market. I happen to be a dairy and beef farmer. I know farmers—and again, I would defer to Chairman Grassley—have felt for a long time that they have been traded off in order to do things like getting Australia to open up its pharmaceutical market.

So, in my judgment, we should not play that card unless we have some confidence that it is going to have a benefit to the United States of America and its prescription drug-buying citizens. So, this is not a new issue. It has been around a long time.

Has anybody done any economic analysis of whether successful negotiation of a greater marketplace in pharmaceutical drugs for foreign countries results in a reduction in the price pressure here in the United States?

Ambassador ZOELLICK. I think it is too early to tell yet, Senator. But since you mentioned agricultural topics, as you know, they are always number one on our list. I recall sugar has an interest in the great State of Florida. As you probably know, I have been roundly criticized for not even including sugar. So, there is one for your constituency.

Senator GRAHAM. We will reassess your grade based on that. [Laughter.]

Ambassador ZOELLICK. And frankly, in terms of dairy, I think we have increased our quota. We did not touch the tariffs one bit, the huge amount of about maybe \$30 or \$40 million a year, which I hand this off to Al Johnson who does the tough labor on this.

Then in beef, as you probably know, we did not increase the quota until like, year three at the earliest because we link it to the BSE levels. We have an 18-year phase-out that Prime Minister Howard personally was pushing to get lowered, which we did not lower.

It actually should work well with our industry, Senator, because we only increased the quota for manufactured beef. As you know, as a cattleman, a lot of our beef is actually raised more with grain, it is a little fattier.

Their manufactured grain beef actually creates a good complement in terms of the hamburger meat. So I hope, as you look at the overall agreement, you feel we got a pretty good deal. Oh,

by the way. We also got an SPS evaluation for citrus, too. So, we tried to take care of the State of Florida.

Senator GRAHAM. I just want to know if that economic trade-off to emphasize opening up Australia's pharmaceutical market is going to result in my constituents paying less for their prescription drugs.

Ambassador ZOELLICK. Well, all I can tell you, Senator, and you know me well enough, is that I insist that we get everything we want as best I can.

The CHAIRMAN. Thank you, Senator Graham.

I would like to have staff of members say that we will keep the record open until the end of business tomorrow for questions that might be submitted for answer in writing. You might have some of those from me, Mr. Ambassador.

Maybe in the way of closing, I would tell you about a major industry in Iowa. This is not a question, just something to be alerted to. A major industry in Iowa that has a famous name has told me that they are going to bring some jobs back from Mexico to Iowa because they have come to the conclusion that you just cannot chase cheap labor around the world from one country to another, to another because there is always somebody that is going to work cheaper someplace else.

They have come to the conclusion that they had better do what they can to enhance their own productivity, and that is what they are about doing with a lot of investment to keep jobs in the United States.

Now, I hope there are a lot of other companies that are doing that as well. If there are companies—and I think this would follow up on your admonition to business, not talking about the good news of trade and the creation of jobs in America, always the bad news seems to get the headlines.

But there has got to be some trade association somewhere in America that can sort out these various companies that are trying to do something like this and get that news out. So the depressing news of out-sourcing, which is true in the sense that it affects those jobs, can be overcome, I guess, with some positive news.

Ambassador ZOELLICK. I appreciate your help and support, Mr. Chairman. I know it is not an easy position to be in, and your support is vital for us.

The CHAIRMAN. Thank you. Thanks to the members here, including Senator Graham, who has come and helped us review the trade policies of the administration.

The hearing is adjourned.

[Whereupon, at 11:51 a.m., the meeting was concluded.]





## APPENDIX

### ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

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#### PREPARED STATEMENT OF HON. MAX BAUCUS

Thank you, Mr. Chairman and thank you Ambassador Zoellick for appearing before the Committee. You have given us a comprehensive overview of the many issues that will be on our radar screen this year. I would like to focus today on one issue, and that's jobs. I think the primary goal of our trade policy should be to keep and create jobs.

In the last three years, we've lost about 3 million jobs in this country. Some of those jobs are moving overseas—and increasingly, the jobs that are moving overseas are higher-paying, and higher skilled jobs. Everyday now, it seems like there is news on the subject of “offshoring.” I hear it from the press, from my colleagues in the Congress, and from constituents. Manufacturing plants moving to China. Call centers moving to India. Even jobs in state unemployment offices are not immune—in some states unemployed workers have to call someone overseas to find out what their state benefits are.

There has been a lot of debate on whether this is good or bad in the big economic picture. But let's face it: offshoring of jobs has people worried. And the legitimate worries of the American public cannot be dismissed. There is no silver bullet. There are lots of pieces to the offshoring puzzle—tax, education, health, research and development—to name a few. But today, we should talk about the trade piece. About how to use our trade policy to create and keep good jobs here at home. I think it is a question of priorities.

First, we need to re-examine how we choose partners for free trade agreements. I remember when we were debating fast track and the Trade Act of 2002. All of us—here in Congress, in the business community, and at the White House—we were all talking about exports, competitiveness, and economic growth. In short, we were talking about jobs.

But somewhere along the line, that goal got hijacked. Instead, as the General Accounting Office recently concluded, foreign policy considerations now dominate this administration's selection of trade partners. I think that's a mistake. I do want to commend you, Ambassador, for continuing to push forward on the World Trade Organization (WTO) Doha Round. The collapse of the new Round in Cancun was a serious setback; we need to continue to make the WTO a priority. I also agree that the WTO can't be the only game in town. We need to move ahead on different fronts. We need to negotiate free trade agreements.

But—we are now negotiating a number of agreements that will have very limited benefits. Now I want to be clear—I welcome more open trade with any country willing to make comprehensive commitments. But negotiating these agreements takes a lot of resources. And our negotiating resources are not unlimited. American workers, farmers, and businesses deserve the most bang for the buck that we can get them. They deserve trade deals with commercially significant markets that will generate job growth at home.

Second, enforcement. Negotiating free trade agreements is not the only way to get market access. Case in point is India. We all know that India is benefiting enormously from the offshoring of service-sector jobs from the United States. But the United States is not getting anything in return, because India has such a closed market. And India is certainly one of the leading countries holding back progress toward greater market access in the WTO.

The administration's proposed solution is to negotiate a free trade agreement with the country next door to India—Sri Lanka. Total U.S. exports to Sri Lanka last year were about \$143 million. So after we expend lots of negotiating resources and wait

out a 10 to 15 year implementation period, we might have free trade with an economy that has a current commercial worth to the United States of \$143 billion a year.

By contrast, American businesses in 2002 lost more than twice that much—\$342 million in retail revenues—just from software piracy in India. India has made commitments under the WTO Trade-Related Aspects of Intellectual Property Rights (TRIPs) Agreement to protect intellectual property rights. What are we doing about enforcement? How can we spur innovation and create jobs at home if we let people steal our intellectual property—\$13 billion worth of software alone in 2002? Wouldn't our limited resources be better spent combating piracy than negotiating agreements with tiny markets?

I think we need to reassess our priorities. That is why today I am requesting that the GAO conduct a review of how we enforce the more than 250 trade agreements that the United States currently has on the books. This study, which will be completed in early 2005, will help Congress and the Administration better assess how well we do at enforcing trade agreements and how to allocate our resources to achieve the best possible results. And by best results, I mean first and foremost jobs. Because that is what Americans need.

Third, we must ensure that U.S. companies can compete on a level playing field. But we should reject the notion that we must lower standards in this country to compete. Instead, we must look to raise standards in the countries we trade with. The Trade Act of 2002 made tremendous progress in this regard, but we must continue to "race to the top."

When it comes to standards on labor and the environment, the debate in the last three years has been about what this administration and this Congress—not our trading partners—will accept. Our trading partners will accept higher standards in order to gain the prestige and access that a trade agreement with the United States gives them. I know that—I've met with the trade ministers and talked with them about these issues. But we negotiate with ourselves instead of with them. We've got to do better.

Mr. Chairman, Ambassador Zoellick, I look forward to working with both of you, and this Committee, as we focus on the priority issues in this year's trade agenda.

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PREPARED STATEMENT OF HON. CHARLES E. GRASSLEY

This is an important time in U.S. trade policy. Just a few years ago, Congress empowered President Bush through the passage of Trade Promotion Authority to negotiate trade agreements to help strengthen the U.S. economy. To date, Congress has implemented two free trade agreements under TPA procedures. Three more are at our doorstep—the Central America Free Trade Agreement, the U.S.-Australia Free Trade Agreement, and the U.S.-Morocco Free Trade Agreement. Each of these agreements has substantial benefits for the U.S. economy. Negotiations continue to create a Free Trade Area of the Americas and, I hope, to conclude a new round of trade talks in the World Trade Organization in the near future. There are also a number of bilateral negotiations under way that require our continued attention.

In my mind, we are now at somewhat of a crossroad in U.S. trade policy. While we have made some progress in leveling the playing field with our foreign competitors through the passage of the U.S.-Chile and U.S.-Singapore free trade agreements, there clearly remains a lot more for Congress to do. With enough political will Congress could—I repeat could—implement as many as three free trade agreements this year. Congress is likely to see even more free trade agreements ready for implementation next year. Most important, Congress could be considering a new World Trade Organization agreement in the not-so-distant future. This negotiation is clearly where we get the most bang from our negotiating buck, especially for American agriculture. And of course, next year Congress will face the issue of whether to extend TPA for an additional two years.

Implementing these agreements and extending TPA will require tough choices and political courage. Unfortunately, political courage is not always in endless supply. After all, this is an election year, and it appears that some of our presidential aspirants are determined to make trade and trade agreements our economic whipping boy. While this may be good politics in some areas of the country, it is disastrous economic policy. That does not mean we should discount workers' concerns about trade and their role in the world economy. But at the same time, we should not pander to these fears for short-term political gain. I was surprised to learn last week that some of my colleagues in the other party made a political decision to load up the FSC/ETI JOBS Act with all kinds of political message amendments designed to stoke worker's fears about the economy. I hope they will reconsider this approach

when we return to the bill after the recess. The European Union is imposing sanctions, and American manufacturing needs a shot in the arm. America's manufacturing future is too important to be playing political games with this bill.

I said earlier we are at a crossroads. Politicians can play on people's fear, throw up barriers to trade, and seek to isolate America from the global economy. Or we can do what we did in the 1980s—rise to meet the real challenges of the world economy. I know President Bush and his team, including Ambassador Zoellick, will not run from these challenges. My message today is simple. If we are going to sustain the prosperity this country has experienced for the past 50 years, we must remain steadfast in our support of open markets. We simply cannot allow our economic policy to be guided by the politics of fear. Mr. Ambassador, we have a lot of important issues to discuss today. I thank you for being here and look forward to your testimony.

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PREPARED STATEMENT OF HON. ORRIN G. HATCH

Thank you, Mr. Chairman.

Ambassador Zoellick, thank you for being here. When I think of the work done by your small agency in the last year, in fact, since the beginning of this Administration less than four years ago, I am impressed and grateful. I am impressed because the number of agreements initiated, negotiated, and concluded is, quite frankly, remarkable. With exports contributing what appears to be a steady one-quarter of our GDP growth, with the U.S. economy appearing to rebound, and with the President so adamantly committed to supporting a global economic regime that stimulates the free market to provide stability and hope throughout the world, your mission is one of the most important in this Administration. I commend you and your team for the hard work of the past years.

I am grateful because my constituents in Utah benefit from your work. Total Utah exports grew by nearly 30 percent between 2001 and 2002, and that means jobs for my constituents. With our NAFTA partner of Mexico, Utah exports grew by almost 20 percent. With Singapore, trade grew by over 400 percent—and these are figures prior to the passage of our FTA with that country. So, clearly, the structures of trade agreements that you are advancing around the world are facilitating commerce, and when you do that, everyone benefits—suppliers' businesses grow and they add jobs; consumers' costs fall and suppliers and families see the benefits in cheaper prices.

We took a stumble in advancing the global trade agenda in the WTO at Cancun last year, but we didn't accept one-sided deals. I commend you for seizing on the sentiment of many participants in the WTO that all of us missed an opportunity, and you are right in resuming negotiations with common-sense suggestions to re-enliven the talks. This is the nature of negotiations, and stumbles should never allow us to lose our focus on the Administration has committed to: pressing the WTO to address trade-enhancing measures across the board.

While I have a number of questions to raise about particular issues, I would like to close by commending your efforts to build trade capacity in nations not yet ready to enter into FTAs. Building a global free trade regime takes vision; an FTA is the end-game in a process that can often take years, if not decades. To get nations to buy into the President's vision, this Administration has been correct to invest significant funds to assisting developing countries in building their trade sectors, and we are not wasting money by being the single largest donor of trade-related technical assistance in the world. While you and your team work to strengthen the WTO, and advance multilateral and bilateral FTAs to build a web of international free commerce, it is important that we assist as many nations as we can in preparing their trading sectors to join a global regime from which we all will benefit.

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PREPARED STATEMENT OF HON. RICK SANTORUM

Mr. Chairman, thank you for convening this hearing and for your efforts to be an advocate for promoting free and fair trade.

Ambassador Zoellick, I want to extend my thanks to you for your continued efforts to open new markets for U.S. goods and services. With 25% of America's recent economic growth tied to our exports, your efforts to remove foreign trade barriers is helping to foster job creation in the United States. Oftentimes, Americans fear the uncertainty associated with new trading relationships.

I am glad to see that in addition to being a strong proponent to opening new markets, you recognize the need to address those who have lost jobs and the need to

provide assistance and training to these displaced workers. In your prepared testimony, you spend a great deal of time addressing the efforts of you and your staff to enforce China's compliance with trade obligations. I am heartened by your remarks, and I urge you and your staff to remain engaged with your Chinese counterparts on issues such as intellectual property rights, tax policy, and textiles.

The Administration has set an ambitious trade agenda for 2004. With recently concluded negotiations with Australia, Morocco, and five Central American countries, Congress will be asked to vote on agreements that, if adopted, will impact the lives of current and future generations of Americans. Additionally, the Administration is conducting negotiations with the five countries of the Southern African Customs Union, has signaled its intention to negotiate free trade agreements with Bahrain and Thailand, is pressing forward on a Free Trade Area of the Americas, and, through your personal efforts, is looking to jumpstart the stalled Doha Development Agenda at the World Trade Organization. As busy as 2003 was for you and your office, 2004 is perhaps even more ambitious.

As you know from previous correspondence, I am concerned that the United States did not come away from our free trade agreement negotiations with Australia with better outcomes regarding pharmaceutical price controls and sugar. While I am pleased to see you were able to secure greater transparency with regard to the operations of Australia's Pharmaceutical Benefits Scheme, I am disappointed to learn that little was done to eliminate the practice of reference pricing employed by the Government of Australia. The use of reference pricing or price controls by foreign governments—if left unchecked—will undoubtedly decimate our pharmaceutical industry and will stifle the innovative breakthroughs of life saving medicines. This industry, the employer of hundreds of thousands of Americans, improve the lives of people around the world more than almost any other industry. American companies lead the world in revolutionary advancements. Price controls or reference pricing will deprive our industry of the funds necessary to foster future research. I urge you not forget the importance of the pharmaceutical industry to our country, and to avoid signing trade agreements that do not recognize the amazing advancements provided by this industry.

Regarding sugar, I am disappointed to see that American consumers will continue to pay far more than the world price for sugar. I held great hope that our negotiations with Australia would lead to real gains for our consumers who pay three times what other consumers around the world pay for sugar. I am also concerned by reports that sugar was not an item for discussion during our talks with Australia. As you may know, given the high cost of sugar here in the United States, domestic candy and confectionary manufacturers are closing up shop here in America and moving abroad to manufacture. Some estimates calculate that our protectionist policies on sugar have cost the confectionary industry 7,500-10,000 jobs over the past six years. In the future, I urge that you not take items off the table when negotiating free trade agreements.

Thank you, Mr. Chairman, for convening this hearing and thank you, Mr. Ambassador, for your willingness to appear before the Committee and to discuss the Administration's trade objectives for 2004. I look forward to your testimony.

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PREPARED STATEMENT OF HON. GORDON SMITH

Thank you, Mr. Chairman. I thank Ambassador Zoellick for testifying today and for coming to the United States Senate to give a picture of the Administration's international trade agenda.

I am firm believer in the benefits of free trade. The dissemination of knowledge and understanding is the best course toward achieving global prosperity and peace. Our communication with trading partners has continuously improved due to our expanding trade relations. We are now actively pursuing trade agreements with Australia, Thailand, Singapore, and other friendly countries.

Ambassador Zoellick and his staff have done an exceptional job with the trade negotiations. However, I would like to take this opportunity to call for trade negotiations with one of our closest allies; New Zealand. I recently returned from Australia and New Zealand, and as a result of my discussions there, I now fully understand the need for moving ahead with a U.S.-New Zealand FTA in conjunction with our efforts on a U.S.-Australia FTA. By completing an FTA with Australia and not signaling our intentions to do the same with New Zealand will unnecessarily hurt the New Zealand economy.

Although an outdated nuclear policy remains in place, it has not stopped New Zealand from actively supporting our efforts in Afghanistan and Iraq, including deployment of ground troops in both countries. I feel just as certain that if we use

the difference of opinion over this policy as a reason—spoken or unspoken—not to move ahead on an FTA, then we will ensure that it will be the official policy of New Zealand as is for years to come. I believe movement is only possible if we strengthen our ties with New Zealand, and an FTA is a definite step in that direction.

Our continued leadership in the global marketplace is necessary to remain innovative. Subsequently, we need to be practical and fastidious in our bilateral trade agreements. Only the marketplace can determine the allocation of resources and capital. Therefore, we must resist the urge to over burden trade agreements with government regulation; yet remain sensitive to vulnerable industries in the U.S. and abroad.

Mr. Chairman, thank you for holding this hearing and I look forward to Ambassador Zoellick's testimony. The President's international trade agenda is an important part of our countries continued economic recovery. I look forward to working with the Administration in securing further bilateral trade agreements with our allies. Thank you.

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PREPARED STATEMENT OF HON. ROBERT B. ZOELICK

Chairman Grassley, Senator Baucus, Members of the Finance Committee:

*Introduction: The Challenge Ahead of Us*

It is a pleasure to be with you again. I want to start by thanking all of you— from both parties—for the support and advice you have provided us, not only over the last year, but for the past three years.

Together we are accomplishing some important results for America.

Yet I know the benefits of trade are a subject of debate.

Consider this statement:

“With America's high standard of living, we cannot successfully compete against foreign producers because of lower foreign wages and a lower cost of production.” Perhaps this pessimism sounds familiar. It could very well have come from one of today's opponents of trade, arguing against a modern-day free trade agreement. But in fact these words were written by President Herbert Hoover in 1929, as he successfully urged Congress to pass the disastrous Smoot-Hawley Tariff Act that raised trade barriers, destroyed jobs, and deepened the Great Depression.

Today, as in the 1930s, trade can be a contentious subject. But as we learned 75 years ago, isolating America from the world is not the answer. We need to open markets for American companies to compete in the world economy, so we can create new jobs and build economic strength at home. When we work with the world effectively, America is economically stronger. Ninety-five percent of the world's customers live outside our borders, and we need to open those markets for our manufacturers, our farmers and ranchers, and our service companies. Americans can compete with anybody—and succeed—when we have a fair chance to compete. Our goal is to open new markets and enforce existing agreements so that businesses, workers, and farmers can sell their goods and services around the world and consumers have good choices at lower prices.

Opening foreign markets to U.S. products and services is vital to economic growth, and an expanding economy is the key to better-paying jobs. U.S. exports accounted for about 25 percent of U.S. economic growth during the last decade and supported an estimated 12 million American jobs.

When the world's consumers fly in an airplane, boot up a computer or watch a movie, they are helping to employ Americans. And 6.4 million Americans have jobs working for foreign companies, building cars in Ohio, Kentucky, Tennessee, Alabama and South Carolina—or processing mortgages in Minnesota or engineering software in California.

Although we have opened many markets, too many foreign countries still will not let us compete on an equal footing. They keep our products out, they illegally copy our technology, and they block us from providing services. We want to make sure our products and services get a fair chance to compete, and to be vigilant and active in enforcing our trade agreements so that American workers have a level playing field.

Recent U.S. trade agreements have cut hidden import taxes and saved every working family in America as much as \$2,000 a year, and our newest agreements could add more to these savings. Arguing for trade barriers is like arguing for a tax on single working moms, because that's who pays the most in import taxes as a percentage of household income. Our goal is to cut those hidden import taxes—while other countries cut theirs too—to give working families a boost.

At the same time, we need to help people manage change—particularly when it concerns jobs. Jobs not only provide for our families, they give us hope for a better tomorrow. Losing a job is hard, whether it is because of a recession, changing technology, or competition from another state or overseas. No matter the cause, it is important to help someone who loses a job to get back on his or her feet.

That's why Congress and the President tripled Trade Adjustment Assistance in the Trade Act of 2002. In 2003, this program provided some \$1.3 billion in support and retraining, with nearly 200,000 workers eligible for assistance.

That's why the President is focused on helping workers to learn new skills for the jobs of the future. His Jobs for the 21st Century initiative provides over \$500 million in new funding for education and job training, including \$250 for community colleges to provide workers job training and skill development.

And that's why the private sector has an important role too: Today American companies spend \$70 billion a year on worker education and training, and they will need to expand this investment in people for the future.

Some of today's opponents of trade, like those of yesteryear, want to retreat, to cut America off from the world. But we need to remember that what goes around, comes around: If we close America's markets, others will close their markets to America. And the price of closing markets is larger than economic isolationists recognize. Over the last decade, trade helped to raise 140 million people out of poverty, spreading prosperity and peace to parts of the world that have seen too little of both. Americans will not prosper in a world where lives of destitution lead to societies without hope.

That's why President Bush's vision is of "a world that trades in freedom."

#### *Strategic Overview*

Three years ago, to support economic growth, an innovative America, development, and fair and open engagement with the world, the Bush Administration outlined a trade strategy for America. At the heart of our effort has been a plan to pursue reinforcing trade initiatives globally, regionally, and bilaterally. Through an ambitious trade agenda, the United States is working to secure the benefits of open markets for American families, farmers, workers, consumers and businesses. By pursuing multiple free trade initiatives, we are creating a "competition for liberalization" that provides leverage for openness in all negotiations, establishes models of success that can be used on many fronts, and develops a fresh dynamic that puts America in a leadership role.

This strategy is producing results.

With the able leadership of Chairman Grassley and Senator Baucus, as well as other members of this Committee, the President secured Congressional approval of the Trade Act of 2002.

The United States was instrumental in defining and launching a new round of global trade talks at the World Trade Organization (WTO) at Doha in late 2001. That same year we completed the unfinished business of China and Taiwan's entry into the WTO, working from the bilateral trade terms established by President Clinton, so as to establish a legal framework for expanding U.S. exports and integrating China's economy into a system of global rules. Also in 2001, the Administration worked with Congress to pass a Free Trade Agreement (FTA) with Jordan and a basic trade accord with Vietnam. After the 2000 election, President Clinton had announced an interest in FTAs with Singapore and Chile, and this Administration negotiated state-of-the-art accords in 2001-02 and gained Congressional approval in 2003.

A critical aspect of the Trade Act of 2002 was the renewal of the President's trade negotiating authority. In 2003 and early 2004, the Administration put that authority to good use, promoting global negotiations in the WTO, working toward a Free Trade Area of the Americas (FTAA), completing and winning Congressional approval of free trade agreements with Chile and Singapore, launching bilateral free trade negotiations with 14 more nations (concluding talks with seven of them), announcing its intention to begin free trade negotiations with six additional countries, and putting forward regional trade strategies to deepen U.S. trade and economic relationships in Southeast Asia and the Middle East.

The Trade Act of 2002 also renewed and improved trade preferences covering an estimated \$20 billion of business with developing countries in Africa, Latin America, and Asia through the renewal and improvement of the Andean Trade Preference Act, the African Growth and Opportunity Act, and the renewal of benefits under the U.S. Generalized System of Preferences. In addition, the Trade Act of 2002 tripled the level of trade adjustment assistance available to U.S. workers to nearly \$6 billion over five years.

USTR, working closely with other federal agencies, works to make sure that our trading partners live up to their commitments. A significant amount of the day-to-day work of USTR is spent pressing foreign officials to abide by their trade obligations.

Just to give an example, successes over just the past few months include pushing China to certify biotech imports of U.S. soybeans, cotton, corn, and other products, getting China to open up its car financing market, urging the Philippines to permit direct access for U.S. telephone calls, pressing investment disputes with the Andean countries close to resolution, and reopening the Mexican market to U.S. beef.

We resolve most problems without resorting to formal dispute proceedings, which take additional time and involve uncertain outcomes. Most U.S. companies suggest formal dispute proceedings only as a last resort. When we determine it will be the most effective way to settle disputes, we pursue cases under the WTO, NAFTA, or our new FTAs.

In particular, we are devoting more enforcement resources to China. While U.S. exports to China support more jobs for American workers, we face a number of persistent problems that must be resolved. I spend a significant amount of my time addressing matters such as Chinese tax policies that disadvantage American exports of products as diverse as semi-conductors and fertilizer; rampant piracy of intellectual property rights; technical commercial standards that are drafted to exclude foreign economic participation—such as on wireless encryption; among other concerns. Ensuring that these trade barriers do not stand is important to achieving the long-term benefits of China's WTO accession package: greater openness, adherence to the rule of law, and the institutionalization of market principles.

We recognize that enforcement of China's commitments requires sticks as well as carrots, and we are certainly willing to utilize the tools Congress has made available to us. These include the careful use of the China textile safeguard (which the Administration invoked for three product categories last December); anti-dumping laws; the product-specific safeguards; and WTO dispute settlement, an option that we may need to deploy very soon.

#### *Pressing Forward in the WTO*

At key points, the United States has offered crucial leadership to launch, prod, advance and reenergize the Doha Development Agenda, the global trade negotiations at the WTO. At the same time, we have emphasized that in a negotiation with 148 economies seeking consensus, others must also work constructively with us.

After the Doha launch, the United States proposed the elimination of all global tariffs on consumer and industrial goods by 2015, substantial cuts in farm tariffs and tradedistorting subsidies, and broad opening of services markets. We are the only major country to put forward ambitious proposals in all three core areas. These proposals reflect extensive consultations with Congress and the private sector.

In addition to laying the groundwork for bold market opening, the United States took the lead in resolving the contentious access-to-medicines issue in August 2003.

At the Cancun WTO meeting in September, however, some wanted to pocket our offers on agriculture, goods and services without opening their own markets, a position we will not accept. Since Cancun, I believe many countries have concluded the breakdown was a missed opportunity that serves none of our interests. That recognition is a useful starting point for getting the negotiations on track.

Only a few weeks after Cancun, more than twenty diverse APEC economies—encouraged by the United States and joined by some of our free trade partners—called for a resumption of WTO negotiations, using the draft Cancun text as a point of departure. In December, the WTO General Council completed its work for the year with an important report by its Chairman on the key issues that need to be addressed if the Doha Development Agenda is to move forward.

By late December, we sensed many WTO members were interested in getting back to the table, probably working from the draft text developed at Cancun. So in January I wrote a letter to all my WTO colleagues putting forward a number of "common sense" suggestions to move the Doha negotiations forward in 2004. I emphasized that the United States did not want 2004 to be a lost year. The letter suggested that progress this year will depend on the willingness of Members to focus on the core agenda of market access for agriculture, manufactured goods, and services.

In agriculture, we believe that WTO Members need to agree to eliminate agricultural export subsidies by a date certain, substantially decrease and harmonize levels of trade-distorting domestic support, and seek a substantial increase in real market access opportunities both in developed and major developing economies. The United States continues to stand by its 2002 proposal to set a goal of total elimination of trade-distorting agricultural subsidies and barriers to market access.

For manufactured goods, we are proposing that WTO Members pursue an ambitious tariff-cutting formula that includes sufficient flexibility so that the methodology will work for all economies. In addition to the tariff-cutting formula, sectoral zero-tariff initiatives need to be an integral part of the negotiations, perhaps using a “critical mass” approach to define participation as in the successful Information Technology Agreement. We also underscored the need to develop specific plans to address non-tariff trade barriers effectively in the Doha negotiations.

In the important area of services, the United States suggested that Ministers press for meaningful services offers from a majority of WTO members, as well as make available technical assistance to help developing countries present offers. The services sector is an increasingly important part of economic development. More open services markets help provide the infrastructure for development. The sector also offers increasing opportunities for developed and developing countries to work together for mutual benefit.

Finally, we are asking that countries not permit the so-called “Singapore Issues” to be a distraction from our critical work on market access. We need to clear the decks. Based on extensive consultations in Africa and Asia, I believe we can move forward together on trade facilitation, which cuts needless delays and bureaucracy at borders and ports. I have urged my colleagues to drop the other topics.

The initial response to this initiative has been encouraging both from overseas and among domestic constituencies. To follow up the January letter, in February I traveled some 32,000 miles—around and up and down the world—to meet with representatives of over 40 countries to hear their ideas and encourage their commitment.

I believe we are regaining some momentum, although the road ahead is marked by risks. Our ability to make notable progress by this summer depends principally, in my view, on two steps: one, reconciling the conundrum of the “Singapore Issues” by agreeing to focus solely on trade facilitation; and two, by concentrating on the draft agriculture text to see if we can agree on specific frameworks for reform. To secure movement on agriculture, all countries will need to agree to eliminate export subsidies, including the subsidy element of credit, to end State Trading Enterprise monopolies, and discipline food aid in a way that still permits countries to meet vital humanitarian needs.

#### *Advancing Negotiations in the Free Trade Area of the Americas*

Since taking office, the Administration has been working to transform years of general talks about a Free Trade Area of the Americas (FTAA) into a real initiative to open markets in the hemisphere, with a focus on first removing the barriers that most affect trade. The FTAA would be the largest free trade zone in the world, covering 800 million people with a combined gross domestic product of over \$13 trillion. It would expand U.S. access to Western Hemisphere markets, where tariff barriers are currently much higher than the trade-weighted U.S. average of 2 percent, and where non-tariff barriers are abundant. Studies report that an average family of four would see an income gain, through greater purchasing power and higher income, of more than \$800 per year from goods and services liberalization in the FTAA.

At the Summit of the Americas in Quebec City in 2001, the United States started to lead the FTAA into a period of concrete market access negotiations. In February 2003, the Administration put forward—on schedule—its comprehensive and significant market access offers to FTAA partners in the areas of agriculture, industrial goods, services, investment, and government procurement. But others hesitated.

Therefore, in November 2003, at the FTAA Ministerial in Miami co-chaired by the United States and Brazil, we developed a pragmatic approach to match the different circumstances of the 34 nations of the hemisphere—ranging from small Caribbean island states to the United States. We agreed to establish a common set of rights and obligations covering all nine areas under negotiation and that benefits would be commensurate with obligations undertaken. In addition, we agreed that nations that are prepared to go further could do so through plurilateral arrangements in some areas. This higher level of commitment—and benefit—creates incentives for countries to do more, without leaving others behind. The countries most likely to be ambitious are the ones that work with us on our gold-standard bilateral FTAs.

The FTAA will not be an easy negotiation, as this Committee knows. Yet we are committed to working creatively and flexibly with our hemispheric partners to achieve a long-held dream: the free flow of commerce throughout the Americas.



*Spanning the Globe With Bilateral Free Trade Agreements*

Miami also provided the venue for the announcement of several new U.S. bilateral free trade initiatives, demonstrating how our movement on multiple fronts can support our larger trade goals.

In 2003, the United States signed free trade agreements with Chile and Singapore, and those agreements won strong bipartisan majorities in Congress. These comprehensive, state-of-the-art FTAs set modern rules for 21st Century commerce and broke new ground in areas such as services, e-commerce, intellectual property protection, transparency and anti-corruption measures, and enforcement of environmental and labor laws to help ensure a level playing field for American workers. They also built on the experience of prior free trade agreements and will serve as useful models to advance other U.S. bilateral free trade initiatives in 2004.

In Latin America, for example, the long-sought FTA with Chile took effect on the tenth anniversary of NAFTA, and only two weeks after the Administration concluded a U.S.-Central America Free Trade Agreement (CAFTA) with El Salvador, Guatemala, Honduras, and Nicaragua. In January, we finalized CAFTA by resolving a few remaining issues with Costa Rica, and on February 20, the President notified Congress of his intent to enter into that agreement. Meanwhile, we continue to work to integrate the Dominican Republic into CAFTA, and indeed this week we are conducting the third and, we hope, final round of negotiations with the Dominicans. CAFTA plus the Dominican Republic would create the second-largest U.S. export market in Latin America, behind only Mexico.

This spring the United States intends to launch new FTA negotiations with Panama, Colombia, and possibly Peru and Ecuador, while continuing preparatory work with Bolivia. Added together, the United States is on track to gain the benefits of free trade with more than two-thirds of the Western Hemisphere through state-of-the-art, comprehensive subregional and bilateral FTAs.

Just last month, we concluded a landmark free trade agreement between the United States and Australia. On February 13, President Bush notified Congress of his intent to enter into this "Manufacturing FTA." Our terms with Australia will eliminate tariffs on more than 99 percent of U.S. manufactured goods exports to Australia on day one. Those exports account for 93 percent of total U.S. sales to Australia's large market, and support 150,000 good-paying American jobs. In creating new export opportunities for America's manufacturers, this deal will help a recovering sector of our economy while also expanding markets for America's services firms, creative artists, and farmers.

With virtually all U.S. manufactured exports going duty-free immediately under this agreement, America's manufacturers estimate they could sell \$2 billion more per year to Australia. They predict that U.S. national income would grow by nearly that much as well. Markets for services such as life insurance and express delivery will be opened, too; intellectual property will be better protected; U.S. investments will be facilitated; and American firms will be allowed to compete for Australia's government purchases on a nondiscriminatory basis for the first time. All U.S. farm exports—more than \$400 million per year—will go duty-free to Australia, benefiting many sectors such as processed foods, fruits and vegetables, corn oil, and soybean oil.

In Southeast Asia and the Middle East, the President has announced initiatives to offer countries a step-by-step pathway to deeper trade and economic relationships with the United States. The Enterprise for ASEAN Initiative (EAI) and the blueprint for a Middle East Free Trade Area (MEFTA) both start by helping non-member countries to join the WTO, strengthening the global rules-based system. For some countries further along the path toward an open economy, the United States will negotiate Trade and Investment Framework Agreements (TIFAs) and Bilateral Investment Treaties (BITS). These customized arrangements can be employed to resolve trade and investment issues, to improve performance in areas such as intellectual property rights and customs enforcement, and to lay the groundwork for a possible FTA.

President Bush announced the Enterprise for ASEAN Initiative in October 2002. Significant progress was made in 2003, and the stage has been set for further achievements in 2004. With the newly enacted Singapore FTA to serve as a guidepost for free trade with ASEAN nations, the President announced that he would begin negotiations for a comprehensive free trade agreement with Thailand in the second quarter of 2004, and on February 12th, we formally notified Congress of our intent to launch FTA negotiations with Thailand. At the Cancun WTO Ministerial last September, Cambodia was offered accession to the World Trade Organization, so it could take another step toward active participation in the global rules-based economy. Spurred by the progress of its neighbors, Vietnam is also working toward WTO membership, building on the foundation of a basic bilateral trade agreement

with the United States that was enacted by Congress in 2001. The United States signed a bilateral trade agreement with Laos in 2003, and the Administration continues to support granting Normal Trade Relations (NTR) to Laos. The United States is using TIFAs with the Philippines, Indonesia, and Brunei to solve practical trade problems, build closer bilateral trade ties, and work toward possible FTAs.

The Middle East Free Trade Area initiative, announced by the President in May 2003, offers a similar pathway for the Maghreb, the Gulf states, and the Levant. In addition to helping reforming countries become WTO Members, the initiative will build on the FTAs with Jordan, Israel, and now Morocco; provide assistance to build trade capacity and expand trade so countries can benefit from integration into the global trading system; and will launch, in consultation with Congress, new bilateral free trade agreements with governments committed to high standards and comprehensive trade liberalization.

The U.S.-Jordan FTA entered into force in December 2001 after close bipartisan cooperation between the Administration and Congress. As a result, trade between the United States and Jordan has nearly tripled in only three years.

In 2003, the Administration launched free trade negotiations with Morocco, which we are pleased we completed just last week. Immediately upon the agreements entry into force, 95 percent of bilateral trade in industrial and consumer goods will become duty free, the best day-one tariff elimination in a U.S. free trade agreement with a developing country. Our terms with Morocco provide immediate cuts in Moroccan trade barriers to wheat, corn and soybeans, and new access for U.S. beef and poultry; openings for service providers like audiovisual, telecommunications, distribution, and engineering firms; and new opportunities for manufacturers of construction equipment, chemicals and information technology.

In January 2004, the United States began free trade negotiations with Bahrain. Last week Representatives Paul Ryan and Jim Turner launched a Congressional Bahrain Caucus backed by more than 20 other members of the House and Senate. The caucus will work with a Bahrain FTA business coalition representing firms ranging from heavy manufacturers and leading-edge technology companies to small businesses.

Morocco and Bahrain have been leaders in reforming their economies and political systems. Our market opening efforts with these two Arab states are part of the opening act in President Bush's Middle East Initiative, which is aimed at fostering prosperity, encouraging openness, and deepening economic and political reforms throughout the region.

In 2004, the United States will continue its efforts to bring Saudi Arabia into the WTO and will expand its network of TIFAs and BITs throughout the region. The United States now has ten TIFAs in the region, most recently signing agreements with Saudi Arabia, Kuwait, and Yemen. We plan to sign TIFAs with Qatar and the United Arab Emirates soon. As additional countries in the Middle East pursue free trade initiatives with the United States, the Administration will work to integrate these arrangements with the goal of creating a region-wide free trade area by 2013.

In Africa, the African Growth and Opportunity Act (AGOA)—enacted in 2000 and expanded in 2002—has created tangible incentives for commercial and economic reform by providing enhanced access to the U.S. market for products from 37 eligible sub-Saharan nations. Enhancements made in 2002 to the African Growth and Opportunity Act improved access for imports from beneficiary sub-Saharan African countries. We look forward to working with Congress on legislation on AGOA that will accelerate its gains, including by extending provisions and enabling countries to take full advantage of AGOA through enhanced technical assistance.

To build on this success, as called for in the AGOA legislation, the United States launched FTA negotiations with the five countries of the Southern African Customs Union (SACU): Botswana, Lesotho, Namibia, South Africa, and Swaziland. The U.S.-SACU FTA will be a first-of-its-kind agreement with sub-Saharan Africa, building U.S. ties with the region even as it strengthens regional integration among the SACU nations.

The bilateral FTAs we have concluded or are pursuing constitute significant markets for the United States. U.S. goods exports to these countries were \$66.6 billion in 2003. This would have made them the third largest U.S. export market behind only Canada and Mexico, and ahead of Japan. The economies of these countries totaled \$2.5 trillion in 2002 at purchasing power parity exchange rates, which would rank them as the world's sixth largest economy. And most are developing countries that offer significant growth opportunities in years to come. We are laying free trade foundations for win-win economic ties between America and these partners.

*Ensuring a Level Playing Field with China*

Since China joined the WTO, it has become America's sixth-largest export market. U.S. exports to China grew 75 percent over the last three years, even as U.S. exports to the rest of the world declined because of slow global growth. China has become a major consumer of U.S. manufactured exports, such as electrical machinery, transportation and telecommunications equipment, numerous components, and chemicals. The market share of U.S. service providers in China has also been increasing rapidly in many sectors. Meanwhile, growth in exports to China of agricultural products has been robust; for example, U.S. exports of soybeans reached an all-time high in 2003 of \$2.9 billion and cotton exports were \$733 million, up 431 percent over 2002.

In 2003, senior Administration officials met frequently with Chinese counterparts to address shortcomings in China's WTO compliance. We delivered a clear message: China must increase the openness of its market and treat U.S. goods and services fairly if support in the United States for an open market with China is to be sustained.

As a result, China has taken steps to correct systemic problems in its administration of the tariff-rate quota (TRQ) system for bulk agricultural commodities, and relaxed certain market constraints in soybeans and cotton trade, enabling U.S. exporters to achieve record prices and sales. Recent approval of biotech soybeans, cotton and corn—and promised additional approvals—has created greater certainty for U.S. exporters. China has also reduced capitalization requirements for financial services, including opening the motor vehicle financing sector.

China's large installment purchases of billions of dollars of U.S. products—including Boeing 777s and 747s, GE and Pratt & Whitney aircraft engines, Ford and General Motors cars, as well as agricultural products—during recent purchasing missions bode well for 2004. However, we continue to stress the need for structural change that ensures ongoing, open, and fair access—not reliance on one-off sales.

In 2004, the Administration will concentrate on ensuring that: American intellectual property rights are protected; U.S. firms are not subject to discriminatory taxation; market access commitments in areas such as agriculture and financial services are fully met; standards are not used—whether for technology or farm products—to unfairly impede U.S. exports; China's trading regime operates transparently; and promises to grant trading and distribution rights are implemented fully and on time. The Administration will consult closely with Congress and interested U.S. stakeholders in continuing to press China for full WTO compliance, and will not hesitate to take action to enforce trade rules.

China's lax enforcement of intellectual property rights, including counterfeiting, is a fundamental issue. Piracy of movies, music and software is so rampant in China that the practices could subvert the development of knowledge industries and stifle innovation around the world. The scope and magnitude of the problem does not just threaten outsiders, but China's own citizens as well. Counterfeit automobile brakes, electrical switches, medicines and processed foods with pilfered brand names and poor quality control present health and safety risks throughout China. Premier Wen Jiabao has spoken of the importance of IPR and has assigned Vice Premier Wu Yi, a former trade minister who helped defuse the SARS crisis, to chair a working group on IPR enforcement. She will meet with Secretary Evans and me next month as part of our Joint Commission on Commerce and Trade.

In addition, China has adopted discriminatory tax policies—most blatantly on semiconductors—and new wireless encryption standards intended to block U.S. market access. We are pressing China to resolve these disputes promptly.

At the end of this year China and the United States face another challenge. Our Uruguay Round commitments, ratified by Congress, required us to begin phasing out our textile and apparel quotas in 1995. That process will be completed at year's end. We have urged the Chinese to recognize concerns raised by this important transition. We are committed to using special safeguards, applying unfair trade laws, such as the antidumping provisions, and taking action under international trade rules if China falls short in its trade commitments.

*Promoting a Cleaner Environment and Better Working Conditions*

No country is doing more than the United States to push for strong labor and environmental provisions in international trade agreements. While some other countries talk about labor and the environment in the context of trade, only the United States is actually doing something to integrate these topics as an active part of its trade agenda. Following the negotiating objectives set forth by Congress in TPA, we are focused on combining effective enforcement with practical cooperation to improve labor and environmental conditions overseas. Our strategy varies depending

on the countries we are negotiating with, because conditions vary and one size does not fit all. But in general, we have a ground-breaking, three-part approach:

- First, we often find that the issue with working or environmental conditions is not the laws on the books in developing countries, it is with the enforcement of those laws. So our FTAs require that countries effectively enforce their own labor and environmental laws, backed up by enforceable dispute settlement procedures.
- Second, we need to understand and address the reasons that laws are not being enforced. Often in poor countries, it is a resource question. Labor Ministries are often poorly funded, and there is a lack of money devoted to enforcement, inspections, and awareness of worker rights. To address this issue, we are pursuing a cooperative approach, working with U.S. AID, the Department of Labor, EPA, the State Department and others to focus on real-world problems, such as a lack of trained inspectors at Labor Ministries, the lack of awareness of employees of their rights under existing laws, and the need for education about child labor. We seek the help of American companies and NGOs, too. We work with the Multinational Development Banks to coordinate projects with them. The provisions in our trade agreements also encourage the development of local civil society, through public participation and transparency so that reforms can be sustained by homegrown efforts.
- Third, we want to cooperate with countries to improve their laws where there are gaps. Chile, for example, repealed its Pinochet-era labor laws during the course of negotiating the FTA with the United States because we took a firm but cooperative approach. Just recently, one of my staff returned from Guatemala with news that the government is working hard to reduce its backlog of worker rights cases in its courts, because they know CAFTA is coming and they want to improve the climate for investment and trade. El Salvador has significantly expanded funding for its Labor Ministry, with monies targeted especially on inspection and enforcement. Morocco enacted a new Labor code that will take effect this year. These are just a few of the many examples where our combination of enforcement standards and cooperation is helping reform these societies.

Of course, free trade also helps developing countries grow, generating the resources for greater protection of workers' rights and the environment. Growing developing countries build a middle class that calls for better environmental and working conditions. Poor people also want better lives for their families. We will not improve their working conditions or environment by making it harder for them to sell the fruit of their labor.

We are putting this multi-faceted approach to trade and development into practice. The Chile and Singapore FTAs create the basis for cooperative projects to promote respect for international core labor standards and to support environmental protection and sound management of natural resources. Both agreements also require that parties effectively enforce their own environmental and labor laws.

The dispute settlement procedures of the new FTAs apply to all obligations of the agreements and set high standards for openness and transparency, such as open public hearings, public release of legal submissions by parties, and the opportunity for interested third parties to submit views. In all cases, the emphasis is on promoting compliance through consultation, joint action plans, and trade-enhancing remedies.

The FTAs with the Central American countries, Morocco, and Australia adopt similar approaches to labor and environmental provisions, but are each tailored to fit individual circumstances. In Central America, for example, the Administration has emphasized trade capacity building projects to enhance the awareness and enforcement of labor laws. We encouraged countries to work with the International Labor Organization (ILO) to identify areas for improvement in labor laws and enforcement. The ILO study found that while the labor laws on the books were generally good, there were some gaps that needed to be addressed, and enforcement needed to be improved. The CAFTA partners are already responding to a number of these recommendations. We are assisting with tradecapacity building and cooperation to help. The fragile democracies of Central America are now looking to the Congress to see whether you will back their drive for selfimprovement and reform.

#### *Building New Bridges: Trade Capacity Building*

The United States is the largest single-country donor of trade-related technical assistance in the world, reflecting its commitment to fostering developing countries full participation in the global trading system. As much as capacity building helps developing countries, it directly advances U.S. interests as well. Capacity building

assistance both improves the quality of trade agreements, increases the ability of our trade partners to fulfill their commitments, and creates the conditions for expanding trade and development.

The U.S. resources from USAID and a dozen other agencies totaled more than \$2.5 billion in funding for trade capacity building activities (FY2000 through FY2003). The United States provided \$752 million in trade capacity building activities in FY2003, up 18 percent from FY2002.

In the CAFTA, FTAA, Morocco and SACU FTA negotiations, the United States has established separate cooperative groups on trade capacity building to define and identify priority needs for trade-related development assistance. The United States also seeks to give eligible countries the capacity to take advantage of preference programs such as AGOA. For example, U.S. technical assistance linked to AGOA assists eligible countries to develop AGOA export strategies, establish linkages with American businesses, and meet U.S. food safety and other standards.

Looking ahead, the Administration will continue to assist the developing world in integrating trade into development strategies. This will include working with multilateral institutions and private sector donors to promote initiatives such as the FTAA's Hemispheric Cooperation Program, and the WTO Technical Assistance Plan and the Integrated Framework. In our efforts in this hemisphere, the Inter-American Development Bank has done excellent work helping us to break new ground meshing trade and development policy by creating new mechanisms to meet the needs of developing countries. We hope to encourage the World Bank to demonstrate similar flexibility and responsiveness.

Helping developing countries understand the importance of trade in services is another role for capacity building. International Monetary Fund and World Bank reports show that efficiency in the production of services is a force multiplier in helping developing economies grow. Studies demonstrate that openness in financial services and technology alone has boosted economic growth rates in developing countries by 1.5 percent. Additional services like transportation, distribution, education, and health are of critical importance in developing countries, both for the emergence of a competitive businesses and, more broadly, for social development and poverty reduction. When developing countries open their services markets, the United States benefits, too.

As bilateral trade negotiations are concluded, the United States will continue to assist trading partners in implementing their commitments and managing their transition to free trade. The Administration will also continue to work with countries to maximize the benefits of preference programs such as AGOA, the Andean Trade Preference Act, the Caribbean Basin Partnership Act, and the Generalized System of Preferences.

In addition, the Bush Administration is emphasizing the important contributions that small businesses make to the U.S. and global economies. Small businesses are a powerful source of jobs and innovation at home and an engine of economic development abroad. By helping to build bridges between American small businesses and potential new trading partners, these enterprises can become an integral part of our larger trade capacity building strategy. In our continuing work with the U.S. Small Business Administration, our Office of Small Business Affairs at the Office of the United States Trade Representative has: increased small business representation in its advisory committee system; included previously excluded small business industry sectors in new trade agreements, such as the inclusion of recycled clothing in CAFTA; and focused on issues of special concern to small businesses, such as trade facilitation, ecommerce, and intellectual property rights protection. Ensuring that American small business concerns are addressed in our trade policy results in stronger agreements that help to create jobs at home and abroad.

#### *Monitoring and Enforcing Trade Agreements*

We take pride in the progress we are making to negotiate new commitments to open markets for American products and workers, but the bulk of the work done day-in and day-out at USTR is to ensure that countries live up to their current commitments or to solve problems for American businesses and workers.

Congress created USTR to assure that trade policy—including enforcement—was centrally located within the Executive Branch. We take USTR's enforcement mandate seriously.

The scope of enforcement extends well beyond the number of cases brought before WTO or NAFTA tribunals. On any given day, there is a steady stream of U.S. companies in the Winder Building working with us to figure out how best to press foreign governments to live up to their commitments to open up their markets to U.S. goods and services.

The vast majority of enforcement efforts by USTR are brought to successful resolution without the need to resort to formal litigation. Most U.S. companies urge us to do everything that we can to resolve a problem without bringing a WTO or NAFTA case, given the amount of time such cases take.

In recent years, informal means of resolving trade issues have enabled biotech farm exports and key U.S. financial services to expand their access to the Chinese market. Japan has agreed to lower customs fees by 50 percent as well as increase intellectual property protections. Mexico has implemented rules for pharmaceuticals that respect U.S. patents, and Canada has dropped copyright legislation opposed by U.S. firms that use the internet. We solved pork, poultry, dry bean, and beef issues with Mexico. We increased access for poultry, pork, and beef in Russia. We addressed rice and motorcycle export problems and are improving IPR protection in Taiwan. We headed off Korea's attempt to close the market to Dodge Dakotas based on questionable tax classifications. We encouraged Hong Kong to clean up illegal production of optical discs. The list goes on and on.

But sometimes enforcement can only be achieved through litigation, and we stand prepared to bring WTO and NAFTA cases to secure compliance.

Some of our recent WTO victories include:

- An important case against Mexico on telecommunications worth \$500 million, according to industry. Under current law, Mexico allows its dominant company, Telmex, the exclusive authority to negotiate, on behalf of all carriers, the rate that U.S. telecom companies must pay to complete their calls in Mexico. These exorbitant rates penalize American and Mexican families seeking to maintain crossborder ties, raise the price of doing business across the border, and burden U.S. telecom firms with unnecessary costs.
- In December 2003, the United States won a major case before the WTO holding that Japan's import restrictions on U.S. apples are a violation of Japan's WTO obligations. Japan had argued that the restrictions were needed to protect Japanese plants from disease, but U.S. scientific evidence showed the apples could not transmit the disease. This is a valuable precedent against others that might use Sanitary/Phytosanitary Standards (SPS) to block farm products unfairly.
- The United States won an important victory in June 2003 when the WTO rejected India's challenge to U.S. laws on determining the country of origin of textile and apparel products.

We have pending cases against: the European Union's ban on new imports of genetically modified foods and against the EU's over-reaching on Geographic Indicators; Mexico's questionable anti-dumping duties on beef and rice; Canada's discriminatory practices affecting wheat; and against Egypt's textile tariffs.

As noted earlier in my testimony, we are focusing more of our enforcement resources on China. While some of China's compliance problems were initially viewed as growing pains as it brought laws and regulations into line with new WTO obligations, China must do more to ensure that it is living up to obligations. Without more progress on matters we have been pressing with China, we will certainly need to avail ourselves of our rights under the WTO.

Of course, our ability to demand that others follow the trade rules is strengthened when we address cases we lose. We very much appreciate Chairman Grassley's and Senator Baucus' effort to repeal the FSC law to end retaliation against U.S. exporters, and we urge others to support their work. We also look to work with Congress to remedy other U.S. violations, including the Continued Dumping and Subsidy Offset Act of 2000, the 1916 Act (reflecting early antitrust practice), Section 211 of the Omnibus Appropriations Act of 1998 concerning conditions that permit the banning of trademark enforcement, and the ruling on hot-rolled steel. America should not be a scofflaw of international trade rules.

#### *Conclusion*

I want to close by again thanking the Committee for its support and guidance. During 2004, we hope to continue to push forward step-by-step toward the vision set out by President Bush of "a world that trades in freedom." It is a vision of a world in which a working family can save money on everyday household items because trade agreements have cut hidden import taxes. It is a vision of a world in which an Iowa pork producer, a New York financial advisor, a Montana cattleman, an Illinois manufacturer of excavators, a Mississippi chicken farmer, or a California entertainer can sell his or her products or services in Costa Rica or Australia or Thailand or Morocco as well as across America. It is a vision of a world in which free trade opens minds as it opens markets, supporting democracy and encouraging tolerance. And it is a vision of a world in which hundreds of millions of people are lifted from poverty through economic growth fueled by trade.

## RESPONSE TO A QUESTION FROM SENATOR GRASSLEY

*Question.* It seems to me we've been dealing with two Japans recently. One the one hand, Japan has demonstrated real vision and leadership in support of the war on terrorism. The Japanese Government took a very difficult political decision to send some of their troops to Iraq. I want to thank them for that.

But when it comes to trade, it seems we've been dealing with another Japan. In the run-up to Cancun and during the ministerial, Japan did not seem to demonstrate leadership or a vision for achieving meaningful trade liberalization. The WTO negotiations will not go anywhere if the world's second largest economy isn't on board to help push for a final agreement.

What is your assessment of the support we're likely to get from Japan in moving the Doha negotiations forward this year?

*Answer.* To be sure, we were disappointed with Japan's performance at the WTO ministerial meeting in Cancun. Japan has, however, been somewhat more constructive since then. During my round-the-world trip in February, which I undertook to re-energize the Doha negotiations, I made Japan my first stop and met with Foreign Minister Kawaguchi, Trade Minister Nakagawa, Agricultural Minister Kamei, and nowformer Chief Cabinet Secretary Fukuda. Unlike the discussions in Cancun, those talks were somewhat more positive and focused on problem-solving.

During my visit, I encouraged the Japanese to join others in agreeing to the elimination of all forms of export subsidies by a date certain and substantial reductions in domestic support. Japan's narrow concerns on market access appear to be holding the Japanese back from showing this needed flexibility. Since that time, we have held a series of meetings with Japanese agricultural officials to explore ways to deal with their domestic sensitivities and our market access objectives. I am hopeful we can find a way to deal with Japan's concerns in a way that does not impair the integrity of the agriculture negotiations but deals with a serious sensitivity.

As a prime beneficiary of liberalized trade in industrial goods and services, Japan should be a leader in these negotiations. In industrial market access negotiations in 2004, Japan has been more active in pursuing liberalization and working constructively with third countries to achieve an ambitious result.

Japan has long been interested in the negotiations on trade rules, including trade remedies. Ironically, Japan is now seeing the importance of these rules from a different perspective as it deals with an increasingly competitive China. We will continue to work with the Japanese on the rule issues, including improving the disciplines on fish subsidies, an area of particular sensitivity to Japan.

Finally, with respect to the so-called Singapore issues of investment, competition, trade facilitation, and transparency in government procurement, Japan has long advocated negotiations on these issues, particularly investment. In a positive move, Japan has recently shifted its position and is now in support of negotiating only trade facilitation as part of the Single Undertaking. Japan, nevertheless, still wants to continue WTO work on the other three Singapore issues, which is opposed by many developing countries. This is a key issue that will continue to be taken up in the coming weeks.

## RESPONSES TO QUESTIONS FROM SENATOR HATCH

*Question 1.* Mr. Ambassador, I applaud your efforts to challenge Australia's Pharmaceutical Benefits Scheme during negotiations and I am pleased to note the success you experienced in addressing these issues of providing transparency and independence to the appeals process. As well, I was pleased to see you working hard to address the pricing issue by the inclusion of the Working Group on Medicines provision.

In my mind, the way large, developed countries, like Australia, address the issue of pricing is very important. Dictating prices will have a lasting and harmful effect on pharmaceutical research and development and will eventually lead us to a point where companies will no longer be willing to undertake the costly research to develop these drugs.

In my mind, the problem isn't that the U.S. does NOT use price controls, but rather that other countries ARE using them and not shouldering their fair share of the cost, thus, creating artificially high prices in the U.S.

It is my hope that these issues will be addressed by the Working Group on Medicines established in the Australian Agreement.

Can you explain how you believe the Working Group will be organized and operate and how successful you believe future trade negotiations will be in encouraging other countries to correct their pricing schemes?

*Answer.* Through recent and ongoing bilateral free trade agreements (FTAs), including our recent agreement with Australia, the United States is:

- Advancing transparency provisions that provide for greater openness for government decisionmaking on drug approvals and reimbursements.
- Pursuing state-of-the-art intellectual property rights (IRR) provisions that afford better protection for test data, extend patent terms to compensate for delays in granting the original patent, and help to prevent arbitrary patent revocation and the marketing of drugs that violate patents.
- Opening new markets to U.S. services and investment, giving American firms opportunities to provide supplemental health insurance and promote awareness of new medicines to consumers abroad.
- Eliminating costly customs duties on U.S. medicines exports worth hundreds of millions of dollars a year. Nearly all duties on U.S. pharmaceutical products were or will be eliminated immediately through our FTAs with Jordan, Chile, Australia, and the Dominican Republic. Most pharmaceutical products will be duty-free immediately on implementation of FTAs with Morocco and Central America, with the remainder removed over a phase-in period.

The Working Group established by the Australia FTA will be organized on a government-to-government basis and include the participation of health officials and trade experts on both sides. The Working Group can address the full range of issues covered by the annex and side letter in the FTA, including transparency and efficacy of the process, as well as recognizing the value of innovative medicines.

We are seeking similar significant results in ongoing negotiations with the Southern African Customs Union, Thailand, and the Andean countries.

In a related area, we have been making progress with Japan on pricing issues under the U.S.-Japan Regulatory Reform Initiative. Our annual regulatory reform report this year to President Bush and Prime Minister Koizumi, for example, includes steps Japan is taking to implement pricing reforms that more effectively recognize the value of innovative pharmaceuticals, and streamline and accelerate product approvals.

*Question 2.* We understand that by mid-2005, the U.S. could have concluded 22 free trade agreements. This is obviously a big drain on your resources. With this kind of aggressive negotiating strategy, I am concerned about your ability to meet other priorities.

In particular, I am thinking of your bilateral initiatives under Special 301 involving intellectual property protection where losses are significant to U.S. industry. Problems include China, Russia, and Brazil which alone account for close to \$3 billion in losses to the economy and these industries.

How do you plan to ensure that we get results under Special 301 when your resources are stretched so thin negotiating so many free trade agreements?

*Answer.* This Administration places a high priority on ensuring adequate and effective protection for U.S. intellectual property rights in foreign markets, and USTR is committed to maintaining the Special 301 process as an important tool to achieve this objective. Last year, USTR added an additional full-time position to our intellectual property office, which helps to ensure that the Special 301 process continues to be vigorously utilized and implemented. In addition, the USTR-led annual Special 301 Review is a closely coordinated interagency process utilizing the expertise and resources of our own regional offices along with several other relevant agencies such as State, Commerce, the Patent and Trademark Office, and the Copyright Office. We also work very closely with our embassies both to implement and monitor various initiatives undertaken under the Special 301 process.

Utilizing these resources both within USTR and our interagency team, we focused on key countries of concern such as China, Russia, and Brazil during this year's Special 301 Review. The 2004 Special 301 Report released in May identified both Brazil and Russia as priority watch list countries and urged their respective governments to take the necessary steps to address rampant piracy and other key IPR-related concerns. This year's report also announced an out-of-cycle review for China in early 2005 to evaluate China's implementation of its stated commitments and its overall progress on improving enforcement and significantly reducing IPR infringement.

*Question 2a.* As well, can you outline for me your two-tier proposal for dealing with intellectual property rights in Brazil in the Free Trade Area of the Americas (FTAA) negotiations?

*Answer.* As you know, this is not an easy negotiation. With respect to the plurilateral set of rights and obligations within the FTAA, the United States will continue to seek its model agreement, containing the standards of protection and enforcement provisions that we seek with all our bilateral FTA partners.

For now, Brazil has indicated that it is only willing to sign on to the common set of rights and obligations that will be applicable to all FTAA signatories. We are working diligently with Brazil and all our other negotiating partners to include in



the IPR chapter of the common set as many U.S. objectives on IPR protection as possible. We believe that the higher level of benefits offered to those countries that undertake additional commitments in the plurilateral negotiations will be an incentive for Brazil and others to undertake those additional commitments, including intellectual property protections.

*Question 3.* Ambassador Zoellick, the pharmaceutical industry is one of the top U.S. exporting industries along with the semiconductor, aerospace, and computer industries. This is an industry that produces high-paying manufacturing jobs—averaging over \$18 per hour. It is an industry that employs well over a million Americans. Eight out of ten new drugs developed today come from U.S. companies. The industry is increasingly threatened, however, by foreign government intervention designed to reduce local consumption of its products. The fact that the industry is so dominated by American firms makes it an easy target for other countries.

I am anxious to see the U.S. continue its market dominance in this sector, not only for the life-saving medicines they produce, but also because of the large amount of high-paying U.S. jobs they provide.

Can you outline for me your strategy for removing export barriers for pharmaceutical products and do you believe USTR is inadequately staffed on this issue to be successful?

*Answer.* The U.S. industry dominates the global market in part because our largely market-based regulatory and pricing regime attracts investment in the pharmaceutical sector. As a result, the United States has a thriving home-grown pharmaceutical industry, and foreign pharmaceutical firms have increasingly moved their R&D facilities and headquarters out of foreign markets and into the United States. Removing regulatory barriers in other markets will likely encourage additional investment in those markets. It may also make the global market more competitive and increase the R&D funding by providing greater incentives for the development of new innovative medicines.

A one-size-fits-all approach to dealing with foreign government interventions in the pharmaceutical market will not be effective given the varied ways in which foreign governments regulate in this area. We are currently developing a multi-pronged approach to dealing with the problem.

First, we are pursuing the expansion of the Uruguay Round zero-for-zero Pharmaceutical Agreement (in which 21 countries eliminated tariffs in the pharmaceutical sector) in two ways: (1) deepening the product coverage of the agreement to include highly-traded intermediate products; and (2) expanding the number of countries participating in the Agreement, with a particular focus on making the agreement more accessible for developing countries.

Given the fact that global trade is highly concentrated among current participants in the Agreement, U.S. industry's first priority is to take advantage of provisions in the Agreement that call for biannual updates as a means of pursuing expansion of product coverage. U.S. industry also supports efforts in the Doha Round to encourage more WTO members to participate in the Agreement and find ways to make it easier to implement. Work on expanding membership in the Agreement will continue as an important part of our overall strategy on non-agricultural market access negotiations. We have begun informal consultations with other Agreement participants to verify their interest and ability to pursue an update of product coverage.

Second, in the conference report accompanying the Medicare Prescription Drug, Improvement and Modernization Act of 2003, the Congress directed the Administration to examine one particular regulatory practice, i.e., drug pricing practices of OECD countries, and assess whether "those practices utilize nontariff barriers with respect to trade in pharmaceuticals." The conference report directs the Secretary of Commerce, in consultation with the International Trade Commission, the Secretary of Health and Human Services and the United States Trade Representative (USTR), to prepare a report designed in part to provide an "[e]stimate of the impact . . . price controls, intellectual property laws and other such measures have on fair pricing, innovation, generic competition, and research and development in the United States and each [OECD] country identified." The Administration is in the process of preparing this report.

The conference report also calls upon USTR, in conjunction with the Department of Commerce and the Department of Health and Human Services, to determine "whether bilateral or multilateral trade or other negotiations present an opportunity to address those price controls and other such practices and . . . [to] develop a strategy to address such issues in appropriate negotiations." Completion of the underlying report on OECD country practices will facilitate the development of a fully informed strategy. In the meantime, we will begin to raise this issue internationally, and are closely consulting with industry on this matter.

USTR is sufficiently staffed to handle this issue. I recently designated an Assistant U.S. Trade Representative (AUSTR) to be responsible for pharmaceutical policy. This position is assigned responsibility to address the further development of pharmaceutical policy in international trade. Clearly, however, any effort in this area will require a substantial contribution of resources and expertise from other agencies, including the Department of Health and Human Services (including the Food and Drug Administration), and the Department of Commerce.

*Question 4.* In 1984, Congress amended the Trade Act to make IPR protection a key criterion for countries receiving unilateral trade preferences under the General System of Preferences (GSP) and similar programs.

At that time and each time we renewed these programs, we urged the Administration to use this important leverage to encourage countries to improve protection. Congress' point was that we should not be providing unilateral benefits to countries which do not provide adequate protection for our intellectual property.

The use of this leverage has resulted in very significant improvements over the years, in Indonesia and Latin America. Recently, however, it appears as if this tool has not been as effectively used in negotiations.

Why aren't you using this tool to improve IPR protection?

*Answer.* GSP was re-established by the Congress in 2002. We are continuing to utilize GSP as a tool to improve IPR protection. It should be noted, however, that the removal of GSP benefits has consequences not only for the exporting country but also for U.S. importers and consumers, including businesses that depend on imported raw materials. These factors need to be weighed carefully when taking decisions on whether to remove GSP benefits. The threat of GSP removal, however, remains a useful tool. There are five ongoing country IPR-practice reviews including Brazil, Kazakhstan, Lebanon, Russia, and Uzbekistan. Often the initiation of a review itself provides effective leverage which results in positive engagement with the trading partner to strengthen MR. We are working closely with our IPR-related industries to achieve effective protection and enforcement of IPR by our trading partners through the various trade tools at our disposal, including GSP. For example, USTR has just announced that the Administration will extend Brazil's GSP eligibility review for a 90-day period. We have been in contact with the Government of Brazil to urge it to take concrete steps to improve copyright enforcement. This extension will allow an examination of progress Brazil is making to address the concerns both countries share regarding copyright piracy.

*Question 5.* Trade issues have recently generated significant media and public attention. The U.S. financial services industry is the world leader and yet our firms face significant impediments to fair competition in part of the world. The European Union's Financial Services Action Plan includes several directives that limit the ability of the U.S. firms to compete in Europe. These include the Financial Conglomerates Directive, the Investment Services Directive, and the Transparency Obligation Directive.

Of particular concern is the Financial Conglomerate Directive. Unless the EU makes a determination that the U.S. financial services regulatory system is "equivalent" to the European models, U.S. firms will face a number of sanctions that will impair their ability to compete on a global basis.

The directive comes into force in the near future and there is a need for an "equivalency determination" by the Europeans very soon.

Can you tell me how you view this situation and what steps you will take to obtain the "equivalency determination" before the Financial Conglomerates Directive goes into force?

*Answer.* The U.S. and EU financial authorities have been working closely together on the Financial Conglomerates Directive and other topics in the U.S.-EU financial market dialogue, which is part of our bilateral interaction under the Positive Economic Agenda. In doing so, EU regulators have held extensive discussions and consultations with the U.S. financial services community.

The Directive goes into effect in Member States in August 2004. Guidance for determining equivalence under the Financial Conglomerates Directive was issued in Europe in April 2004. This will be used by relevant EU Member States' regulators to judge equivalence, on a case-by-case basis, of U.S. conglomerates located within their jurisdiction. To facilitate findings of equivalence, all U.S. regulators (Federal Reserve Board, Office of Thrift Supervision, National Association of Insurance Commissioners, and Securities Exchange Commission) have been cooperating closely with Brussels and with EU Member State regulators to explain their approaches. The U.S. Government remains in close contact with EU financial authorities on this issue. Further questions on the details of this issue can be directed to the Treasury Department.

## RESPONSE TO A QUESTION FROM SENATOR THOMAS

*Question.* Ambassador Zoellick, I note from your Trade Policy Agenda report that “enforcement of existing trade agreements remains a top priority for this Administration.”

Nearly three years have passed since Brazil’s State of Rio de Janeiro imposed a tax which is 17% higher on U.S. soda ash than on soda ash produced in Brazil. This discriminatory tax is clearly in violation of GATT 1994’s national treatment commitments.

As you know, in October of last year, the U.S. industry filed a draft Section 301 petition with your office on this matter. In the same month, I joined Senator Enzi, Senator Smith, and Representative Cubin in a letter asking USTR for their support and assistance. This U.S. industry was advised in early November that a formal protest would be lodged with the Brazilian government.

Our domestic producers and the thousands of jobs dependent on this industry in my state and elsewhere are facing fierce competition to increase U.S. exports. Trade barriers throughout the world are hampering industry’s efforts to compete. You and your staff have been strong advocates for U.S. soda ash—from supporting efforts to lift the 7-year temporary restraining order in India to negotiating the elimination of tariffs in the Australia FTA—and I am forever grateful for those efforts.

Unfortunately, with industry-wide profit margins at historic lows and the U.S. industry being supplanted by China as the world’s largest soda ash exporter, all trade barriers are having a devastating impact on this once thriving U.S. export industry.

I strongly support the Administration’s continued recognition that enforcement of existing trade agreements is a top priority of the United States. I would be interested to hear the status of USTR’s efforts to address the situation in Brazil, and your thoughts on how quickly this issue might be resolved.

*Answer.* We have been working aggressively and closely with our industry to resolve this issue. Industry brought this matter to our attention, in part through the preparation of a draft Section 301 petition last fall. Industry representatives explained, however, that they did not believe that litigation would be the most effective means by which to address the problem. They instead asked that we raise this matter formally and at high levels with Brazilian officials. This is what we have done.

My Deputy, Ambassador Peter Allgeier, raised the issue of the State of Rio de Janeiro’s tax with the Brazilian Minister of Development, Industry and Foreign Trade during meetings in Brasilia in December.

To demonstrate the seriousness of our concerns in this matter, we followed up on Ambassador Allgeier’s meeting with a demarche to the Brazilian Government on April 15. The demarche set out our serious concerns regarding the state-level Brazilian tax on soda ash, asked that Brazil explain whether they believe the tax to be consistent with their WTO commitments, and requested Brazil to inform us of how they intend to address this apparent discrimination against imported soda ash.

On an informal basis, Brazilian officials have informed us of their need for time to confer with officials of the State of Rio de Janeiro to obtain details on the functioning of the tax. In the meantime, in concert with U.S. Embassy personnel in Brazil, we are continuing to engage the Brazilian Government on this topic to obtain an official Brazilian response to the demarche.

We will continue to work closely with our industry, and take all appropriate and effective measures to ensure optimal market access for U.S. soda ash producers.

## RESPONSES TO QUESTIONS FROM SENATOR SMITH

*Question 1.* The CAFTA provides a great benefit for the apple, pear, and cherry growers of Oregon and the Pacific Northwest. This agreement gives our growers immediate duty-free access into these countries, which is equal to what their competitors from Chile already enjoy. CAFTA helps prove to my growers that free trade agreements can provide equitable and immediate benefits. Will you pledge to strive to achieve this kind of successful outcome for my fresh fruit growers in other FTAs currently under negotiation?

*Answer.* We seek the best possible outcome for U.S. agriculture, including for apples, pears and cherries, in all of our trade negotiations. In our FTA negotiations, we continue to press other countries to eliminate tariffs as soon as possible for U.S. agricultural export priorities, including apples, pears, and cherries. We were able to achieve immediate tariff elimination on these products in the Central America (including the Dominican Republic), Australia, and Bahrain FTAs. Under the U.S.-Morocco FTA, tariffs on pears and cherries will be phased out in five years in equal annual increments. On apples, Morocco agreed to establish a new TRQ (seasonal—February through May) that will provide duty-free access for 2,000 metric tons of

U.S. apples upon entry into force of the Agreement, with 4 percent growth in this inquota quantity annually. The overquota rate of 52 percent (Morocco's current applied MFN rate) will be phased out over ten years in equal annual increments. We will continue to make these products a priority in subsequent FTA negotiations.

*Question 2.* The original U.S. position was not to negotiate food aid in the WTO. We recognize this will not be avoided. Please try to clarify what type of disciplines Mr. Zoellick would consider.

*Answer.* Food aid programs are currently covered by WTO rules which require food aid programs to be managed consistently with standards set in the FAO and the Food Aid Convention. Discussions in the WTO are focused on ensuring that food aid programs do not displace commercial sales. The United States shares this objective, both to foster the development of agricultural markets in developing countries and to protect U.S. commercial sales from unfair competition from food aid donations. Our position in these discussions in the WTO is to maintain intact key U.S. food aid programs while tightening rules that guard against abuse of food aid programs. That means we support disciplines that would require an assessment of market disruption of food aid programs before shipments are made and that would increase transparency of food aid activities. We are opposed to disciplines that would require all food aid to be channeled through UN organizations or that would limit food aid deliveries to emergency circumstances.

*Question 3.* The wheat industry believes that export state trading and/or export monopolies must be eliminated in any and all free trade arenas and any agreement in the WTO should prohibit monopoly exporting. How does the Administration see this issue being resolved in future FTAs and within the WTO?

*Answer.* The United States has a clear and straightforward position on the existence of agricultural monopoly export state trading enterprises—eliminate their monopoly export authorities. In the WTO negotiations, the United States tabled specific language in July 2002 to eliminate export monopolies, thus allowing any producer, distributor, or processor to export agricultural products. The United States also tabled language in the WTO to end special financial privileges granted to state traders and expand their WTO transparency obligations. We have made solid progress in achieving the U.S. objectives on state trading enterprises, developing an international coalition supporting our position.

Of those FTAs that have recently been negotiated or that are being negotiated, Australia is the only country with monopoly agricultural state trading enterprises, including the AWB, Ltd., Queensland Sugar Corporation and New South Wales Rice Marketing Board. In response to U.S. concerns about Australia's state trading enterprises, Australia (as part of the FTA) committed to work with the United States in the ongoing WTO agriculture negotiations to develop export competition disciplines that eliminate restrictions on the right of entities to export. Although the U.S. and Australia do not trade wheat bilaterally, Australia's commitment as a part of the FTA is an important achievement that will provide added impetus for achieving this goal in the WTO negotiations.

*Question 4.* We are concerned that FTAs are more focused on political needs and not focused on market growth opportunities. What criteria will future FTAs countries have to meet?

*Answer.* U.S. commercial interests are very important factors we consider when selecting potential free trade partners. When considering potential free trade agreement partners we consider a number of important criteria, which were developed through interagency deliberations. The criteria include the following: (1) country readiness; (2) economic and commercial benefits; (3) benefits to the broader trade liberalization agenda; (4) compatibility with U.S. interests; (5) Congressional and private sector interest; and (6) U.S. government resources.

Our new and pending FTA partners constitute America's 3rd largest export market and the 6th largest economy in the world. In addition, our current and pending FTA partners in the Americas encompass two-thirds of the Western Hemisphere's GDP (excluding the United States).

*Question 5.* The agriculture industry has long been aware of the opposition of developing countries toward U.S. domestic support programs and the pressures to give these programs up in the WTO negotiations. What assurances can the USTR give that no tradeoffs will be made without adequate increases in market access?

*Answer.* The U.S. negotiating objectives for agriculture in the WTO are based on substantial reform in each of the three pillars of market access, export competition, and domestic support. Our ultimate objective for reform in the WTO remains the elimination of all trade-distorting measures in agricultural trade in each of the three pillars. For the current round of negotiations, we will only accept an agreement that entails substantial reform in each pillar and balance across the pillars. U.S. agriculture has much to gain from global reform of export subsidies, trade-dis-

torting domestic support, and market access barriers. We will continue negotiating until we achieve a substantial and equitable result.

*Question 6.* Agriculture needs analytical work on whatever degree of market access is needed to offset the loss of domestic support programs. Will USTR work with USDA and producer groups to design/identify farm programs that will be WTO legal and provide economic stability for U.S. producers?

*Answer.* USTR works with USDA and other agencies to assess farm program proposals, focusing on WTO consistency of proposed changes in U.S. laws. We will continue to engage in this process of evaluating U.S. farm programs with respect to existing and potential new WTO disciplines.

*Question 7.* Grassroots agriculture is uneasy about trade agreements. Some just do not trust negotiators. An outreach program is needed in the U.S. to sell producers on the need for new agreements. Would USTR be able to work as hard in the agriculture community to promote the benefits of trade as it does with trading partners?

*Answer.* USTR and the U.S. Department of Agriculture work proactively to reach out to U.S. farmers and ranchers on the Administration's trade agenda. The hundreds of meetings and trips that USTR and USDA officials participate in, across the range of agricultural commodity groups, give the message that increasing agricultural exports are vital to the well-being of U.S. agriculture. In addition, USTR and USDA websites contain important agricultural trade information. With 96 percent of the world's consumers of food living outside the United States, we clearly need to increase U.S. agricultural exports to find homes for U.S. agriculture's increasing productivity.

*Question 8.* How is USTR planning on enforcing agreements? Will this be a USTR function or will industry have to carry the burden? Considering the number of FTAs in process and others proposed, are there sufficient resources, both personnel and fiscal, to meet implementation and enforcement needs?

*Answer.* USTR has been enforcing trade agreements for over 40 years. We have developed an enforcement strategy that seeks to maximize the benefits of the trade agreements we negotiate. This strategy is primarily preventative in that we seek to resolve trade issues before they become formal disputes. This strategy consists of a variety of mechanisms that include consulting informally; building local support; offering technical assistance; exploring mutually acceptable outcomes, including through our FTA negotiations; invoking U.S. trade laws; and threatening litigation. Yet, when disputes arise, our knowledge of the issues, the nuances and history of the agreements, and the fora themselves allow us to litigate both aggressively and successfully.

Interagency coordination is critical to this effort. To that end, USTR leverages the resources and expertise of other agencies, so that Federal resources are efficiently matched to the trade issue at hand. This coordination, which has been a central task of USTR since its creation, provides for the most flexible and effective enforcement of our trade agreements.

Indeed, when Congress created the Special Trade Representative in 1961, it relied on the logic of a "networked" organization long before that concept was popularized. Given the range of problems USTR addresses, we rely on the expertise, insight, and support of many other entities. USTR's placement within the Executive Office of the President fosters its ability to leverage resources throughout the government in the most effective and efficient manner.

U.S. industry plays a critical role in USTR's enforcement coordination structure. USTR's work is done in close conjunction with our 32 formal private-sector advisory groups encompassing more than 750 individuals and our networks with private-sector associations and businesses. Through the Advisory Committee for Trade Policy Negotiations (ACTPN) and its subcommittees, USTR promotes the flow of information to and from the private sector, which is central to our enforcement efforts. While U.S. industry is a valuable participant in the enforcement process, it is one among many which assists USTR in its enforcement of trade agreements.

In order to reinforce its implementation and enforcement efforts, USTR has responded to the increasing number and complexity of trade agreements in several ways. Using our current appropriation, we have: (1) increased the number of front-line attorneys in our General Counsel's office by 20 percent; (2) reestablished an Office of China Affairs and expanded the number of China negotiators at USTR by 100 percent; (3) increased the staff in our Office of Industry to cover the manufacturing economy and follow key industries; and (4) added staff in both Washington, D.C., and our Mission to the WTO in Geneva that are dedicated to enforcing China's WTO implementation obligations. In addition to focusing on these priority areas, USTR continues to work to improve the coordination of interagency enforcement efforts to promote the most effective mobilization of resources.

*Question 9.* I understand that in all the FTAs that you have negotiated you have succeeded in finding a reasonable and balanced solution to film issues in trade agreements. All of us have heard Jack Valenti lament about being thrown overboard by previous U.S. Trade Representatives. Your agreements ensure that our film industry has good access to the markets of our trading partners, while at the same time being respectful of others' cultural concerns. In today's international environment, standing up for our economic interests while also addressing foreign cultural concerns is an important and necessary balance to find. Can you give the committee a better understanding of your achievements in this area?

*Answer.* You are correct that in our FTA negotiations, we have ensured that our film industry enjoys good access to the markets of our trading partners while permitting our trading partners to protect legitimate cultural concerns.

In our FTAs with Chile, Morocco, Australia, CAFTA, and Bahrain, for example, we have obtained market access and national treatment obligations for the production, distribution, and exhibition of U.S. audiovisual products. This is balanced by a narrow exception that permits our FTA partner to enter into co-production agreements with third countries for cultural activities. While having little trade impact on the U.S. industry, this exception permits our trading partners, most of whom have small domestic markets, to pool their limited market size and scarce resources.

In addition, the U.S.-Australia FTA provides binding rules ensuring U.S. content suppliers reasonable access to the Australian market, while accommodating Australia's desire to maintain certain limited areas of discretion for broadcasting and digital services. Rules relating to the national treatment of content that were negotiated in the FTA provided an additional level of certainty by defining this balance in a binding framework that required Australia to take specific reservations for policies permitting limited cultural protections. Along the same lines, certain of the CAFTA countries were allowed to retain content restrictions with narrowly limited application.

*Question 10.* I understand that the copyright provisions in the U.S.-Australia FTA are precedent setting and beneficial to the intellectual property industries. Can you tell the committee what hurdles had to be overcome and what impact this Agreement will have on our copyright community?

*Answer.* The IPR chapter enhances protection across the range of IPR matters, including extension of the copyright term, a number of provisions to protect digital technologies, improved patent rights, and tough penalties for piracy.

With respect to copyrights, a challenge that we faced was that Australia was reluctant to amend legislation when their existing rules provided generally good protections for rightsholders. This included legislation that addressed, to some extent, the protections for digital works that are contained in the WIPO Internet treaties. However, implementation of the FTA will be of significant benefit to our copyright community by strengthening protection in several critical ways:

1. The FTA provides for clear protection for all "temporary" copies, which is crucial in the age of digital media and the Internet. While this will not require a change to Australian law, this is an important protection to codify in the FTA.
2. The term of protection for copyright works is extended to life of the author plus 70 years; the term of protection for works that are not measured by the life of a person, such as sound recordings, is also extended to 70 years.
3. There are stronger prohibitions against anti-circumvention of technological protection measures (TPMs) to protect copyrighted works.
4. The rules for Internet liability will encourage use of the Internet by creating a balance, similar to the Digital Millennium Copyright Act (DMCA), that will provide greater certainty to rightsholders and to Internet service providers.
5. Clear rules against retransmitting TV signals over the Internet.
6. Improvements in enforcement rules, including strong rules for seizure and destruction of infringing goods, elimination of unnecessary procedural burdens on rights holders, illegal use of software by companies ("end user piracy"), distribution of pirate works over the Internet, and satellite TV piracy will be subject to criminal penalties.

*Question 11.* What actions have you taken regarding China's newly proposed standard for encryption methodology in wireless local-area network products? It is my understanding this issue has been discussed at negotiations. What has been the Chinese response to our concerns? What are your plans in light of the impending June deadline?

*Answer.* At the Joint Commission on Commerce and Trade on April 21, 2004, Chinese Vice Premier Wu Yi committed to the United States that China would postpone implementation of that standard for an indefinite period of time. In early May, China implemented this commitment. We will continue to be vigilant against imposition of technical standards that disadvantage U.S. exports such as the wireless

encryption standard you note. However, we were pleased that our policy of leveraged engagement has led to this important result for American manufacturers and their workers.

*Question 12.* What is the administration doing to improve the quality of panelists selected from the United States, and are you taking all possible steps to ensure that the selection of a panel is fair and balanced?

Specifically, what are you doing to ensure that unbiased panelists are selected who understand and will follow U.S. trade laws?

*Answer.* In WTO disputes, the United States carefully considers the background and experience of each individual proposed to serve on dispute settlement panels, consulting broadly on each candidate's qualifications and suitability to serve. The United States also seeks to ensure that the proper mix of expertise and experience is reflected on each panel. In particular, when the dispute involves U.S. trade remedy laws, the United States seeks to include on panels individuals with experience as administrators of trade remedy laws in their own countries. We also seek individuals with legal experience that enables them to understand how U.S. trade remedy laws operate and the nature and limits of WTO obligations with respect to these laws.

With regard to U.S. panelists, because the United States is a party to a large number of disputes, the number of U.S. panelists is limited, as WTO rules generally bar nationals of the parties from serving as panelists. Nevertheless, some U.S. nationals have served with distinction on panels in recent years, including the recently appointed member of the WTO Appellate Body, Professor Merit Janow.

In NAFTA disputes, the United States regularly considers candidates to serve on various dispute settlement rosters from which panelists are selected. Applicants submit materials on their qualifications to USTR, which then consults with an interagency task force and Congressional staff before deciding which panelists are most qualified to serve. Depending on the roster, these candidates are then either added to the U.S. roster or proposed to Canada and Mexico as candidates for a jointly agreed roster. In the latter case, the three parties consider the qualifications of all proposed candidates before reaching agreement on which candidates should be added to the roster.

NAFTA disputes involving U.S., Mexican, or Canadian trade remedy laws (*i.e.*, antidumping and countervailing duty laws) are considered by five-member panels. Where U.S. laws are at issue, the United States proposes two panelists and the other involved NAFTA country proposes two panelists. The countries determine by lot which of them gets to propose the fifth panelist. Each country can exercise up to four peremptory challenges to panelists proposed by the other country. In proposing its panelists, USTR draws from a roster of approximately 70 highly qualified individuals. Many persons on the U.S. roster have experience working at the Department of Commerce or the International Trade Commission and have extensive expertise with respect to the substantive law and the appropriate standard of review.

*Question 13.* It seems that when the United States requests a NAFTA binational panel to review an antidumping or countervailing duty law imposed by Mexico or Canada, every request moves in slow motion. On the other hand, when those countries request panel reviews of duties imposed by the United States, the process shifts to fast forward. Are you disturbed by the disparate treatment for U.S. industries under NAFTA?

*Answer.* While panel formation has taken longer than anticipated in a few cases, overall the NAFTA Chapter 19 review process has worked well, with no evidence that cases are treated differently due to nationality.

According to the NAFTA Secretariat, 99 disputes have been brought under Chapter 19 provisions since this system began operating. A majority of these cases (61) have been brought against the United States. In recent years, the number of cases filed against the United States has increased, while the number of cases brought against Canada and Mexico has declined. As of June 30, 2004, the United States has 23 active cases against it, of which 11 have composed panels and 12 are awaiting panel composition. Canada currently has no cases against it, and Mexico has four, including three cases awaiting panel composition and one case with a composed panel.

*Question 14.* What is the Administration doing to persuade Canada to adopt fair trading policies in its exports of softwood lumber?

*Answer.* USTR and the Department of Commerce have been involved in ongoing negotiations and discussions with both the federal government of Canada and the provincial governments. We recently met with provincial officials from British Columbia and Ontario to discuss their ongoing forest management policy reforms. We are encouraged by those reforms and will continue to work with the provinces to

wards the goal of market-oriented, non-subsidized forest systems. Many producers, consumers, and policy makers on both sides of the border have concluded it would be in the interests of the United States and Canada to reach a permanent solution to their long-standing differences over softwood lumber. We remain committed to the pursuit of a durable solution. In the meantime, enforcement of U.S. trade laws and litigation will continue until a solution is reached.

*Question 14a.* Why have you not been able to reach a negotiated settlement of this problem with Canada?

*Answer.* As you are aware, there are many complex aspects of the dispute over softwood lumber. There are currently seven ongoing lumber cases in NAFTA and WTO dispute settlement. At the core of the problem is the need for Canadian forest reforms leading to a non-subsidized, market-based system. However, each province manages its system differently. We are involved in negotiations and discussions with the federal government of Canada and with individual provinces on how best to implement reforms. We are encouraged by reforms we have already seen and will continue to work with parties on both sides of the border to find a solution that is acceptable to all stakeholders. Until that time, enforcement of U.S. trade laws and litigation will continue.

*Question 14b.* If Canada is unwilling to settle the lumber dispute on fair terms, is the administration committed to enforcing a full offset of unfair Canadian trading policies?

*Answer.* This issue has been the subject of ongoing negotiations led by the Department of Commerce, with active USTR involvement. Negotiations to find a durable solution as an alternative to the cycle of trade cases and litigation have focused on two objectives:

- agreement on the market-oriented reforms to Canadian provincial forestry practices; and
- an interim measure to be imposed by Canada that would both stabilize the market pending the completion of reforms.

At the end of 2003, U.S. and Canadian negotiators agreed to present to their respective stakeholders a proposal for an interim measure. This proposal proved to be unacceptable to Canadian stakeholders.

While the administration remains committed to the pursuit of a durable solution, negotiations are a two-way street. We have informed Canada that litigation and enforcement of U.S. trade laws will continue until there is sufficient interest in returning to the negotiating table.

*Question 15.* Commerce is conducting a formal review of whether the countervailing duties paid by importers of Canadian lumber should be included as a cost of selling on the United States for the antidumping duty calculation. Apparently, 40 other countries use this methodology, which would increase the dumping offset substantially. Is USTR working with Commerce to ensure a full and fair review of this issue?

*Answer.* The Commerce Department has statutory responsibility for U.S. anti-dumping and countervailing duty law. It is reviewing the duty-as-a-cost issue in the context of a proposed change in Department policy. USTR is actively following this process.

#### RESPONSES TO QUESTIONS FROM SENATOR BAUCUS

*Question 1.* By my count, the United States is negotiating or about to negotiate free trade agreements with at least 18 developing countries. In the 2004 Trade Policy Agenda that you sent up last week, the Administration has made trade capacity building and technical assistance a centerpiece of its strategy for improving environmental and labor standards in these countries. I certainly support this principle. But frankly, talking about capacity building won't win broad support in Congress for these new agreements unless Congress has some assurance that labor and environmental conditions in FTA partner countries are really improving.

Is the Administration committed to creating and funding an institution to provide grant-based funding over the duration of the FTA transition periods and beyond?

Will the Administration commit to making monitoring by an objective, expert institution a requirement for all labor and environment capacity building projects?

*Answer.* The Administration is exploring a number of options for providing stable, long-term funding for the labor and environmental cooperation mechanisms in the FTAs with developing countries. In fact, James Connaughton, the Chairman of the Council for Environmental Quality, and I have contacted the Cabinet officers of key agencies to communicate the importance of the environmental cooperation mechanisms and our desire to develop an Administration-wide strategy to ensure their effective implementation and funding. We also hope to work closely with you on the



funding issues as part of the FTA implementation packages. Congress has the power of appropriations, and we are willing to discuss with the appropriate Committees how best to provide the funds needed in future fiscal years.

The Environmental Cooperation Agreement with Central America, concluded at the same time as the CAFTA, commits the Parties to establish benchmarks for measuring progress towards improving environmental standards and seeking input from relevant outside organizations to assist us in monitoring progress toward reaching the goals of the agreement. The State Department is now developing the CAFTA environmental cooperation work plan, which will provide more details on monitoring. We have already discussed this with your staff and plan to share it with our official advisors on the Trade and Environment Policy Advisory Committee prior to tabling it with our Central American partners.

The grant solicitation and award process of the U.S. Department of Labor's Bureau of International Labor Affairs (ILAB) assures that there are measurable milestones not only for each grantee (*i.e.*, FUNPADEM for CAFTA, the ILO for Morocco and SACU) but also for each of our negotiating partners in the FTAs.

*Question 2.* For many years the nitrogen fertilizer companies throughout the country have suffered losses due to market conditions caused by surges of low-priced Russian fertilizers. Russia's gas prices are the cause of distortion in the U.S. and other markets worldwide.

In light of overwhelming evidence drawing a direct link between trade distortions and Russia's policies, do you agree that Russia has the responsibility to reform its gas price policies to eliminate trade distortions when it joins the WTO?

*Question 3.* In the Commerce Department's recent report on manufacturing in America, Secretary Evans established as a priority the use of trade agreements to eliminate foreign countries' policies and practices that distort international trade.

Do you agree that, consistent with this goal, the United States must seek to ensure that Russia eliminate its distortive domestic natural gas price policies as it seeks to join the WTO?

*Answers 2&3.* We are keenly aware of the problems that Russian fertilizer exports have caused in the United States. Although some of these problems have been addressed through the application of antidumping duties, we recognize that other products remain problematic and that longer-term issues must be addressed as well. The transition from a non-market to a market economy is inevitably a difficult one. While Russia has made remarkable strides, some areas of the economy remain in need of reform.

The issue of Russian domestic natural gas pricing has been the focus of extensive discussions in the Russian WTO accession negotiations for the U.S., EU, and others (Australia, Norway and Canada). USTR and Commerce have been consulting and working very closely with the U.S. fertilizer industry throughout the accession process and will continue to do so. In May, the EU and Russia reached a bilateral agreement relating to a number of WTO accession issues. We understand that Russia is ready to commit in the WTO to the principle that domestic gas prices must cover the full cost of production, including a profit, and has also specifically agreed to a schedule of price increases.

The U.S. fertilizer industry characterized the EU agreement as a "significant breakthrough." We view the agreement with the EU as a good first step and intend to build upon it in the course of completing Russia's accession negotiations.

#### RESPONSES TO QUESTIONS FROM SENATOR ROCKEFELLER

*Question 1.* Congress directed the Administration to negotiate a solution to the World Trade Organization's (WTO) ruling against the Continued Dumping and Subsidy Offset Act through a provision in the FY04 Omnibus Appropriation bill. When will the United States present its negotiating position on this matter to the WTO? And, when will you share your strategy with Congress?

*Answer.* In accordance with the Appropriations bill language, the United States filed and presented a formal paper in the World Trade Organization (WTO) Negotiating Group on Rules for its meeting the week of April 26, 2004, raising the issue of the right of WTO Members to distribute monies collected from antidumping and countervailing duties. That paper is publicly available on the WTO website ([www.wto.org](http://www.wto.org)), under the document designation TN/RL/W/153 (April 26, 2004).

It should be noted that the November 2001 Doha Ministerial Declaration mandate for the WTO Rules Group calls for an initial phase of issue identification before any negotiations over specific changes. Given this Doha mandate, it has been U.S. practice for all issues we have raised thus far in the Rules negotiations to begin with a submission identifying the issue generally. We followed this practice in our paper with respect to this issue as well.

USTR staff discussed this issue in conference calls with the staffs of the Senate Committee on Finance and the House Committee on Ways and Means during the week of March 22, 2004, before submission of the paper, and then again during the week of May 17, 2004, after submission of the paper. During these calls, we discussed our ideas with respect to how best to present this matter to the WTO, and sought guidance from Congressional staff.

*Question 2.* Congress directed the Administration to report to the Congress every 60 days on the progress of the negotiations, again in the FY04 Omnibus bill. Given the Congressional directive to negotiate a solution to this matter, what is the Administration doing to initiate these negotiations?

*Answer.* As discussed in the answer to question 1 above, the United States filed and presented a formal paper in the WTO Negotiating Group on Rules for its meeting the week of April 26, 2004. The paper raised the issue of the right of WTO Members to distribute monies collected from antidumping and countervailing duties.

*Question 3.* Will the first update be provided consistent with the statutory direction 60 days from enactment of the omnibus appropriations bill, which would be on or about March 23, 2004?

*Answer.* USTR and the Department of Commerce provided the first update during the week of March 22, 2004, in conference calls with staff members (both majority and minority) of the Senate Finance Committee and the House Ways and Means Committee, and then a further update in conference calls with staff members (both majority and minority) of the same committees during the week of May 17, 2004.

*Question 4.* When the President decided to prematurely end the Section 201 tariffs on steel, his statement said that he "is committed to America's steel workers and to the health of our steel industry." It also stated that, "steel import licensing, established when the safeguard measures were imposed, will continue to provide WTO-consistent data collection and monitoring of steel imports. This will enable the Administration to quickly respond to future import surges that could unfairly damage the industry."

The President's Proclamation of the same date similarly stated that "the licensing and monitoring of imports of certain steel products remains in effect and shall not terminate until the earlier of March 21, 2005, or such time as the Secretary of Commerce establishes a replacement program."

Does the Administration have a plan to expedite the adoption of those expanded regulations? When does the Administration intend to request public comment with respect to its new import monitoring and licensing system and when will this program be up and running?

*Answer.* As you know, on December 4, 2003, the President determined that the steel safeguard measures had achieved their purpose and it was time to lift them. The U.S. steel industry's performance subsequent to the removal of safeguard tariffs supports the President's decision. Increased demand for steel worldwide, led by China, is improving the financial position of American steelmaking companies and their competitors. The top three steel producers, U.S. Steel, International Steel Group, and Nucor all reported first quarter profits. At an industry conference June 22 in Beijing, industry analysts from World Steel Dynamics predicted that this trend will continue. They also foresee that 2004 will be a banner year for steelmakers, with profits rising exponentially. Further, the domestic steel industry continues to consolidate, creating improved economies of scale and more viable steel companies.

The President's decision terminating the safeguards also continued the current system of licensing and monitoring of steel imports. It will remain in place until March 2005 or until such time that a replacement program is established by the Department of Commerce. We understand the steel industry's concern that the current system may need to be enhanced, particularly along certain product lines. Even though today's market is strong, we are certainly aware that conditions in the steel market can change rapidly. Commerce is currently considering possible changes to the program and is conferring with U.S. producers, consumers and exporters.

*Question 5.* As you know, the United States is currently facing WTO-approved sanctions from the EU as a result of our alleged failure to comply with the WTO's decision on the U.S. FSC/ETI law. If you step back, however, the only reason this law was even an issue was because of the oddity in WTO rules that treat VAT and other consumption taxes (which are chiefly used by our trading partners) differently than the type of corporate income taxes relied upon in the United States. Basically, foreign countries can rebate VAT-type taxes on exports (and impose them on imports), while the United States cannot rebate its income taxes on export or impose them on imports. The effect is to "double tax" U.S. businesses and to give an enormous (some have estimated as much as 15-20 percent) advantage to foreign producers. There is no economic basis that I know of for this disparity in WTO rules,

and yet U.S. workers and businesses continue to operate under a double standard that does them great harm.

Every fast track bill has made elimination of this disparity in WTO rules a top priority, and yet nothing ever seems to get done about it. It seems ludicrous that a country with a \$500 billion trade deficit—including a deficit of close to \$100 billion with the EU alone—does not have more leverage on our trading partners on this point? Haven't U.S. manufacturers waited long enough for relief? Why shouldn't we tell the rest of the world that we simply will not sign any further trade agreements until this problem is resolved to our satisfaction?

*Answer.* Consistent with the negotiating objectives set by Congress in the Trade Act of 2002, in the Doha Round we have identified that an essential part of the work of the WTO Negotiating Group on Rules is the question of the different disciplines currently applicable to direct and indirect tax regimes. Specifically, we informed the Group that it should "work toward greater equalization in the treatment of various tax systems that, at least with regard to their subsidy-like effects, have only superficial differences." (TN/RL/W/78). We are continuing to pursue this issue as we move forward in the negotiations.

#### RESPONSES TO QUESTIONS FROM SENATOR CONRAD

*Question 1.* Agriculture and the WTO. Mr. Ambassador, as you well know, current WTO rules lock in place an advantage for the European Union when it comes to farm subsidies. On domestic support per acre, the EU outspends us by \$277/acre to \$48/acre, a ratio of more than 5:1; on export subsidies, the inequity is an even more glaring 87:1. In addition, U.S. farmers face increased competition from major agricultural exporting nations, such as Brazil, that self-define themselves as developing countries to gain advantages in the competition for global markets. American farmers can compete with farmers anywhere in the world on a level playing field, but they cannot succeed indefinitely if the rules of world trade continue to discriminate against American agriculture. For these reasons, I have long argued that the U.S. needs an aggressive, politically savvy approach to the current round of WTO negotiations on agriculture.

Unfortunately, in my view, the U.S. effort suffered a significant setback at Cancun. I believe U.S. negotiators made several tactical errors that contributed to the failure to reach an agreement that would provide significant benefits to American farmers. First on export subsidies, the U.S. agreed with the EU not to push for modalities that would call for the elimination of agricultural export subsidies. As a result, U.S. negotiators in Cancun spent time and negotiating capital defending an EU priority that is contrary to the interests of American farmers and helped fuel the rise of the so-called G-21.

Second, on domestic support, the U.S. dropped its previous position that the ceilings should bring EU spending to rough parity with U.S. spending. Although no numbers were formally proposed, informal discussions made it clear that the proposal contemplated EU reductions of 60% and significant reductions (in the neighborhood of 50%) in the U.S. amber box ceiling. This new USTR position would have left the EU with an advantage of more than 2.5:1 on domestic support—far short of the level playing that is ostensibly USTR's goal in this area. Again, the U.S. found itself in the position of defending much higher EU subsidies, rather than being able to focus on the gains in developing countries and the Cairns Group nations of far deeper reductions in EU domestic supports.

Third, on market access, developing country markets hold the greatest potential for U.S. export gains because they have both high barriers and rapidly growing demand. Yet in this key area, the U.S. found itself on the defensive in large part because of USTR's failed tactics on domestic support and export subsidies. As a result, our negotiators in Cancun were prepared to agree to proposals that would create significant exceptions to the market access obligations of developing countries, leaving little benefit to U.S. exports from the agreement.

To put it bluntly, I am glad the Cancun talks fell apart before the U.S. signed onto this failed set of proposals. In my view, the goal of these negotiations is to raise U.S. farm income. But cutting U.S. domestic support in half without any guarantee of significant new market access opportunities cannot possibly achieve this goal—particularly if, at the same time, the EU is allowed to maintain its massive advantages on trade distorting support programs. Such a deal will clearly not be in the interest of the farmers I represent.

So my question to you is this: What are you doing to reverse the mistakes U.S. negotiators made at Cancun? And what are you doing to produce a result that will eliminate the current inequities in agricultural trade rules, level the playing field for U.S. farmers, and boost farm income in this country?

*Answer.* Export subsidy elimination has long been a U.S. negotiating objective in the WTO. This did not change with the framework proposal developed with the EU. Export subsidy elimination remains a core objective of the negotiations and our work over the past two years has brought us much closer to that point, as the EU is now prepared to negotiate terms for export subsidy elimination in the WTO. Substantial reductions in trade-distorting domestic support, including greater harmonization in support levels allowed for the United States and the EU, remains a U.S. negotiating objective. This did not change in the framework proposal developed with the European Union. Our work over the past two years has brought us much closer to substantial cuts and greater harmonization in trade-distorting domestic support, as the EU is now prepared to accept a larger cut in the Aggregate Measurement of Support than the United States and is prepared to cap the level of support under the "Blue Box". Substantial improvement of market access, for developed and developing countries alike, remains a U.S. negotiating priority. Our work over the past two years has brought us much closer to achieving this objective, as many WTO members are now prepared to engage in tariff negotiations under the guiding principle that higher tariffs be subject to greater cuts.

A successful WTO negotiation will result in a more market-oriented global agricultural trade system. This system will benefit the United States as a whole, and U.S. agriculture in particular, by harvesting the benefits of greater trade and openness. We will continue to press for agreement based on core U.S. objectives in the three pillars of market access, export competition, and domestic support because these objectives embody the principles that will expand economic growth and opportunity.

*Question 2. Sugar.* Last week I sent you a letter urging that sugar be excluded from the Free Trade Agreement negotiations with the Dominican Republic. In my view, sugar should be off the table in bilateral FTA talks. Because the global sugar market is badly distorted, sugar trade talks can only be successful if they are done comprehensively and multi-laterally in the WTO. Bilateral talks with major sugar producing countries that result in increased access to the U.S. market can only serve to destroy the U.S. domestic sugar program and industry because they do not address the many worldwide distortions that lead to sugar being sold in a "dump market" at far below the world cost of production.

The conclusion of the Australian FTA demonstrates that leaving sugar off the table need not jeopardize our agricultural market access goals. As your own materials on the Australian agreement note, U.S. agriculture will get immediate duty-free access to the Australian market, even though sugar was not included in the FTA.

It is my understanding that the Dominican Republic is not able to fill its current U.S. sugar quota and meet domestic consumption demands without importing sugar. To me, it makes no sense under these circumstances to give the Dominican Republic increased access to our sugar market, particularly when you have just demonstrated in the Australia agreement that tough negotiating can result in the complete removal of tariff barriers to U.S. agricultural exports without providing increased access to the U.S. sugar market. Consequently, I urge you to be just as tough in negotiations with the Dominican Republic and achieve full access to the Dominican market for U.S. agricultural exports without giving up any additional access to our sugar market.

Will you take sugar off the table in the Dominican Republic FTA negotiations as you did in the Australia FTA talks? Will you take sugar off the table in other FTAs you are negotiating?

*Answer.* Sugar was included in the Dominican Republic FTA negotiations. U.S. commitments (a 10,000 mt TRQ increase with 2% annual growth) are well within the parameters of U.S. farm legislation. The agreement does not result in any change in the U.S. out-of-quota duty, requires the Dominican Republic to be a net sugar exporter on the world market before gaining access to the U.S. market, and includes a provision allowing for alternative compensation to Dominican Republic sugar exporters in the event the U.S. sugar program is threatened by imports of Dominican Republic sugar.

Every negotiation has its own dynamic. The specifics of what is needed to put together a package that works for both sides are different for different countries. Consequently, we are looking at each of the FTAs on a case-by-case basis to determine what best meets our needs. In some cases it will make sense for sugar to be included, in some cases it will not. For CAFTA, sugar had to be part of the deal. Sugar is a very large part of the economy in that region, and access to the U.S. market was critical for the Dominican Republic and the Central American countries. Without sugar, there would not have been an agreement. In contrast, Australia has a much more diversified agricultural economy, and economy overall. Sugar was not

a critical element for that deal, and the overall balance did not require it be included.

*Question 3. Wheat.* The U.S. wheat industry continues to suffer unfair competition from export state trading monopolies like the Canadian Wheat Board. The positive Section 301 ruling you issued in 2002 requires USTR to take actions that will reverse Canada's unfair practices.

In light of the most recent WTO ruling on the Canadian Wheat Board, what actions are you taking to provide relief to American wheat growers?

*Answer.* In response to a section 301 petition filed by the North Dakota Wheat Commission, on February 15, 2002, USTR announced a four prong approach to fight for a level playing field for American wheat farmers.

First, the Administration committed to work with the North Dakota Wheat Commission and the U.S. wheat industry to examine the possibilities of filing U.S. countervailing duty and antidumping petitions. In October 2003, the U.S. Department of Commerce and U.S. International Trade Commission concluded that Canadian wheat was being unfairly subsidized and dumped into the U.S. market, injuring U.S. wheat farmers. The USG applies an 8.87% dumping duty and 5.29% countervailing duty on Canadian hard red spring wheat.

Second, USTR agreed to identify specific impediments to U.S. wheat entering Canada. The part of the WTO dispute regarding Canada's grain handling and rail transportation systems is a direct result of that investigation.

Third, USTR committed to examine initiating a WTO dispute settlement case against the Canadian Wheat Board. USTR initiated WTO proceedings in March 2003 to examine: (1) the wheat trading practices of the Government of Canada and the Canadian Wheat Board (CWB); (2) Canada's requirements to segregate imported wheat in the Canadian grain handling system; and (3) Canada's discriminatory policy that affects access of U.S. grain to Canada's rail transportation system.

In early April, the WTO panel published its decision. The panel accepted the U.S. claim that Canada has acted inconsistently with its WTO obligations by treating Canadian grain more favorably than imported U.S. grain. The panel also accepted the U.S. claim that Canada's rail transportation measure known as the "rail revenue cap" discriminates against imported grain. These results are consistent with a long history of WTO rulings that additional regulatory hurdles cannot be placed only on foreign products and that a country may not give special treatment to its own products without extending that special treatment to imported goods.

While the panel found for the United States with respect to our claims that Canada's grain handling system and rail revenue cap discriminate against imported grain, it found against the United States with respect to the unfair practices of the Canadian Wheat Board. This issue is now on appeal.

Finally, through the WTO negotiations, the United States has aggressively pursued permanent reform of monopolistic export state trading enterprises such as the Canadian Wheat Board. We have made solid progress in achieving the U.S. objectives on state trading enterprises, developing an international coalition supporting our position.

*Question 4. Trade Deficit.* In just four years, the annual U.S. trade deficit has nearly doubled from \$260 billion in 1999 to a record \$489 billion last year. On goods alone, the deficit hit a record \$550 billion. In my view, trade deficits of this magnitude are simply unsustainable. Clearly something is dramatically wrong with the trade policies we have been pursuing if they result in a doubling of the trade deficit in just a few years.

What changes in trade policy are you contemplating that might reverse this trend and get our trade deficits under control?

*Answer.* The aggregate U.S. trade deficit reflects macroeconomic factors such as differences in rates of economic growth among countries, levels of domestic saving and investment, and international capital flows. While a market-opening trade policy brings many economic benefits, it has little direct impact on such macroeconomic conditions and related aggregate trade imbalances.

In the second half of the 1990s, the United States experienced a quickening of economic growth relative to many of our trade partners. This relatively strong performance of the U.S. economy has been sustained over the last three years, despite the recession at the beginning of decade and the initial modest rate of recovery. Weaker economic growth abroad has contributed to a stalling of U.S. exports, even as U.S. imports experienced a modest expansion.

Consider the period since the last recession: 2000 to 2003. Over this period the U.S. goods trade deficit increased by roughly \$100 million, from \$436 million to \$536 million (Census basis). Nearly 60 percent of this increase resulted to a reduction in U.S. exports. In fact, in the last three years U.S. goods exports declined by 7.4 percent, compared to a modest three-year increase of 3.4 percent in U.S. im-

ports. This divergent performance in U.S. exports and imports reflected, in part, substantial differences in rates of economic growth between the United States and major trade partners. For example, while the U.S. economy managed to expand by 5.6 percent between 2000 and 2003, that of the EU grew only 3.6 percent, Japan, 2.7 percent, Mexico 1.9 percent and the rest of Latin America by just 0.2 percent.

Strong growth is a benefit to the United States. The nearly 6 percent annualized growth rate in last year's second half is heartening. We also benefit, however, when the economies of our trade partners improve as well. Stronger growth abroad is vital to U.S. exports which began to show unmistakable signs of revival during the course of last year. As the macroeconomic conditions underlying current global trade imbalances begin to adjust, the U.S. trade policy so clearly focused on opening foreign markets and expanding trade should help ease the effects of adjustment and facilitate economic growth.

*Question 5. Currency Value.* I have long argued that we must pay more attention to currency values as part of trade policy. The simple reality we face is that currency movements can swamp gains we might otherwise expect to achieve from reducing tariffs on U.S. exports. For example, in the NAFTA we expected U.S. goods to become more competitive because Mexico's tariffs, which averaged 10% were being eliminated. But shortly after NAFTA took effect, Mexico devalued its currency by 50%—meaning that U.S. goods were on net, 40% more expensive in Mexico than before NAFTA. As a result, it is not surprising that our trade balance with Mexico has gone from a small surplus before NAFTA to a deficit of \$40 billion last year.

More recently, China's manipulation of its currency has been in the news a great deal. Again, we hoped that a reduction in China's tariffs would help open that market to U.S. exports, but the reality is that China devalues its currency by as much as 40%, making it virtually impossible for U.S. exports to compete with products made in China. And again, not surprisingly, we find that our trade deficit with China continued to explode, reaching \$124 billion last year.

My question is this: What are you doing to incorporate currency issues into U.S. trade policy?

*Answer.* I will leave discussion of exchange rates to my colleague, the Secretary of the Treasury, who is the Administration spokesperson on these issues. However, I do want to commend Secretary Snow and his team for the depth and breadth of their discussions with the Chinese to help move China forward toward its stated goal of a more market-oriented currency. The strong sense of the Administration is that we are achieving real results through our policy of leveraged engagement with China, and that a more litigious approach would not deliver the results in China's currency and other economic policies that all of us seek.

We have seen that the reduction of Chinese tariffs and other trade liberalizing actions that accompanied China's WTO accession have had a significantly positive impact on U.S. exports to China. Indeed, since China joined the WTO, China has become our 6th largest export market. We sold nearly \$30 billion of U.S. manufactured goods, agricultural commodities, services and high-tech products to China last year. Trade this year is up 40% over the same period in 2003. Imports from China are still increasing some 25% per year, but exports are increasing at a rate faster than Chinese imports. We have no doubt that our exports can be and are competitive in China.

The benefits of trade liberalization are concrete and real, irrespective of exchange rate movements. The elimination of a 10% tariff will lower the selling price of U.S. products to foreign purchasers from what the price would otherwise have been. Also the removal of all tariffs eliminates a source of potential national resource misallocation arising from divergent tariff treatment among products. Finally, bound tariff reductions and eliminations are, by their nature, permanent, bringing permanent benefit. In the case of the Mexican financial crisis of 1995, it is important to remember that, with NAFTA in place, Mexico continued to lower its tariffs vis-a-vis the United States, instead of raising them as it had done during the financial crisis of the early 1980s. The value of U.S. exports to Mexico has risen by 134% since NAFTA. The United States continues to enjoy a 62 percent share of Mexican goods imports from the world.

*Question 6. Offshoring.* The President's chief economist, Gregory Mankiw, has said that it is a good thing that high-paying service jobs are moving offshore. To me, that statement is totally out of touch with the reality that American workers and communities face. We cannot stay strong economically or militarily if we totally lose the capacity to produce in this country.

So, I ask you, do you agree with Dr. Mankiw? If not, what changes are you going to make in U.S. trade policy to reverse the trend that sees millions of ranks of the unemployed, underemployed, and discouraged workers who have dropped out of the labor market?

*Answer.* New competition in the services sector from foreign providers of services is a serious concern, and deserves serious discussion. Much of the new competition in services is driven by technology and the fact that English has become the world's second language. But it is important to remember that the United States provides far more services to the rest of the world than foreign countries provide to us. In fact, we have a \$51 billion trade surplus in services.

But any time an American loses a job, we need to understand that it is a difficult and painful experience, and we need to help those who are affected. We must provide that help in ways that do not destroy other jobs. Only 5% of the world's consumers live in the United States, and we rely on exports and open markets to sell to the other 95% of the world's customers who live beyond our borders. And our economy is interconnected with the world: twelve million Americans have jobs that depend on exports, and 6.4 million Americans have "insourced" jobs working for U.S. affiliates of foreign companies. So we must take care that our policy response does not endanger these jobs by erecting walls and barriers around America.

Economic isolationism is not the answer, nor do we need more bureaucratic regulations that will increase prices for consumers and won't work. Rather, the correct response is to open new markets for the best products and services in the world: American ones. Our policy is to open new markets so that entrepreneurs can create jobs and economic growth here at home. We also need to enforce our trade agreements to make sure that Americans have a level playing field to compete in world markets. And we need to continue cutting hidden import taxes that hurt working families the most.

We also need to continue providing help for those who have lost a job to get back on their feet. The President signed the Trade Act of 2002, which tripled the level of Trade Adjustment Assistance (TAA) for workers who lose their jobs because of foreign competition; that Act also provided health care benefits and an alternative TAA program for older workers. In addition, the President's Jobs for the 21st Century Initiative envisions \$500 million in new funds for job training and worker education initiatives.

These are important initiatives, and we will not rest until every American who wants a job has one. To create those jobs, we will pursue a policy of opening markets, reducing trade barriers, providing a level playing field, cutting hidden import taxes, and helping workers get trained for the new jobs of the 21st Century. We will avoid economic isolationism.

#### RESPONSES TO QUESTIONS FROM SENATOR GRAHAM

*Question 1.* I understand that you have included in various trade agreements, such as CAFTA, data exclusivity provisions during which a signatory's marketing authority may not approve a generic version of a drug. The length of these data exclusivity periods exceed those provided under U.S. law. What is the justification for seeking data exclusivity periods in treaties that exceed those provided under U.S. law? Can you assure the Committee that this Administration will not support extension of data exclusivity periods under U.S. law based on these treaty agreements?

*Answer.* In fact, the data exclusivity periods in the proposals that we have tabled in our various trade agreements are for the same lengths as those under existing U.S. law. As under U.S. law, our FTAs require a five-year period of protection for confidential information submitted to obtain marketing approval for pharmaceutical products and a ten-year period of protection for confidential information submitted to obtain marketing approval for agrochemical products.

I can reassure you that this Administration will not seek to extend data exclusivity periods under U.S. law based on our trade agreements.

*Question 2.* In November 2001, the United States committed itself to the Doha Declaration on access to medicines. Our country's commitment to the Declaration was given the force of law in the Trade Promotion Act (TPA) of 2002, which requires the Declaration to be treated as a principal negotiating objective in all U.S. trade agreements. Do you believe that the data exclusivity provisions included in CAFTA and bilateral treaties with Singapore and Chile are consistent with this commitment? How does the inclusion of these provisions fulfill the statutory requirement that adherence to the Doha Declaration be a principal negotiating objective of the United States?

*Answer.* TPA recognizes the complementary nature of high standards IPR protection and the objectives of the Doha Declaration. Thus, at the same time that TPA states that IPR rules should respect the Doha Declaration, it also states that "the provisions of any multilateral or bilateral trade agreement governing intellectual property rights that is entered into by the United States [should] reflect a standard of protection similar to that found in United States law." The IPR rules in our FTAs

meet both these objectives. The data exclusivity provisions of our trade agreements, which reflect U.S. standards, are fully consistent with the Doha Declaration. The United States certainly would not interpret or apply the data exclusivity provisions in a manner that prevented a developing country from utilizing the flexibility recognized in the Doha Declaration.

We support the Doha Declaration and are committed to ensuring that trade rules, including TRIPS and our FTAs, and preserve flexibility to take measures necessary to protect public health. For example, we have included in two of our most recently signed agreements, CAFTA and Morocco, a side letter building on the Doha Declaration and memorializing an understanding with our FTA partners that the IPR obligations do not affect a Party's ability to take necessary measures to protect public health by promoting access to medicines for all, nor prevent the effective utilization of the TRIPS/health solution.

#### RESPONSE TO A QUESTION FROM SENATOR JEFFORDS

*Question 1.* I'd like to ask you a question about the Central American Free Trade Agreement. I know that you have made an effort to strengthen the labor rights and environmental provisions of CAFTA. I am still concerned, however, that the agreement does not go far enough in this regard. There are such disparities between our country and the countries of Central America in these areas. Central America still has a long way to go on respect for labor rights and enforcement of strict environmental standards. I believe CAFTA must move them forward in these areas, both for their sakes and for ours. I'd like to hear you comment in greater detail on this concern.

*Answer.* I share your view that the U.S.-Central American Free Trade Agreement (CAFTA) should promote strong labor rights and environmental protection in the countries of Central America and the Dominican Republic. But history shows that we can do more to improve labor and environmental conditions by promoting trade and economic growth than by isolating poor countries from the global economy. By dismantling the trade and investment barriers that impede farmers, businesses, and workers in Central America and the United States from taking full advantage of their skills, productivity, and creative abilities, the CAFTA should spur economic growth, promote development, and raise living standards in both the United States and its trading partners.

Vibrant, growing economies in the region will, in turn, increase public support in Central America for strong worker protections and help generate revenues that governments need to enforce their labor laws. Moreover, by increasing opportunity, prosperity and hope, the CAFTA will also help foster stable and resilient democracies in Central America, a vital step in ensuring that Central American governments are committed to—and enforce—high labor and environmental standards.

We also are breaking new ground in the CAFTA, which includes labor and environmental provisions that far surpass anything in trade agreements by other nations. With the bipartisan guidance received from Congress in the Trade Act of 2002, the United States has a three-part cooperative strategy that is producing real, measurable improvements in labor rights and environmental protection.

First, the CAFTA countries must effectively enforce their own labor and environmental laws. This provision is backed up by monetary fines that are channeled back into fixing labor or environmental problems. The United States is the only nation that insists on including this kind of enforceable provision in the core text of its trade agreements. Also in the CAFTA, in response to our NGOs, we have established an independent review mechanism where citizens can raise concerns about environmental issues.

Second, we are working with the CAFTA countries to upgrade labor and environmental laws and practices. We encouraged the CAFTA governments to work with the International Labor Organization (ILO) to identify areas for improvement in their labor laws and enforcement. The ILO study found that while the labor laws on the book do give effect to the core rights and principles identified in the ILO Declaration on Fundamental Principles and Rights at Work, there were some gaps that needed to be addressed and enforcement needs to be improved. The CAFTA countries are fully engaged, even before the Agreement goes into effect. In Guatemala, fines on employers have greatly increased, exemplifying effective implementation of its 2001 labor law reforms. Strong government support also encouraged the first-ever collective bargaining agreements with Export Processing Zone (EPZ) unions. In other examples, Costa Rica has cut its labor court backlog in half, while El Salvador increased the number of labor inspectors by 50 percent.

Finally, labor and environment cooperation agreements will help ensure that these efforts continue after the agreement has entered into effect, and will help pro-



vide resources to assist them in carrying out their work plans. As part of this, ILAB awarded a \$6.75 million grant to The Foundation for Peace and Democracy, an NGO based in Costa Rica, to educate Central American workers about their legal rights and to promote non-violent ways to resolve labor disputes. U.S. and other donors have funded \$25 million in projects to combat exploitative child labor. Our trade capacity building efforts have teamed up with business to improve monitoring of labor standards in garment factories. Working with Senator Baucus, we are also exploring establishing specific benchmarks for measuring environmental progress and for monitoring success in meeting those benchmarks. Taken together, our three-part cooperative strategy provides confidence that the CAFTA's greater economic opportunities will be accompanied by improving labor and environmental conditions, an objective we both share.

CAFTA also brought about new partnerships to address important environmental and conservation concerns through our trade capacity building program. These partnerships include innovative efforts to promote higher environmental standards and conservation with a focus on economic development. An important concern for Central America is preserving and protecting endangered sea turtles through education, conservation measures and sustainable economic activities. To that end, U.S. NGOs are working with the Central American governments to promote marine turtle conservation by developing turtle stations on the Caribbean and Pacific coasts—habitat for critically endangered species. For example, in Tortuguero, Costa Rica, on the Caribbean coast, approximately 100,000 tourists visit the turtle station annually to observe the nesting and hatching of endangered turtle species. The economic opportunities brought about by this turtle station provide an important incentive to protect these magnificent but endangered animals.

I would like to commend you, Senator, on your efforts to promote Turtle Conservation through the Marine Turtle Conservation Act. By combining conservation efforts with opportunities for economic development we can set the stage for long-term success that benefits Central Americans, endangered species, and habitat. This is one example of how CAFTA promotes economic development and integration as well as conservation and higher environmental standards.

#### RESPONSE TO A QUESTION FROM SENATOR BINGAMAN

*Question 1.* New Mexico has attracted advanced semiconductor manufacturing facilities. I am concerned that China's discriminatory value-added tax rebate is distorting trade and investment patterns in this sector by disadvantaging imports and creating an incentive to invest in China for market access purposes. The VAT rebate is not consistent with China's WTO obligations.

Has there been any indication of movement from the Chinese Government on this issue? Is USTR prepared to move forward with WTO dispute settlement on the VAT if necessary?

*Answer.* USTR fully shares your concerns regarding China's VAT rebate for integrated circuits manufactured or designed in China. Despite numerous bilateral discussions on this issue beginning over a year ago, China's Government has refused to alter this policy. On March 18, we filed a request for consultations under the World Trade Organization's dispute settlement mechanism, with the aim of achieving a solution to this problem as soon as possible. We believe we have an excellent case. All indications from China are that they will seek to resolve it before the WTO decides against them on the matter. Settlement negotiations on the issue are ongoing. If these are not resolved to our satisfaction, we intend to move forward.



## COMMUNICATIONS

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### STATEMENT OF THE ADVANCED MEDICAL TECHNOLOGY ASSOCIATION (ADVAMED)

AdvaMed represents over 1100 of the world's leading medical technology innovators and manufacturers of medical devices, diagnostic products and medical information systems. Our members are devoted to the development of new technologies that allow patients to lead longer, healthier, and more productive lives. Together, our members manufacture nearly 90 percent of the \$75 billion in lifeenhancing health care technology products purchased annually in the United States, and nearly 50 percent of the \$175 billion in medical technology products purchased globally. Exports in medical devices and diagnostics totaled \$22.4 billion in 2003, but imports have increased to \$22 billion indicating a new trend towards a negative trade balance for the first time in over 15 years.

The medical technology industry is fueled by intensive competition and the innovative energy of small companies—firms that drive very rapid innovation cycles among products, in many cases leading new product iterations every 18 months. Accordingly, our U.S. industry succeeds most in fair, transparent global markets where products can be adopted on their merits.

#### *Global Challenges*

Innovative medical technologies offer an important solution for industrialized nations, including Japan and European Union members that face serious health care budget constraints and the demands of aging populations. Advanced medical technology can not only save and improve patients' lives, but also lower health care costs, improve the efficiency of the health care delivery system, and improve productivity by allowing people to return to work sooner.

To deliver this value to patients, our industry invests heavily in research and development (R&D), and U.S. industry is a global leader in medical technology R&D. The level of R&D spending in the medical device and diagnostics industry, as a percentage of its sales, more than doubled during the 1990s, increasing from 5.4% in 1990, to 8.4% in 1995, to 12.9% in 1998. In absolute terms, R&D spending has increased 20% on a cumulative annual basis since 1990. This level of spending is on par with spending by the pharmaceutical industry and more than three times the overall U.S. average.

However, patients benefit little from this R&D investment when regulatory policies and payment systems for medical technology are complex, non-transparent, or overly burdensome, causing significantly delays in patient access. They can also serve as non-tariff barriers, preventing U.S. products from reaching patients in need of innovative health care treatments.

AdvaMed applauds continued progress on international trade initiatives, including bilateral, regional and global trade negotiations, such as the Free Trade Area of the Americas (FTAA) and the Doha Development Agenda in the World Trade Organization (WTO). We support new efforts like the Central American Free Trade Agreement (CAFTA), under which the Central American partners to the agreement will grant U.S. exports of medical devices duty-free treatment. We are hopeful that future bilateral agreements can also include directives to knock down tariff and non-tariff barriers for medical technologies. In addition, the President and U.S. Trade Representative (USTR) should continue to pursue trade liberalization in the medical technology sector with our major trading partners.

AdvaMed believes the USTR, Department of Commerce (DOC) and Congress should monitor regulatory, technology assessment and reimbursement policies in foreign health care systems and push for the creation or maintenance of transparent assessment processes and the opportunity for industry participation in decision making. We look to the Administration and Congress to actively oppose excessive

regulation, government price controls and arbitrary, across-the-board reimbursement cuts imposed on foreign medical devices and diagnostics.

*Continued U.S. Leadership Needed to Fight Trade Barriers in Japan*

For the medical technology industry, the Bush Administration's efforts with Japan under the U.S.-Japan Partnership for Economic Growth are critical for maintaining access to the Japanese health care market.

After the U.S., Japan is the largest global market for medical technologies at \$25 billion. U.S. manufacturers annually export over \$2.5 billion to Japan. These statistics are good indicators of our industry's global competitiveness in the field of medical technology and it strongly underscores the importance of critical ongoing efforts with the U.S. government to open the Japanese market further to cost-saving and life-enhancing medical technologies.

In 1986, U.S. Government leadership began to help open Japan's marketplace for medical devices under the Market Oriented Sector Specific (MOSS) trade agreements. These efforts have helped to grow and sustain a favorable U.S. trade balance for medical devices in the range of \$1.1 billion in recent years.

In late 2001, however, the Japanese Ministry of Health, Labor and Welfare (MHLW) took steps that constituted a significant setback in the progress that had been made over the last 15 years in the medical device sector by adopting a new pricing policy that includes 'foreign average pricing' (FAP). The U.S. Government and Congress have long opposed FAP schemes, which discriminate against the U.S. industry and fail to recognize the significantly higher costs of doing business in Japan. Combined with very slow processes for the introduction of new product reimbursement prices, industry supports the following targeted proposals for reform of Japan's reimbursement system:

- Transparent, public processes and predictable rules in setting product reimbursement levels and related adjustments;
- When FAP is applied, the use of reasonable comparator U.S. list prices;
- Measures to expedite the coverage, payment and access to brand-new-to-Japan medical technologies (category C2), as per earlier trade agreement commitments; and
- Creation of payment categories that better reflect the differences in technologies.

In addition to these reimbursement concerns, industry also has pressing issues in the realm of regulatory product approvals, as Japan works to implement the 2002 Pharmaceutical Affairs Law by April 2005. A number of provisions of this law are essential to medical device products, as industry seeks to achieve a streamlined and transparent product approval process. Key issues in the PAL and other areas include (but are not limited to):

- Improved "pre-consultations" process and use of a standardized "checklist" of submission contents to clearly identify requirements prior to application submission, as well as better documentation practices within MHLW on discussions with industry (to avoid misunderstandings and to create binding decisions);
- Clearly defined review performance goals as part of the newly established user fee program. Performance goals should represent improvement over current performance and provide predictability in the review process with clearly defined procedures for stopping and restarting the review clock;
- Establishment of an appeals mechanism to resolve scientific disputes in a timely and efficient manner; and
- Better harmonization with international standards and with Global Harmonization Task Force recommendations in areas such as "adverse event reporting" and "quality systems programs" where Japan is implementing unique and burdensome requirements on manufacturers.

Going forward, industry seeks U.S. Government and Congressional support to help ensure open dialogue with Japan. We also seek assistance in securing and enforcing Japanese commitments so that restrictions in both the regulatory and reimbursement areas do not disproportionately and unfairly impact U.S. medical technology manufacturers.

In addition, the Bush Administration's efforts with Japan under the U.S.-Japan Partnership for Economic Growth are critical for achieving further market-opening measures in Japan's healthcare market.

*Regulatory and Reimbursement Obstacles Impede Market Access in Asia-Pacific*

AdvaMed looks to the U.S. government to pursue trade liberalization throughout the Asia-Pacific region, including in China, Taiwan and Korea. AdvaMed and its member companies have identified a number of real and potential barriers to doing business in these countries. While most of the barriers pertain to unnecessary or

redundant regulatory requirements, there are increasing concerns in the areas of reimbursement and intellectual property. AdvaMed looks forward to working with Congress and the Administration to address the following barriers:

- A Lengthy and Costly Product Registration Process
- Redundancy in the Registration Process
- Antiquated Type-Testing Requirements
- Lack of Transparency in Decision-Making
- Inappropriate Price Controls
- Counterfeiting of Medical Technology
- Parallel Trade of Medical Technology

For the medical technology industry, the Bush Administration's efforts with China under the U.S.-China Joint Commission on Commerce and Trade are critical for allowing U.S. medical technology firms broader access to the burgeoning Chinese health care market. The nascent U.S.-China Health Care Forum initiative, led by the U.S. Department of Commerce and supported by AdvaMed and other health care partners, holds great promise as another vehicle for addressing many of the trade-related and health policy-related barriers confronting U.S. medical technology firms in China.

China has quickly become an important market for the U.S. medical technology sector. While solid statistics are not widely available yet, AdvaMed estimates that the Chinese market for medical technology is \$3 billion and growing rapidly. It is on pace to surpass some of the key European markets for medical technology in a few short years. As global leaders, U.S. medical technology firms already account for a significant portion of sales in China and the position of these firms underscores the importance of ongoing efforts with the U.S. government to open the Chinese market further.

*Europe: Seek Appropriate Policies That Improve Patient Access to Innovative Medical Technologies*

Efforts to oversee foreign policies impacting the export and sale of U.S. medical technologies abroad should also focus on the European Union (EU). U.S. manufacturers of medical devices export nearly \$8.8 billion annually to the EU and maintain a \$1.2 billion trade surplus with the EU. Within the EU, Germany (\$20 billion) and France (\$8 billion) are the largest markets for medical devices. The industry will monitor the accession of ten new Member States on May 1, 2004 to determine the impact on exports of medical devices to the European Union.

We appreciate Congressional and Administration efforts on behalf of the industry in opposition to a European Commission draft directive that would up-classify all shoulder, hip and knee joint implants from Class IIB to Class III. This directive, which is guided by 1980s data and application of the precautionary principle, could affect thousands of devices, many of which are made by U.S. manufacturers, and would cost the average orthopedic company approximately 500,000 in fees alone for the Notified Body reviews necessary to comply with the directive. Importantly, the decision-making process on this issue has been opaque, and has offered little opportunity for stakeholder input.

In addition, the industry looks forward to the implementation of the medical device annex of the U.S.-EU Mutual Recognition Agreement (MRA). Bringing healthcare products to the market faster is an important priority consistent with the protection of public health and the reduction of regulatory costs and redundancy. The medical device industry was disappointed that the MRA transition was not completed by the original December 2001 deadline, but we anticipate that the European Commission and the FDA will complete transition activities in the near future. We ask Congress to push for the full implementation of the medical device annex of the MRA.

Finally, as the health technology assessment (HTA) trend spreads throughout Europe, EU Member States should be encouraged to adopt policies for their health technology assessment systems that are transparent, timely, and adequately account for the benefits of innovative technology. Industry should be allowed to participate in the HTA process.

*Utilize Multilateral, Regional, and Bilateral Forums to Eliminate Tariff and Nontariff Barriers to Trade that Unnecessarily Increase the Cost of Health Care*

We encourage Congressional and Administration efforts to eliminate significant tariff and nontariff barriers to trade for medical technology maintained by many countries, particularly developing countries. Such barriers represent a self-imposed and unnecessary tax that substantially increases the cost of health care to their own citizens and delays the introduction of new, cost-effective, medically beneficial treatments. For example, the medical technology sector continues to face tariffs of 15–

20% in Mercosur countries, 9–12% in Chile, Peru, and Colombia, and 6–15% in China.

The Doha Development Agenda offers an important opportunity for the United States to ensure global access to medical technology by securing global commitments on lowering tariff and nontariff barriers for the medical technology sector. We encourage the U.S. government to build upon the zero-for-zero tariff agreement on medical technology achieved in the Uruguay round by expanding the product coverage and adding countries throughout Latin America and Asia as well. Moreover, elimination of nontariff barriers such as burdensome import licensing regulations and non-transparent government procurement policies will help developing countries ensure patient access to lifesaving medical technologies.

*Utilize Multilateral Opportunities to Establish Basic Regulatory and Reimbursement Principles to Expand Global Trade and Patient Access to New Technologies*

We commend the WTO's recent efforts to ensure global access to medicines and medical products. While all economies seek to provide high quality, cost effective healthcare products and services to their citizens, they should also ensure timely access to state-of-the-art, life-saving equipment and implement compliance procedures that are efficient and effective. To further expand patient access to safe and effective medical devices and ensure cost effective regulatory compliance, USTR should seek to ensure that economies around the world make their policies and practices conform to the relevant and appropriate international trading rules established by the World Trade Organization (WTO).

Toward that end, member economies should agree to make their medical device regulatory regimes conform to these guiding principles:

- Acceptance of International Standards;
- Transparency and National Treatment;
- Use of Harmonized Quality or Good Manufacturing Practice Inspections;
- Recognition of Others Product Approvals (or the Data Used for Those Approvals);
- Development of Harmonized Auditing and Vigilance Reporting Rules;
- Use of Non-Governmental Accredited Expert Third Parties Bodies for Inspections and Approvals, where possible.

Similarly, many economies require purchases of medical technologies to take place through centralized and/or government-administered insurance reimbursement systems. To ensure timely patient access to advanced medical technologies supplied by foreign as well as domestic sources, member economies should agree to adopt these guiding principles regarding the reimbursement of medical technologies:

- Establish clear and transparent rules for decision-making;
- Develop reasonable time frames for decision-making;
- Data requirements should be sensitive to the medical innovation process;
- Ensure balanced opportunity for the primary suppliers and developers of technology to participate in decision-making, e.g., national treatment;
- Establish meaningful appeals processes.

The medical technology industry is committed to working with Congress and the Administration on upcoming trade policies and agreements to ensure patients throughout the world have access to medical products.

*Conclusion*

AdvaMed appreciates the shared commitment by the President and the Congress to expand international trade opportunities and encourage global trade liberalization. We look to the President and his Administration to aggressively combat barriers to trade throughout the globe, especially in Japan. AdvaMed is fully prepared to work with the President, USTR Ambassador Zoellick, the Department of Commerce, and the Congress to monitor, enforce and advance multilateral, regional and bilateral trade agreements, particularly with our key trading partners.

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STATEMENT OF THE ASSOCIATION OF FOOD INDUSTRIES, INC. (AFI)

Dear Mr. Chairman:

On behalf of the Association of Food Industries (AFI), I am pleased to provide comments for the record in connection with the Finance Committee hearing on President Bush's Trade Agenda, held on March 9, 2004. Given that the issue of the Byrd Amendment was raised at the hearing, I would like to share with you AFI's strong support for repeal of this law, and I hope it will be a priority issue for the Committee this year.

The Association of Food Industries is a trade association representing hundreds of U.S. importers of food products and overseas suppliers. AFI members are committed to encouraging free and fair trade and fostering compliance with U.S. laws and regulations for the food industry. One of the most significant issues facing our industry right now is the Byrd Amendment, also known as the Continued Dumping and Subsidy Offset Act (CDSOA). Total Byrd disbursements totaled \$560 million for fiscal years 2001 and 2002 and are expected to reach \$240 million for FY 2003.

The Byrd Amendment could result in severe consequences for the U.S. food importing sector. Imports of pasta, garlic, pineapple, sugar, salmon, and mushrooms are among the products most affected by the Byrd disbursements. AFI's most immediate goal is to prevent the next round of disbursements for FY 2004, because these payouts are hurting our members. Domestic food industries received over \$40 million in 2001 and 2002, with no oversight as to why they received these payouts or how they spent the money. For example, one pasta company alone received \$2.5 million in 2002.

Because the Byrd Amendment undoubtedly encourages U.S. domestic industries to file antidumping petitions against our international partners, AFI suppliers in overseas markets can no longer compete with Byrd disbursement recipients here in the United States, which, on average, received checks in excess of \$1 million each in 2001 and 2002. These disbursements increased by over 50% from 2001 to 2002, a concerning trend that will continue to undermine the ability of poorer countries to build their export sectors.

As you know, the Congressional Budget Office recently stated in a report that Byrd Amendment disbursements could total an additional \$4 billion over the next decade. This enormous expenditure on corporate welfare, with some companies receiving multimillion dollar payments each year, will come at the expense of domestic industries that consume and use the affected items. As a result, prices will increase and there could even be product shortages for automobile makers and other steel users, farmers, retailers, homebuilders, and other industries.

AFI is also fearful of the negative precedent and likely effects of failing to repeal the Byrd Amendment. As you know, the World Trade Organization has ruled that this law violates international trade rules and has called for the United States to repeal the measure. Our failure to take this step by the WTO's December 27, 2003, deadline has made U.S. companies that are not even party to this dispute vulnerable to trade retaliation by the European partners. Retaliation could run into the hundreds of millions of dollars and take effect as soon as this June.

By not complying with the WTO's ruling, we undermine our credibility in the global trade arena and make it more difficult to compel our trading partners to comply with rulings against them. Even more significantly, the continued perception of the U.S., one of the primary supporters of a worldwide system of trade rules, as a scofflaw jeopardizes the viability of the WTO itself. Leaving the Byrd Amendment in place would certainly not help efforts to reverse these trends.

AFI feels that the following are also compelling arguments for repealing the Byrd Amendment as soon as possible:

- The Bureau of Customs and Border Protection (CBP) has mismanaged the distribution of AD/CV revenues, overpaying by at least \$25 million.
- The White House has twice proposed repeal in its annual budget requests for FY 2004 and 2005.
- Lawmakers and Administration officials alike recognized that this law was bad trade policy and would violate WTO rules, which was perhaps one of the main reasons it was surreptitiously slipped into an unrelated bill without proper consideration by committees of jurisdiction.
- Finally, this law does nothing to address the underlying problems of illegal dumping and subsidization of foreign-made products, nor does it provide a way to ensure that the revenues distributed to U.S. producers are used as intended, which is to preserve U.S. jobs.

Mr. Chairman, AFI hopes that the Committee will consider repeal of the Byrd Amendment without delay. This would enable us to avoid not only foreign trade sanctions, but also the serious negative effects on our industry, and the domestic economy more generally, that would be caused by another round of corporate welfare handouts. We sincerely appreciate your consideration of this issue and stand ready to assist you in any way we can to achieve a repeal of this law.