

1992

**THE EFFECTS OF GREATER ECONOMIC
INTEGRATION WITHIN THE EUROPEAN
COMMUNITY ON THE UNITED STATES:
SECOND FOLLOWUP REPORT**

Investigation No. 332-267

USITC Publication 2318

September 1990

UNITED STATES INTERNATIONAL TRADE COMMISSION

UNITED STATES INTERNATIONAL TRADE COMMISSION

COMMISSIONERS

Anne E. Brunsdale, Acting Chairman

Seeley G. Lodwick

David B. Rohr

Don E. Newquist

Office of Industries

Robert A. Rogowsky, Director

**Address all communications to
Kenneth R. Mason, Secretary to the Commission
United States International Trade Commission
Washington, DC 20436**

**THE EFFECTS OF GREATER ECONOMIC
INTEGRATION WITHIN THE EUROPEAN
COMMUNITY ON THE UNITED STATES:
SECOND FOLLOWUP REPORT**



*USITC Publication 2318
Investigation No. 332-267*

**United States International Trade Commission
Washington, DC 20436**

THE EFFECTS OF GREATER ECONOMIC INTEGRATION WITHIN THE EUROPEAN COMMUNITY ON THE UNITED STATES

Project Staff

Project Leader

John J. Gersic

Deputy Project Leader

James A. Emanuel

Project Coordinators

Lee Cook, Mark Estes, Sylvia McDonough, Dennis Rapkins, Elizabeth Root,
Linda Shelton, Wanda Tolson, Robert Wallace

Assisted by

Marilyn Borsari, Cynthia Foreso, James Lukes, Cynthia Payne

Team Leaders and Major Contributors¹

- Chapter 1, "Introduction to the Europe 1992 Program" – *Joanne Guth and Paul Bardos*
Chapter 2, "Review of Customs Union Theory and Research on the 1992 Program" – *Joseph Flynn*
Chapter 3, "U.S. Trade and Investment in the EC" – *David Michels*
Chapter 4, "Standards, Testing, and Certification" – *Kim Skidmore Frankena, Paul Bardos, Andrea Casson, and Rhonda Hughes*
Chapter 5, "Financial Sector" – *Daniel Shepherdson*
Chapter 6, "Public Procurement and the Internal Energy Market" – *Joanne Guth*
Chapter 7, "Customs Controls" – *Janis Summers*
Chapter 8, "Transport" – *Marc Bernstein and Nelson Hogge*
Chapter 9, "Competition and Corporate Structure" – *Elizabeth Hafner*
Chapter 10, "Taxation" – *William Gearhart*
Chapter 11, "Residual Quantitative Restrictions" – *Joanne Guth*
Chapter 12, "Intellectual Property" – *Wayne Herrington*
Chapter 13, "EC Integration, the GATT, and the Uruguay Round" – *Susan Bloom*
Chapter 14, "EC Integration and Other EC Commitments" – *Katherine Jones*
Chapter 15, "The Social Dimension" – *Andrea Casson*
Chapter 16, "Research and Development" – *Sylvia McDonough, William Fletcher, Timothy McCarty, and Sundar Shetty*
Chapter 17, "Reciprocity" – *Daniel Shepherdson*
Chapter 18, "Rules of Origin and Local-Content Requirements" – *Janis Summers*
Chapter 19, "Industry and Company Action and Reaction" – *William Warlick*
Chapter 20, "Automotive Sector" – *Dennis Rapkins and Juanita Kavalauskas*
Chapter 21, "Telecommunications Sector" – *Nelson Hogge and Scott Baker*
Chapter 22, "Chemicals and Pharmaceuticals Sector" – *Ed Cappuccilli, Eric Land, and Elizabeth Nesbitt*

Other Contributors

Peder Andersen, James Bedore, Sujit Chakravorti, Michael Hagey, Olha Holoyda, Kathleen Lahey,
David Ludwick, Ruben Mata, Ruben Moller, Mary Murphy, Kelly Nunis, Cynthia Trainor, Tom Westcot

Industry Analysts

Stephen Burket, Kenneth Conant, Roger Corey, Alfred Dennis, William Greene,
John Kitzmiller, Alvin Macomber, Douglas Newman, Rick Rhodes, Victoria Salin,
Rose Steller, Adam Topolansky, Fred Warren

Administrative Staff

Chief Designer, *Pamela Chase*
Designers, *Keven Blake, Joyce Bookman, Paulette Henderson*
Chief Editor, *David Saia*
Associate Editors, *Clifford Brown, Helen Troupas*
Secretaries, *Brenda Carroll, Maroa Tinner, Paula Wells, Sharon Williams*
Clerk-Typist, *Linda Cooper*

¹ Team leaders were also major contributors to their respective chapters.

PREFACE

On October 13, 1988, the United States International Trade Commission (Commission) received a joint request from the House Committee on Ways and Means and the Senate Committee on Finance (presented as app. A) for an investigation under section 332(g) of the Tariff Act of 1930 (19 U.S.C. 1332(g)), to provide objective factual information on the EC single market and a comprehensive analysis of its potential economic consequences for the United States. The committees requested that the Commission provide a report by July 15, 1989, with followup reports as necessary. In response to the request, the Commission instituted investigation No. 332-267 on December 15, 1988. The report was issued in July 1989, and the first followup report was issued in March 1990.

In their letter of request, the committees stated that the form and content of the policies, laws, and directives that remove economic barriers and restrictions and harmonize practices among the EC member states may have a significant impact on U.S. business activities within Europe overall and in particular sectors, and further, the process of creating a single market may also affect progress and results in the ongoing Uruguay Round of GATT multilateral trade negotiations. The committees requested that the Commission study focus particularly on the following aspects of the EC's 1992 program:

1. The anticipated changes in EC and member-state laws, regulations, policies, and practices that may affect U.S. exports to the EC and U.S. investment and business operating conditions in the EC.
2. The likely impact of such changes on major sectors of U.S. exports to the EC and on U.S. investment and business operating conditions in the EC.
3. The trade effects on third countries, particularly the United States, of particular elements of the EC's efforts.
4. The relationship and possible impact of the single-market exercise on the Uruguay Round of GATT multilateral trade negotiations.

The committees also stated in their letter that "Given the great diversity of topics which these directives address, and the fact that the remaining directives will become available on a piecemeal basis, the Commission should provide the requested information and analysis to the extent feasible in an initial report by July 15, 1989, with followup reports as necessary to complete the investigation as soon as possible thereafter." The initial report contained background, introductory, definitional, and descriptive material related to the EC 1992 program. It also discussed the institutional framework and procedures for the implementation of the EC 1992 program. The bulk of the initial report, however, consisted of the discussion and analysis of changes expected from the implementation of those directives issued prior to January 1, 1989, grouped into key categories, and information and analysis of the EC 1992 program and its relation and impact on the GATT, the Uruguay Round, and other EC member-state obligations and commitments to which the United States is a party. The first followup report essentially followed the format of the initial report, with summaries of each of the initial report's chapters and discussions of developments since January 1, 1989. That report included expanded coverage of local-content requirements, rules of origin, directive implementation by member states, and the social dimension of integration. This second followup report follows the same format and covers developments since January 1, 1990.

Copies of the notice of the second followup report, including the schedule of a public hearing, were posted at the Office of the Secretary, U.S. International Trade Commission, Washington, DC. The notice was published in the *Federal Register* (55 F.R. 12566) on April 4, 1990, and is included in appendix B of this report, along with the original *Federal Register* notice and first followup report notice.

CONTENTS

	<i>Page</i>
Preface	i
Executive summary	v
 Part I. Introduction and background	
Chapter 1. Introduction to the Europe 1992 program	1-1
Chapter 2. Review of customs union theory and research on the 1992 program	2-1
Chapter 3. U.S. trade and investment in the EC.	3-1
 Part II. Anticipated changes in the EC and potential effects on the United States	
Chapter 4. Standards, testing, and certification	4-1
Chapter 5. Financial sector	5-1
Chapter 6. Public procurement and the internal energy market	6-1
Chapter 7. Customs controls	7-1
Chapter 8. Transport	8-1
Chapter 9. Competition policy and company law	9-1
Chapter 10. Taxation	10-1
Chapter 11. Residual quantitative restrictions	11-1
Chapter 12. Intellectual property	12-1
 Part III. Implications of EC market integration for GATT, the Uruguay Round, and other international commitments	
Chapter 13. EC integration, the GATT, and the Uruguay Round	13-1
Chapter 14. EC integration and other EC commitments	14-1
 Part IV. Other policies and special topics	
Chapter 15. The social dimension	15-1
Chapter 16. Research and development	16-1
Chapter 17. Reciprocity	17-1
Chapter 18. Rules of origin and local-content requirements	18-1
 Part V. Anticipated changes in the EC and potential effects on certain U.S. industries	
Chapter 19. Industry and company action and reaction	19-1
Chapter 20. Automotive sector	20-1
Chapter 21. Telecommunications sector	21-1
Chapter 22. Chemicals and pharmaceuticals sector	22-1
 Appendixes	
A. Request letter	A-1
B. <i>Federal Register</i> notices	B-1
C. Calendar of public hearing	C-1
D. List of EC 92 initiatives addressed in this investigation	D-1
E. Index of industry/commodity analyses contained in report chapters 4 through 12	E-1

EXECUTIVE SUMMARY

The European Community (EC), as it is known today, was created by the merging of three original communities, the European Coal and Steel Communities (ECSC), the European Economic Community (EEC), and the European Atomic Energy Community (Euratom). The Treaty Establishing a Single Council and a Single Commission of the European Communities signed in 1965 effectively completed the formation of the EC.

Although the EC has had no internal customs duties and has had common external duties, internal as well as external trade has encountered numerous nontariff obstacles. These barriers principally developed as EC countries attempted, from time to time, to insulate particular industries or products after internal duties were eliminated. These measures were usually effective for the purposes devised, but they did have costs. Whereas the costs were tolerable in the 1950s and 1960s, they became more onerous in the late 1970s as most European economies slowed and a general "Eurosclerosis" developed that also reduced the competitiveness of the EC nations in the world market.

A recognition of these costs and the desire to complete the internal market, begun with the formation of the EC and the elimination of internal duties, were at least partially responsible for the White Paper issued by the EC Commission in June 1985. This White Paper contained broad goals for the integration program and set a date of December 31, 1992, for the complete elimination of physical, fiscal, and technical barriers to trade. This was to be accomplished through the issuance of approximately 280 directives dismantling barriers.

The initial USITC report, issued in July 1989, contained three sections. The first section addressed (1) the genesis of and prospects for the 1992 program, (2) the institutional framework and procedures for implementation of the 1992 program, (3) the descriptive and definitional aspects of the 1992 program, and (4) U.S. trade with the EC. The second section analyzed the changes expected from the implementation of each of the 261 measures issued or proposed prior to January 1, 1989, grouped into key categories. The third section contained information on and analysis of the implications of the 1992 program for GATT, the Uruguay Round, and other EC member-state obligations and commitments under bilateral or multilateral agreements and codes to which the United States is a party.

The first followup report issued in March 1990 followed the same format as the initial report. A brief summary of each of the initial report's chapters was followed by a discussion of new developments in the chapter area primarily for the period January 1, 1989, through December 31, 1989. The report also contained expanded coverage of the social dimension of integration, local-content requirements, rules of origin, and directive implementation by member states.

This second followup report follows the previous format and covers the period since December 31, 1989. In addition, this report contains chapters on research and development and three industry sectors—automobiles, telecommunications, and chemicals and pharmaceuticals.

A public hearing was held on June 21, 1990, in connection with the second followup report of this investigation. The calendar of the public hearing is presented as appendix C. A list of EC 92 initiatives addressed in this investigation is presented as appendix D, and an index of industry/commodity analyses contained in chapters 4 through 12 is presented as appendix E.

The highlights of this investigation are summarized below, by report section.

Introduction and Background

Introduction to the Europe 1992 Program

- *Under the Irish presidency of the EC Council of Ministers during the first half of 1990, the EC continued to pass the legislation needed to effectuate the 1992 integration program.*

At the end of that presidency, all of the 282 planned internal market measures had been issued by the EC Commission as proposals to the EC Council, which had formally adopted 164 of the measures.

- *The EC is planning significant changes to its institutional framework.*

Political union is the most notable development, along with the creation of new agencies such as a central bank and an environmental agency. However, in addition, the EC institutions are discussing their existing relationships in such debates as the current one over the EC Commission's use of article 90 to enforce member-state compliance with EC law.

Article 90 of the Treaty of Rome applies the treaty's rules on competition to public undertakings, i.e., business entities run by member-state governments, and undertakings that are granted special or exclusive rights. The article also empowers the EC Commission to issue directives and decisions to EC member states to enforce those rules. By issuing directives itself under article 90 rather than proposing directives to the Council and Parliament under article 100A, the EC Commission avoids the more complicated cooperation procedure and may prompt the other institutions and the EC member states to suspect that the EC Commission is claiming more power for itself than is appropriate.

- *The EC 92 process may well be the first step towards wider European integration.*

The EC and EFTA nations recently approved mandates to negotiate a European Economic Space (EES) that would enable the free movement of goods, persons, services, and capital between the 18 EC and EFTA countries as well as Liechtenstein. At the same time, the countries of central and Eastern Europe as well as the U.S.S.R. are forging closer ties with both the EC and EFTA. By July 1, 1990, the EC had concluded a network of bilateral trade and economic cooperation agreements with all of the European Council for Mutual Economic Assistance (CMEA) countries except Romania. The EC plans to negotiate more extensive association agreements with these countries in the near future.

- *Although German reunification and the reforms taking place in central and Eastern Europe are momentous events, the EC, including West Germany, appears determined to meet the goals of the single-market process on time.*

The prevailing opinion is that these changes have in fact spurred the EC integration process in order to anchor Germany firmly within the EC, to better meet the demands of the reforming countries, and to ensure the EC's role as a model for these countries.

- *Overall member-state implementation of 1992 measures continues to proceed slowly.*

The pace of implementation differs from member state to member state. The United Kingdom, West Germany, and France have generally good records, but on occasion encounter difficulties in implementation. Spain is a newcomer to the EC and needs to catch up with member states of longer standing.

Overall, as of January 17, 1990, only 14 of the 86 single-market directives that should have already been transposed into national law had been fully transposed by all member states.

The EC Commission, charged with monitoring implementation, is using court action and other means when necessary to force member states to implement measures. The success of the EC 92 exercise is contingent on member-state implementation of EC legislation.

Review of Customs Union Theory and Research on the 1992 Program

- *The EC 1992 program will expand trade within the EC. However, customs union theory alone cannot predict whether trade with nonmember countries will increase or decrease.*

Reduction of internal trade barriers under the 1992 integration program will create trade between EC member countries, although at the expense of less efficient domestic producers in those member states. The internal trade liberalization will also tend to increase trade among EC countries at the expense of existing trade with more efficient producers in the United States and other nonmember countries. Producers in nonmember countries will benefit if the EC 1992 program boosts growth in the EC.

- *Certain recent economic research on the EC 1992 program is skeptical about the estimates reported in the Cecchini Report.*

Certain research studies on the EC 1992 program conclude that certain economic assumptions, limitations, and omissions made in the Cecchini Report result in estimates of

welfare gains that are too optimistic. Moreover, the Cecchini Report does not specify the distribution of the welfare gains among the EC nations and assumes that the gains flow to consumers. Also, projected gains in employment by the EC Commission are regarded as ambitious. It is noted that the EC Commission's estimate does not allow for the fact that part of the output growth is due to productivity gains that result in lowering employment.

- *Other research studies, however, conclude that the Cecchini Report underestimates the benefits of the EC 1992 program because dynamic effects are not accounted for in the estimates.*

The research studies conclude that the greatest benefits of market liberalization are not in the one-time effects on resource allocation but rather in the dynamic effects of more innovation, faster productivity gains, and higher growth rates for output and income. In fact, it is argued that the 1992 program impact on EC Gross Domestic Product – including the dynamic effects – could be between 40 and 3,900 percent greater than current static estimates. Furthermore, the estimates suggest that the proposed market integration could permanently add between one-quarter and one full percentage point to the EC growth rate.

Overall, it is still too early in the EC 92 process to know whether the estimates in the Cecchini Report are pessimistic, optimistic, or realistic.

U.S. Trade and Investment in the EC

- *The EC program could affect U.S. trade and the trade balance with the EC.*

The EC has been the largest export market for the United States since 1987 and the second-largest source of U.S. imports since 1985. The EC has consistently supplied about 19 percent by value of total U.S. imports and has accounted for about 23 percent of the total U.S. export market during 1987-89.

- *EC imports from Eastern Europe were virtually unchanged between 1984 and 1987. EC exports to Eastern Europe increased steadily, at an average rate of 9 percent per year.*

EC imports from these countries amounted to \$28 billion in 1987, representing a decline of 1 percent from the 1984 figure. Imports in 1985 and 1986 were lower than in 1984 and 1987. Exports to Eastern Europe amounted to \$22 billion in 1987, representing an increase of 27 percent over the 1984 figure. Exports to the Soviet Union reached \$10.6 billion – 48 percent of all EC exports to Eastern Europe, and imports from the Soviet Union amounted to about \$15 billion, or about 53 percent of total EC imports from Eastern Europe.

- *U.S. investment in the EC increased in 1989.*

Cumulative U.S. investment in the 12 EC member states in 1989 was \$150.0 billion, representing an increase of 14 percent in overall cumulative investment from 1988. U.S. investment in the EC made up 40 percent of total U.S. foreign investment in 1989.

- *The EC investment in the United States in 1989 totaled \$234.8 billion.*

The EC 12 member states had direct investment in the U.S. totaling \$234.8 billion in 1989, about 58 percent of the total \$400.8 billion of foreign investment in the United States. EC investment in the United States in 1989 represented an increase of 21 percent over the level of \$194 billion recorded in 1988.

Anticipated Changes in the EC and Potential Effects on the United States

Standards, Testing, and Certification

- *The EC continued to make progress during 1990 on developing the regulatory and other requirements for products to be sold in the European market after 1992.*

A large portion of the standards directives for the EC 1992 program have been at least initially introduced. While the pace of EC work in the area of animal and plant health accelerated in 1990, progress remained slow. Mechanisms put into place in 1989 to improve

transparency of the drafting process and provide U.S. suppliers with some influence over the standards-drafting process appeared to be working reasonably well. Reportedly, there was also some evidence that environmentalists, consumers, and workers were exerting greater influence on the EC's standards-development process.

- *During 1990, the focus of interest in the standards-developments area shifted from the legislative front to Europe's private regional standardsmaking institutes.*

Growing concern was voiced over the slow rate of progress by the regional standardsmaking institutes—the European Committee for Standardization (CEN), the European Committee for Electrotechnical Standardization (CENELEC), and the European Telecommunications Standards Institute (ETSI). These bodies are behind schedule in the creation of standards that are essential to the elimination of technical barriers in the EC. Largely as a result of these concerns, the EC Commission released a draft of its Green Paper on standardization. This paper laid out a number of recommendations to bring a higher level of coordination, power, and resources to the regional standardsmaking bodies and to expand participation by affected interests.

- *Use of common standards in bid specifications has long been recognized as key to the EC's goal of a more open environment for public purchasing.*

On May 21, 1990, a working document on EC policy towards use of harmonized European standards in public procurement was released. The paper reaffirmed the obligation imposed by EC law on public purchasers in the member states to use harmonized European standards, technical specifications, technical approvals, and quality-assurance schemes in their procurement specifications, even though compliance with such standards is normally voluntary. This obligation is expected to play a major positive role in future U.S. access to the public sector market in the EC for products such as telecommunications equipment, power-generation equipment, water supply equipment, and public works construction.

- *Testing and certification remained a prominent issue in 1990, as the EC Commission worked to refine its policy towards the acceptance of test results from outside the EC.*

U.S. companies and associations generally support the development of a transparent EC approval process that is fair, equitable, nondiscriminatory, not overly burdensome, and enhances trade. However, some are concerned that the EC's proposed testing and certification policy may place them at a competitive disadvantage relative to firms producing in the EC should the EC fail to accept tests generated outside the EC for purposes of demonstrating conformity with EC requirements.

The EC continued to refine its "Global Approach" to testing and certification, notably the conditions under which it would accept tests generated outside the EC for purposes of regulatory enforcement. During the first 6 months of 1990, EC officials took pains to reassure the Community's trading partners that foreign suppliers will continue to be accorded national treatment in product-approval schemes consistent with the Community's international obligations. EC officials have said that they will encourage the arrangements between EC and non-EC parties on the mutual recognition of test results.

- *Several factors, including the strengthening of the EC's environmental authority in the Single European Act, response to environmental catastrophes, the increased influence of the Green Party, and increased public awareness of environmental issues, have contributed to the EC's growing emphasis on environmental themes as it moves towards market unification.*

EC and member state legislation in the environmental area is among the most active, including proposed or recently adopted directives on the establishment of a European Environmental Agency; freedom of environmental information; disposal and transportation of hazardous waste; civil liability for damage caused by waste; water quality; air pollution; biotechnology; and chemical labeling. These directives undoubtedly will increase costs and affect business planning and operations for all businesses operating in the EC, including U.S.-owned firms. However, the increase in EC environmental legislation has, and will continue to create opportunities for environmental consultants, attorneys, and engineers, as well as environmental control firms—fields in which U.S. firms have a leading expertise. These directives are also likely to open opportunities for U.S. exports of pollution control systems.

- *In the standards area, labeling requirements, advertising restrictions, and standards for service have been employed in an effort to ensure that consumers' "right to know" is protected and to prevent fraudulent or misleading claims by suppliers.*

The original Treaty of Rome did not explicitly establish consumer protection policy as an EC goal. However, the interests of consumers have been protected by such longstanding EC programs as EC competition law, which forbids unfair practices that can drive up consumer prices. Article 100A(3) of the Treaty of Rome, added by the Single European Act, states that the EC will in its consumer protection measures take as a base a high level of protection, in order to ensure consumer confidence in the functioning of the internal market.

The EC's consumer protection policy has directly resulted in the proposal of only a small number of EC 1992 directives, which mainly aim at protecting economic interests. There are, however, other EC 1992 measures that involve consumer protection even though they mainly address other concerns, such as safety and health, and insurance.

- *The EC's public health and safety policy is one that is still in the early stages of development and, thus, is still evolving.*

The EC aims to eliminate to the fullest extent possible technical barriers preventing the free movement of goods among its member states, while recognizing national differences in producing the goods that may affect their safe use in other member states. However, what is considered to be a health or safety problem in one country is not necessarily considered to be a problem in another. This is particularly true in the animal and plant health area.

The most important issues in the public health and safety arena pertain to foodstuffs and pharmaceuticals. The EC's free trade in foodstuffs program aims to set general food safety and hygiene standards and establish a more informative system of labeling.

Financial Sector

- *The 1992 program for financial services has raised interest and concern in the United States.*

Liberalized and open financial and capital markets in the EC should create potential business opportunities for U.S. financial-services firms. EC capital markets and financial firms are likely to become relatively more competitive and efficient, thereby benefiting EC consumers. The liberalization of the EC's financial sector has prompted further consideration of whether reform of the U.S. regulatory system is necessary or appropriate to maintaining or enhancing the global competitiveness of the U.S. financial sector.

- *Legislative progress with the 1992 banking measures and the liberalization of capital movements and mutual funds has been followed, albeit more slowly, in the securities and insurance area.*

In June 1990, the EC Council reached a common position on the amended proposal for a Second Life Insurance Directive. The directive would permit a life insurance firm to sell life policies on a cross-border basis to groups and individuals. In the securities area, the EC Commission has issued the proposed Capital Adequacy Directive, after considerable debate within the EC. Like the Own Funds and Solvency Ratio Directives in the banking area, the proposal would set capital requirements for investment firms that undertake investment services throughout the Community.

- *Market access by third-country financial firms will be subject to the Community's reciprocity policy, which is based on "national treatment and effective market access."*

The EC could seek to negotiate with the United States in order to obtain "comparable competitive opportunities," which could be defined by the EC to include the right of an EC bank or securities or insurance firm to sell a wide range of financial services throughout the United States under a single authorization. In other words, the EC might seek to receive better than national treatment in the United States.

Public Procurement and the Internal Energy Market

- *The goal of the 1992 program in public procurement is to remove longstanding barriers at the member-state level by establishing rules to encourage more open public procurements, transparency, and nondiscrimination in all phases of public purchasing.*

- *The most noteworthy development in the area of public procurement during the first half of 1990 was an agreement for a common position on the directive covering the four so-called excluded sectors of water, energy, transport, and telecommunications.*

The major changes incorporated into the common position covering the excluded sectors raised the threshold value for supplies contracts above which the directive applies and introduced conditions allowing entities involved with the exploration for or extraction of oil, gas, coal, or other solid fuels to be exempted from the directive's requirements. Although the most controversial provision of the directive for non-EC firms—the 50-percent content rule—remained unchanged, the common position established a new rule of origin based on the last substantial transformation.

- *The EC Commission outlined a strategy to increase the participation of small and medium-sized enterprises (SMEs) in public procurement markets.*

The EC Commission proposed a variety of initiatives to help SMEs win public contracts without imposing higher costs on the purchaser or discriminating against larger firms. These proposals include (1) facilitating access of SMEs to award procedures by dividing larger contracts into lots, by promoting association among SMEs to reach a scale appropriate to participation in public contracts, by encouraging subcontracting, and by eliminating unnecessary qualification requirements; (2) minimizing administrative and financial costs for SMEs by simplifying procedures and accelerating the flow of bidding information; and (3) preparing SMEs for effective participation in contract-award procedures through training, technical support, and expanded use of electronic bidding information services and public procurement data bases.

- *U.S. industry claims that the EC's public procurement markets are not likely to open significantly in the short run. U.S. suppliers are particularly concerned that the 50-percent content rule in the excluded-sectors directive will place U.S. firms at a disadvantage.*

Evidence indicates that the public procurement sector is the area that shows the strongest potential for increased investment in the EC. Some U.S. companies recommend accommodating their concerns over the 50-percent content rule by strengthening the GATT Code on Government Procurement to cover the excluded sectors.

- *The four directives constituting an important part of the EC's internal energy market program are aimed at reducing price opacity and market compartmentalization in the energy sector.*

The EC Council adopted a directive covering the transparency of gas and electricity prices and reached a common position on the directive covering the transit of electricity through transmission grids. Two measures were delayed—the regulation requiring notification of investment projects of Community interest to the EC Commission and the directive covering the transit of natural gas through the major systems. The first was delayed because of concerns over unnecessary EC Commission intervention in investment planning, and the second, because of concerns over applying the principle of common carriage to the gas sector.

- *The creation of an internal energy market is likely to increase competition among energy suppliers and cause restructuring of the EC energy sector.*

U.S. companies supplying coal and energy equipment, as well as U.S. firms operating in the EC, should benefit from the internal energy market program. The more competitive environment will likely permit more third-country suppliers of coal and energy equipment to participate in the energy market and will eventually lower operating expenses for all firms established in the EC.

Customs Controls

- *The EC is attempting to complete the task of eliminating internal customs formalities, replacing them with controls at the external boundaries of the Community, and to achieve freedom of movement and employment for persons residing in the EC.*

The resulting reduced costs and delays are likely to benefit both EC and foreign firms. The EC Commission's goal is that all regulation of external trade will eventually occur at the

member states' borders with other countries and at other points of initial entry into the EC. Important efforts were also made toward free movement of persons, mutual recognition of professional and vocational qualifications, and expansion of the authority of EC institutions to ensure that places of work in the EC will be safe and healthy. All of these initiatives were favorably received by interested parties outside the EC, although concerns were raised on other aspects of EC customs administration and trade policy.

- *The level of EC legislative activity in the area of customs controls has abated, because relevant proposals have been issued if not adopted.*

The most significant development, in the area of free movement of goods, is the issuance of the EC Commission's proposed Common Customs Code for the EC. This regulation would include existing customs measures and those relating to the integration process in a single document, adding new procedures for obtaining and appealing customs rulings and for placing goods in free circulation. In addition, amendments to several other proposed directives were submitted by the EC Commission.

- *Free movement of persons (whether or not they are workers) continued to receive attention as a very important aspect of integration, but no new directives concerning the recognition of professional and vocational qualifications occurred.*

The effort to achieve German unification prompted greater interest in EC measures and policies relating to employment opportunities and social benefits, as East Germans would become able to move freely throughout the EC. The EC institutions continued to monitor changes in Eastern Europe as well as efforts within the member states to work toward harmonized EC policies on immigration, asylum, and related issues.

Transport

- *Transport directives are designed to introduce competition into the air-, water-, road-, and passenger-transport industries within the EC.*

These directives do not deal directly with third-party rights covered under existing bilateral agreements, and uniform implementation of the directives by individual member states may not be achieved.

- *The United States supports the aviation liberalization measures being undertaken by the EC and anticipates that these measures will lead to increased opportunities for U.S. and EC air carriers across the North Atlantic.*

The United States has urged that airline services, such as computer reservations systems, slot allocations, and air cargo, be made available to U.S. air carriers on a fair and nondiscriminatory basis.

- *In March 1990, the EC Transport Minister indicated that the EC had started a process aimed at gradually replacing member-state bilaterals with third countries with Community bilaterals.*

A U.S. Government transport official indicates, however, that the current bilateral air-carrier agreements existing between the United States and the EC member states are not likely to be changed in the foreseeable future. The official did indicate that whenever bilaterals are negotiated in the future, both EC officials and officials from the affected member states must be present at the negotiations.

- *The EC issued a proposal covering safeguard mechanisms in the event a crisis occurs in the road-transport sector.*

The proposal defines a crisis as a serious and lasting imbalance between supply and demand that results in a clear excess capacity and that threatens the financial stability of a significant number of road-haulage firms. Solutions offered to solve the crisis include temporarily limiting capacity, encouraging firms to convert to other lines of business, or encouraging haulers to engage in other road-transport markets where there are no imbalances.

Competition Policy and Company Law

- *The EC Commission has issued draft documents to explain the difference between cooperative and concentrative joint ventures and to define ancillary restrictions to clarify confusing aspects of the Merger Regulation.*

In preparation for the upcoming effective date for the Merger Regulation passed by the Commission on December 21, 1990, the Commission has adopted Implementing Regulations and a Notification Form CO, which set forth the procedures for notifying the Commission on a proposed merger.

The Commission has also issued two notices; a Notice on Ancillary Restrictions and a Notice on Concentrative and Cooperative Joint Ventures. These Notices clarify how the Commission will interpret these terms as it applies the Merger Regulation.

- *The EC Commission is moving forward in trying to eliminate barriers to takeovers in the EC.*

A new draft Thirteenth Company Law Directive on Takeovers may be submitted to the EC Council before the end of the year.

- *The Economic and Social Committee (ESC) has submitted to the EC Commission its comments on the European Company Statute.*

Although the ESC generally supports the statute, it recommended some procedural changes to clarify the statute as well as substantive changes to increase the efficiency of a European company and to effectuate employee participation provisions.

Taxation

- *EC tax initiatives related to the 1992 program have focused on three areas: (1) harmonization of indirect taxes (value-added taxes (VAT) and excise taxes), (2) action on three long-outstanding proposed directives regarding intracompany transfers, and (3) possible tax evasion resulting from the liberalization of capital movements.*

The focus of EC tax harmonization efforts has been in the area of indirect taxes, because these taxes are applied at member-state borders. Tax harmonization has been one of the most difficult issues facing the EC 1992 effort because changes in rates and coverage can have significant revenue, political, and social implications for individual member states.

- *The EC continued to move forward on taxation matters during the first half of 1990.*

With regard to VAT, discussions were held in February concerning the scope of a lower rate VAT, and in May the EC Commission presented proposals for the transitional arrangements for the collection of VAT during the interim period January 1993-December 1996. In April, a compromise proposal was advanced for a phaseout of VAT-related restrictions on out-of-state purchases by travelers, which must occur by January 1, 1993, but no agreement was reached. With regard to company taxation, in April the EC Commission issued a major communication on company taxation, and in June the Council approved all three of the proposed corporate tax directives after a compromise was reached with West Germany. The liberalization of EC capital movements became effective as scheduled on July 1, 1990, without final action on any of the proposed anti-tax-evasion measures.

Residual Quantitative Restrictions

- *The EC Commission intends to eliminate existing, or residual, national quantitative restrictions (QRs) by the end of 1992 because they will be unenforceable in the single, integrated market.*

The EC Commission has not indicated how it intends to address national QRs in sensitive sectors other than automobiles. In the automobile sector, the EC Commission is seeking an EC-wide voluntary restraint arrangement with Japanese producers for an undetermined transition period beginning no later than January 1, 1993. EC Commission officials claim that the plan for an EC-wide restraint on automobiles would not be extended to other sectors.

Intellectual Property

- *The issue of intellectual property rights in the EC is an important one for the United States.*

Many U.S. products sold in the EC are or can be protected by some intellectual property right. Such rights are especially important for firms selling high-technology products such as biotechnology and computer software, because of the considerable investment often required to develop such products (e.g., biotechnology), the ease in copying such products (e.g., computer software), or both.

- *The proposed regulation on the creation of a supplementary protection certificate for medicinal products would create a new instrument to extend the term of patents for medicinal products, the marketing of which has been delayed due to required regulatory approval.*

The maximum extension would be for 10 years. The additional period of exclusivity would permit more time for firms owning such patents to recoup their investment in research and development.

Implications of EC Market Integration for GATT, the Uruguay Round, and Other International Commitments

EC Integration, the GATT, and the Uruguay Round

- *The United States and other countries are concerned that the EC 1992 program might result in increased protectionism or discrimination against their exports.*

Specific concerns include reciprocity, transparency, transitional measures on autos and textiles, and standards and certification issues. Also, the EC trading partners are apprehensive over limits on national treatment, requirements for third countries to continue trading in the EC, local-content rules, and quantitative restrictions.

- *The EC 1992 program may have an impact on the Uruguay Round of GATT multilateral trade negotiations.*

The Uruguay Round of multilateral trade negotiations, which are scheduled to end in December 1990, may be affected by the EC 1992 program. However, because negotiations are still ongoing there is little definite information on the impact of the EC program in this area.

EC Integration and Other EC Commitments

- *In the previous USITC reports on the EC 92 program, this chapter discussed agreements other than the General Agreement on Tariffs and Trade (GATT), to which the United States and the EC or its member states are a party, with which the 1992 program might conflict.*

The first followup report discussed three specific areas in which such conflicts might arise: (1) various international human rights treaties and the Broadcast Directive, (2) the OECD Codes and reciprocity requirements in the Second Banking Directive and other directives, and (3) bilateral Memoranda of Understanding (MOUs) and certain aspects of the EC standards program.

- *Since the first followup report was published, there have been few new developments in any of the three areas discussed.*

Anticipated discussions in the OECD regarding the best method of reconciling the Second Banking Directive and the OECD Codes have not yet taken place and there have been few new developments in the standards area relating to intergovernmental agreements. Developments regarding the EC's "Global Approach to Certification and Testing" are discussed in chapter 4, Standards, Testing, and Certification.

Other Policies and Special Topics

The Social Dimension

- *In the first half of 1990, the EC Council adopted several labor directives, all of which address worker safety and health.*

The Council has adopted three more directives falling within the Framework directive for worker safety and health. The newly adopted directives address visual display units (VDUs), the handling of heavy loads, and worker exposure to carcinogens. The VDU standard is likely to require changes in many work places, given the prevalence of this type of equipment. Industry representatives object to this directive because they believe it presupposes a risk without scientific evidence of such risk.

- *The EC Commission has presented proposed directives on two of the subjects included in the social dimension action program and is in the process of drafting directives on several other action program measures.*

The EC Commission has presented a package of three proposed directives addressing temporary and part-time work. The EC Commission has also proposed a directive setting requirements for shift and night work and establishing daily and weekly rest periods. Industry representatives believe these directives reach into areas that should be left to collective bargaining.

- *The social dialog between management and labor has been ongoing in 1990.*

The Social Dialogue Steering Committee met in January and July and will meet again in September. It has adopted a joint option on education and training and has progressed on an option discussing the European job market.

Research and Development

- *In 1987, the Single European Act included a provision for the formation of a multiyear, cooperative R&D program, the Framework Program, that gave science and technology policy equal status in the EC with social and economic policy.*

For the period 1987-94, the EC has allocated 11.1 billion ECU to these research and development programs and matching funds from private and government sources have increased this amount by more than 75 percent. The principal focuses of the Research and Development (R&D) programs are information and communications technologies; industrial and materials technologies; and energy, especially nuclear fusion. The goal of the EC research and development policy is to maintain and increase the international competitiveness of European industry, especially in high-technology markets.

- *U.S. firms have complained that they are relegated to a second-class role in EC R&D programs because no U.S. firm is on the program-selection boards or the program advisory committees, which control the direction of the major projects.*

In reply, EC officials have stressed the openness of their research system, stating that "every natural or legal person under public or private law who is resident or established in an EC member state" is eligible to participate. The Framework programs require non-EC companies to have what is called an "integrated presence" in Europe, which means that a company wishing to participate must engage in production, marketing, and research operations in the EC. For example, U.S. organizations with EC research facilities have participated in the ESPRIT program; however, outside participation by non-EC members has been primarily as subcontractors rather than principal researchers.

Reciprocity

- *The European Community's reciprocity policy has raised concerns that access to the single market could be unduly restricted in certain sectors for third-country firms.*

Reciprocity provisions have been incorporated in various 1992 measures, including directives that cover financial services, testing and certification, government procurement, merger control, and intellectual property. In general, reciprocity provisions effectively

provide for conditional national treatment, making nondiscriminatory market access contingent upon how EC firms are treated in the third country concerned. The United States has continuing concerns about the Community's reciprocity policy and is monitoring its interpretation and implementation.

- *The United States maintains that the Community's reciprocity policy is inconsistent with the Community's international obligations, including the OECD Codes and bilateral Friendship, Commerce, and Navigation (FCN) agreements, and may undermine multilateral trade liberalization.*

The EC's reciprocity policy makes market access and national treatment in the single market conditional on the treatment of EC firms in the United States. In each area where a 1992 directive contains a reciprocity provision, there is a potential risk that U.S. firms will not benefit from unconditional national treatment and will not be able to compete on an equal and nondiscriminatory basis.

Rules of Origin and Local-Content Requirements

- *The related issues of EC rules of origin and local-content requirements have frequently been cited as having a significant negative impact on U.S. manufacturers and exporters.*

While these measures are not the sole subject of directives involved in the integration process – and according to EC officials, will not be used to restrict trade and investment after 1992 – they are of great importance to non-EC countries and their firms.

- *The proposed Common Customs Code reiterates the existing EC standards for determining the origin of goods in trade, which are based on the principle of "last substantial transformation."*

No content-related criteria were included, and no changes in rules relating to antidumping/anticircumvention cases were proposed.

- *The EC agreed to the adoption of the adverse report of the GATT panel evaluating Japan's challenge to EC anticircumvention and "screwdriver plant" policies.*

The report has not yet been published, and to date the EC has given no indication that it will make significant legal changes in response to the report.

Anticipated Changes in the EC and Potential Effects on Certain U.S. Industries

Industry and Company Action and Reaction

- *Significant differences in the strategies employed by U.S. companies to prepare for an integrated European market make it difficult to offer general conclusions about the performance of a given industry in gearing up for 1992.*

In each of the three industry sectors analyzed in this report, U.S. involvement in the EC market has been largely confined to a relatively small number of U.S. companies. However, even in industries dominated by larger firms, variation exists in corporate strategy and preparedness for EC 92.

- *Small and medium-sized firms, which account for a large and growing share of U.S. output and employment, can also expect to benefit from the EC 92 process if steps are taken early to formalize a European market presence.*

Despite the existence of many size-related obstacles that have historically limited small business activity in overseas markets, the EC 1992 program appears to have prompted many smaller firms in the United States to explore new opportunities for participation in the single European market. Particularly in emerging technology sectors, many barriers to market entry for smaller U.S. firms are being lowered substantially by the single-market program. Most small U.S. firms continue to serve the EC market through direct exports, but joint ventures with European firms are gaining favor.

Automotive Sector

- *The overall impact of EC economic integration on U.S. automobile producers appears to be beneficial.*

The removal of national quotas will allow for increased competition and will likely provide U.S. automakers with the opportunity to expand sales in some of the currently more protected countries, such as Spain, Italy, France, and Portugal. Standards harmonization and one-stop regulatory approval will likely reduce costs and administrative burdens.

- *Overall, U.S. auto parts firms are relatively well positioned for the changes resulting from the EC integration.*

U.S. parts firms in the EC have a strong international focus, are technologically innovative, and have experienced the same restructuring in the United States that is now largely being replicated in the EC auto sector. The adoption of EC-wide emissions standards for autos similar to those in place in the United States is expected to stimulate demand for parts, such as catalytic converters, in which the United States is highly competitive. However, the increasing competitiveness of the EC market for parts and U.S. industry concerns regarding the harmonization of parts standards may serve to limit U.S. exports of auto parts to the EC.

Telecommunications Sector

- *Overall, the impact of EC economic integration on the U.S. telecommunications industry appears to be beneficial. Standards will be one of the key areas where integration can improve U.S. access to the EC market.*

In the area of standards, the harmonization of type-approval for terminal equipment is expected to reduce the costs U.S. firms incur in marketing their products in the EC. Similarly, with harmonization of the conditions of usage, tariff principles, and network interfaces, the Open Network Provision (ONP) directive is expected to aid in the development and provision of transfrontier telecommunication services.

- *The opening up of public procurement is expected to benefit U.S. firms.*

For example, about \$5 billion of the approximately \$8 billion in telecommunications equipment purchased in West Germany in 1989 was purchased by the Bundespost, West Germany's telecommunications authority. Similar procurement levels exist for other member states.

Chemicals and Pharmaceuticals Sector

- *U.S. chemical companies with investments in the EC market, either by affiliations, subsidiaries, or joint ventures, will probably greatly benefit from the EC 1992 program over the long term.*

Although no change is expected in the overall structure of the U.S. chemical industry's presence in the EC, it is expected that there will be an increase in both the number of U.S. firms involved in the EC and in the size of the average U.S. investment in the EC chemical industry. Nevertheless, most U.S. firms currently active in the EC foresee that entering the EC market may become more difficult as the economic unification progresses, primarily because of the increased attractiveness of entering the EC market and the corresponding increased level of competition that would result.

- *Continuing pharmaceutical industrywide restructuring and an increasing number of joint ventures are expected as a result of increasing R&D costs, the need to continue innovation in expectation of growth in the generic market, and the continued internationalization of the industry.*

The industry has undergone a significant amount of restructuring in recent years and such activity is continuing, although not necessarily driven by EC 92. It has been suggested that the industry could eventually be dominated by a small number of larger multinational R&D-based companies. These companies would reportedly be better placed to fund development of innovative products and, because of their multinational nature, to secure

better access to local markets. Currently, the industry shares its domestic market with U.S. subsidiaries of foreign firms and has developed facilities in foreign markets in an effort to overcome any barriers related to transportation, regulations, or import restrictions.

- *Although generally positive about the EC 92 process, pharmaceutical industry representatives have identified certain aspects of the process that are of concern to them.*

Two issues important to the industry that are still under consideration in the 1992 process are the existence of disparate national pricing/reimbursement systems and the creation of a single-market authorization procedure for pharmaceuticals. Both effectively impact the EC and the U.S. industry and are, to some degree, interrelated, since, according to industry sources, a free market and free circulation need free pricing. Other issues identified as particularly important to the industry include patent-term restoration and new guidelines on the granting of duty suspensions for certain EC imports. The industry is also watching developments in regard to the directive on advertising.

PART I
INTRODUCTION AND BACKGROUND

CHAPTER 1
INTRODUCTION TO THE EUROPE 1992 PROGRAM

CONTENTS

	<i>Page</i>
Developments covered in the previous reports	1-3
Background and outlook for EC 1992	1-3
Implementation	1-3
Developments since the first followup report	1-4
Introduction	1-4
Political union	1-4
Other institutional changes	1-5
Disagreements between the institutions	1-5
Implementation	1-7
The status of implementation	1-7
Implementation in individual member states	1-9
United Kingdom	1-10
Spain	1-11
West Germany	1-12
France	1-12
External Relations	1-13
Central and Eastern Europe and the U.S.S.R.	1-13
Status of trade and economic cooperation agreements	1-13
German reunification	1-14
Aid to central and Eastern Europe	1-14
Future relationship	1-15
Relationship to EC 92	1-15
Patterns of trade and investment	1-16
EFTA	1-18
Japan	1-19
Schengen countries	1-20
 Figure	
1-1. Breakdown of implementation by member state.	1-9

CHAPTER 1

INTRODUCTION TO THE EUROPE 1992 PROGRAM

The EC has embarked on an ambitious program designed to stimulate growth and international competitiveness through further integration of the EC's internal market. This integration program is scheduled for completion by yearend 1992.

Developments Covered in the Previous Reports

Background and Outlook for EC 1992

The EC plan to create a single internal market was envisaged over 30 years ago in the EC founding charter, the Treaty of Rome, signed in 1957. The Treaty of Rome established a customs union and required member states to eliminate intra-Community quantitative restrictions and all measures having an equivalent effect. The actions called for in the Treaty of Rome as originally adopted had been largely implemented by the mid-1960s. Over the next 20 years Community membership doubled but few additional internal barriers were eliminated. Stagnating growth, high unemployment, and increased import competition raised domestic pressures for protectionist measures and reduced the momentum towards further integration among the member states. Not until the early 1980s did "Eurosclerosis," reduced European competitiveness, and the increasing ineffectiveness of the EC institutions prompt member-state governments to seek greater cooperation among themselves.

In June 1985, the EC Commission issued a White Paper entitled "Completing the Internal Market" that outlined a detailed plan to remove all obstacles to the free movement of goods, people, services, and capital by December 31, 1992. EC leaders recognize that not all sensitive issues are likely to be resolved by 1992 and that a barrier-free Europe by that date is unlikely. Certain measures—such as those in the area of tax harmonization—have prompted strong member-state resistance.

Progress on the EC single-market program and the development of EC relations with third countries have become inextricably linked. The rapid changes in Eastern Europe and German reunification have encouraged efforts to "deepen" the EC 1992 process by intensifying cooperation among the existing 12 EC member states in all spheres—political, social, monetary, and defense, as well as economic. Some non-EC European nations are seeking membership in the Community in order to take full advantage of the benefits of the internal market. The six European Free Trade Association (EFTA) nations, concerned that their special relationship with the EC is being challenged,

agreed with EC leaders in December 1989 to begin formal negotiations. These negotiations aim to create a European Economic Space and to realize the free movement of goods, services, people, and capital between the two blocs. Further, the recent renegotiation of the Lome Convention with developing countries guarantees that these countries will continue to receive the same or expanded preferential access to the EC market after 1992. Finally, the EC Commission argues that the external effects of integration will be positive. However, some third countries—including the United States—are concerned that increased competition among the 12 member states could induce certain sectors of EC industry to seek protection against imports, thus forming a "Fortress Europe."

Implementation

Under the French presidency of the EC Council of Ministers during the second half of 1989, the EC made substantial progress toward passing the legislation needed to effect 1992 integration. As set out in the White Paper, 279 internal market measures will form the integration program. Of these, the EC Commission had tabled (formally proposed) 261 as of January 1, 1990. Also as of that date, the EC Council had formally adopted 142 of these measures, or about 60 percent of the program. Within the EC Council, the presidency changed hands according to treaty provisions, with Ireland assuming the chair for the first half of 1990. Within the EC's judiciary, the Court of First Instance of the European Communities, newly created to take some of an increasing caseload from the Court of Justice, held its first plenary session in December 1989.

As the EC Commission, Parliament, and Council complete more and more of their work on single-market measures, implementation of those measures by EC member states assumes greater and greater importance. Some internal market measures are recommendations and decisions, which take effect immediately upon their issuance in all member states, but the vast majority of measures are directives, which take effect only upon their transposition into member-state law. However, as of January 17, 1990, only 14 of the 86 single market directives that should have already been transposed into national law had been fully transposed by all member states.

The EC Commission is the agency responsible under the Treaty of Rome for ensuring that directives are implemented by the EC member states, and it is attempting to enforce the implementation requirement. Both the European Parliament and the EC Council of Ministers have also recognized the importance of increasing the pace of implementation and have determined to increase their role in promoting implementation.

Technical standards form a special case, in that the EC Commission works closely with private European standards bodies to produce European

standards. Although the EC Commission drafts mandatory technical requirements in its standards directives, it issues mandates to the private bodies to issue voluntary standards.

Although Italy is one of the most strongly pro-EC member states, it has the worst implementation record. Slow implementation in Italy is a problem both of inefficient administration and of parliamentary delay. Problems remain, although the Italian Government has recently taken significant steps to cure its noncompliance with EC law, notably by passing the so-called "La Pergola" law to streamline implementation. Greece has been hampered in implementation by frequent changes of Government as well as bureaucratic inefficiency. Certain member states have devolved considerable power on autonomous states, provinces, or regions. This situation raises the possibility of implementation by some regions and not by others. Although West Germany appears to deal relatively well with decentralized implementation, Belgium has encountered problems. Spain faces both the problems of decentralization and of catching up with other member states in implementing measures issued prior to Spain's entry into the EC.

Developments Since the First Followup Report

Introduction

Under the Irish presidency of the EC Council of Ministers during the first half of 1990, the EC continued to pass the legislation needed to effectuate the 1992 integration program. As set out in the White Paper, 279 internal market measures were to form the integration program. The EC Commission had transmitted to the EC Council proposals covering all of those measures, as well as supplementary proposals,¹ as of July 18, 1990.² As of that date, the EC Council had formally adopted 164 of the measures.³ The EC Council issued 20 internal market measures during the 6 months of the Irish presidency, and has estimated that two-thirds of the 1992 measures have been passed.⁴

On April 6, 1990, the EC Commission noted that 1,000 days remained until the program deadline of January 1, 1993.⁵ The EC is confident that the

¹ Such additional measures raised the total to 282. EC Commission, "Fifth Report of the Commission to the Council and the European Parliament concerning the Implementation of the White Paper on the Completion of the Internal Market," Com (90) 90, Mar. 28, 1990, p. 6.

² *Ibid.*; EC Commission data base Info92, July 25, 1990.

³ EC Commission data base Info92, July 25, 1990. The Council had as of July 18, 1990, also partially adopted five measures, and reached common positions on nine more. *Ibid.*

⁴ The EC summit in Dublin on June 25 to 26, 1990, noted the need to accelerate progress on stockbroking, insurance, and corporate take-overs; road transport; taxes; and health and safety standards. *Common Market Report*, Commerce Clearing House (CCH), July 5, 1990, p. 1; *European Report* No. 1598 (June 27, 1990), Document p. 2.

⁵ Boodle Hatfield, C&M International Ltd., and Crowell and Moring, *EC-US Business Report*, May 1, 1990, p. 4.

integration program is irreversible and will be virtually completed by the deadline, although some small measures will still remain to be done. Currently, some "quite controversial" issues are still outstanding, notably the treatment of taxes, which is politically sensitive, free circulation of persons, and the fate of Japanese automobile imports into the EC.⁶ The EC Commission is pressing the Council to maintain its current adoption rate of one directive per week.⁷

Within the EC Council, the presidency changed hands according to treaty provisions, with Italy succeeding Ireland to the chair for the second half of 1990, effective as of July 1, 1990. Luxembourg will assume the presidency at the beginning of 1991.⁸ Jacques Delors was confirmed as EC Commission President for another 2 years.⁹

Political Union

The EC institutions are moving toward a possible major restructuring within the framework of the planned political union of the EC. In April 1990, French President Francois Mitterand and West German Chancellor Helmut Kohl jointly called for political union to be placed on the agenda of EC summits; however, British Prime Minister Margaret Thatcher termed the move premature, and EC Commission President Jacques Delors urged caution in the move toward political union, stating that the political discussion should not cut across progress toward monetary union.¹⁰

On May 17, 1990, representatives of the EC Commission, the Council, and the Parliament met to coordinate plans for an intergovernmental conference on political union scheduled for the end of 1990. At their summit in Dublin on June 25-26, 1990, the EC Heads of State and Government confirmed that the conference would begin on December 14, 1990, in Rome.¹¹ The conference aims to issue proposed amendments to the Treaty of Rome by the end of 1991, but no blueprint for the restructuring has yet been agreed on.¹² Belgium proposed that the EC should increase the number of decisions, notably those involving social policy, tax, and the environment, to be governed by the Single European Act cooperation procedure that provides for majority rather than unanimous decisionmaking in the Council of Ministers.¹³ Belgium also

⁶ Ambassador Andreas van Agt, Head of the EC Mission to the United States, address to "1992 in Europe, A Practical and Legal Guide to Doing Business in the Single European Market," American Bar Association-EC conference, New York, June 7, 1990 (ABA-EC conference, "1992 in Europe").

⁷ *EC-US Business Report*, May 1, 1990, p. 4.

⁸ *Common Market Reporter* (CCH), July 5, 1990, p. 8.

⁹ *European Report*, No. 1598 (June 27, 1990), Document p. 10.

¹⁰ *Financial Times*, Apr. 27, 1990, p. 1.

¹¹ *Common Market Reporter* (CCH), July 5, 1990, p. 1; *European Report* No. 1598 (June 27, 1990), Document p. 1.

¹² Ambassador Andreas van Agt address to ABA-EC conference, "1992 in Europe," June 7, 1990; *European Report*, No. 1588 (May 19, 1990), Institutions and Policy Coordination, p. 2.

¹³ Italy also favors this change. *Financial Times*, May 16, 1990.

proposed that Parliament be given more authority in decisionmaking and the power to elect EC Commission presidents, that the Court of Justice's authority be strengthened, and that the EC coordinate security policy.¹⁴

The EC Commission also has considered and rejected a suggestion that Parliament be split into two houses; opposes, as does Parliament, an increase in the decisionmaking powers of the Council; and seeks greater executive powers for itself, such as the right of initiative in political cooperation matters.¹⁵ Although some had predicted that foreign policy and security measures would be brought within the EC's sphere of competence, the Council does not seem to contemplate such an extension of EC authority.¹⁶

Although the EC appears to be moving toward increasing the authority of its institutions over the member states, the EC remains committed to the principle of "subsidiarity." EC Commission President Jacques Delors endorsed the definition of that principle as indicating that "European union assumes only the tasks that it can perform more efficiently than the Member States acting on their own, or that are vital to European Union."¹⁷ President of Parliament Enrique Baron Crespo recognized that national parliaments must continue to play an important role in the EC, but pointed to the need for action at the Community level in such matters as dealing with pollution of the Rhine, the North Sea, and the Moselle.

Other Institutional Changes

The EC Commission seeks to increase its authority by becoming the executive body for the Economic and Monetary Union (EMU), implying a reduction of the powers of the Council of finance ministers. Although the EMU is not strictly a part of the 1992 program, the EMU will consolidate the work of integration, and is a highly delicate operation because it involves transfer of a significant amount of sovereignty from member states to the EC.¹⁸ The EC Commission also seeks to draw Parliament further into the functioning of the EMU by having Parliament monitor member-state compliance. The other principal institution of the EMU would be the European System of Central Banks, popularly styled Eurofed, an independent central bank. Eurofed would comprise 16 members, including the governors of the member states' central banks, and a four-person directory. The body's responsibilities would include the formulation of common monetary policy, the issuance of Ecus (European currency units), and the coordination of banking surveillance.¹⁹

¹⁴ *Financial Times*, Apr. 28, 1990.

¹⁵ *Ibid.* pp. 3, 5.

¹⁶ *Common Market Reporter* (CCH), May 24, 1990, p. 7.

¹⁷ *European Report*, No. 1572 (Mar. 17, 1990), Institutions and Policy Coordination, p. 2.

¹⁸ Ambassador Andreas Van Agt, address to ABA-EC conference, "Europe 1992," June 7, 1990.

¹⁹ *Ibid.* Economic and Monetary Affairs, pp. 2-3.

The EC's institutions have engaged in a long debate about the functions of the planned European Environment Agency. On May 7, 1990, the Council of foreign ministers approved setting up the agency.²⁰ Although the Council rejected Parliament's call for a grant of inspection and control powers to the agency, Parliament has threatened to block funding for the agency if its wishes are not respected.²¹ There is also disagreement over where to put the headquarters of the agency. Various sites have been suggested, including Brussels, Berlin, Strasbourg, and Karlsruhe.²²

The EC also plans to set up a European Medicines Agency, a centralized body for reviewing the safety of medicines,²³ and a European Organization for Standards and Testing (EOTC).²⁴

Parliament appears to have resolved, at least temporarily, its internal debate over the seat of its operations. Although Strasbourg—the traditional headquarters of Parliament—and Brussels had each hoped to play host to all Parliament sessions, Parliament has decided to hold all 12 of its ordinary annual plenary sessions in Strasbourg, and any extraordinary sittings in Brussels. In addition, Parliament will retain certain offices in Luxembourg.²⁵

German reunification might have led to a debate over whether to change the structure of the EC institutions had not West Germany moved to scotch any dispute. The West German Government assured the EC that a united Germany would not seek greater representation in the European Parliament, the EC Commission, or the Council of Ministers in spite of the growth in population resulting from reunification.²⁶

Disagreements Between the Institutions

EC Commission President Delors recently acknowledged that the relationship between the EC Commission and Parliament has grown strained. In an address to Parliament, he suggested that a "code of conduct" be set up to govern Parliament-Commission relations, under which the EC Commission would improve its procedures for

²⁰ Council Regulation (EEC) 1210/90 of May 7, 1990, *Official Journal of the European Communities* (OJ) No. L 120 (May 11, 1990), p. 1.

²¹ *European Report*, No. 1586 (May 12, 1990), Internal Market, p. 13.

²² *European Report*, No. 1566 (Feb. 24, 1990), Document, pp. 9-10. Copenhagen has also been suggested, in order to reward Denmark's advanced level of environmental protection, as has Madrid, to encourage Spain to increase its own level of protection. *European Report* (Apr. 4, 1990), Internal Market, p. 5.

²³ *Financial Times*, May 21, 1990.

²⁴ The latter organization should be in place by the end of 1990. EC Commission, "Fifth Report," Com (90) 90, p. 17.

²⁵ *European Report*, No. 1583 (May 3, 1990), Document p. 14.

²⁶ Irmgard Adam-Schwaetzer, West German Deputy Foreign Minister, interviewed in *Europe*, No. 296 (May 1990), p. 30. West Germany currently has 81 members in Parliament, 2 seats on the EC Commission, and 10 votes in the Council of Ministers. *Ibid.*

informing Parliament of Council decisions, consulting Parliament on the choice of legal bases for new initiatives, and explaining disagreements with Parliament amendments to EC Commission proposals. In return, he requested that Parliament speed up its issuance of opinions.²⁷

One particular source of controversy has been the EC Commission's use of article 90 of the Treaty of Rome. Article 100A of that treaty, as amended by the Single European Act, provides that the EC will issue most directives designed to effectuate the 1992 integration process according to a cooperation procedure that gives each of the three principal EC institutions, i.e., the EC Council of Ministers, the EC Commission, and the European Parliament, a role in decisionmaking. However, the EC Commission has recently engendered controversy by issuing directives on its own without reference to the other institutions. The EC Commission based its actions on authority granted by article 90 of the Treaty of Rome. Article 90 applies the treaty's rules on competition²⁸ to public undertakings, i.e., business entities run by member-state governments and undertakings that are granted special or exclusive rights. The article also empowers the EC Commission to issue directives and decisions to EC member states to enforce those rules.²⁹ By issuing directives itself under article 90 rather than proposing directives to the Council and Parliament under article 100A, the EC Commission avoids the more complicated cooperation procedure and may prompt the other institutions and the EC member states to suspect that the EC Commission is claiming more power for itself than is appropriate.

The dispute over the EC Commission's use of article 90 surfaced most recently when the EC Commission issued under article 90 a directive on May 16, 1988, requiring the liberalization of the telecommunications terminals market.³⁰ On July 22, 1988, France challenged the validity of the directive in a suit before the Court of Justice of the European Communities.³¹ France argues that the EC Commission exceeded its authority under article 90 in issuing a directive that is allegedly overbroad and that concerns an area that is so politically charged that the EC Commission should not have issued such a directive on its own.³²

²⁷ *European Report*, No. 1566 (Feb. 24, 1990) Document p. 4; *Europe*, Feb. 15, 1990, p. 13.

²⁸ The rules are contained in arts. 85-102 of the EEC Treaty. Art. 90 also imposes on public undertakings the prohibition set out in art. 7 against discrimination on the grounds of nationality.

²⁹ EEC Treaty, art. 90(3).

³⁰ Commission Directive on Competition in the Markets in Telecommunications Terminal Equipment, May 16, 1988, *OJ* No. L 131, p. 73.

³¹ *France v. EC Commission*, Case 202/88, 31 *OJ* No. C 216 (1988), p. 6.

³² J. Falvey, "France v. the Commission of the European Economic Community: the Power of the Commission to Issue a Directive Under Article 90," *Virginia Journal of International Law*, vol. 3, p. 937.

The Court of Justice has in the past upheld the power of the EC Commission to issue directives under article 90.³³ Nevertheless, the EC Commission's use of its authority in this case has caused concern within the EC. Even before the directive was issued, the ministers of France, the United Kingdom, and West Germany expressed displeasure with the EC Commission's directive at a Council of Ministers meeting on April 28, 1988. The ministers were concerned that the EC Commission was extending its authority too far and infringing on the powers retained by member states. They suggested that the EC Commission proceed under the cooperation procedure established by article 100A, which gives a role in decisionmaking to the Council and the European Parliament as well as to the EC Commission.³⁴ The Governments of Belgium, Greece, West Germany, and Italy have expressed support for France's suit, and Spain has threatened to bring an action on its own.³⁵ On January 18, 1990, Parliament discussed the telecommunications undertakings directive and opined that the cooperation procedure "is a more appropriate legal basis for adopting directives relating to such enterprises." Parliament also called on the EC Commission to afford Parliament the opportunity to deliver an opinion before the Commission takes action under article 90.³⁶

The Court of Justice has not yet issued its opinion.³⁷ However, whether it upholds the EC Commission's action in this case or not, the Court's legal judgment may not end the political debate over how power is to be shared among the EC's institutions.³⁸

The remainder of chapter 1 is devoted to two issues of importance to EC integration. First, the fact that the vast majority of integration measures being issued by the EC are directives that member states need to implement by transposition into national law is bringing the issue of implementation into increasing prominence. Second, the question of how the EC conducts its external relations has assumed great importance in view of the significant changes occurring in the world.

³³ *Re Public Undertakings*, 1982 E. Comm. Ct. J. Rep. 2545, [1982] *Common Market Law Report*, vol. 3, p. 144.

³⁴ J. Falvey "France v. the Commission", p. 937. See also R. Wainwright, "Public Undertakings Under Article 90," 1992 and *EEC/U.S. Competition and Trade Law*, Fordham Corporate Law Institute (Oct. 26-27, 1989).

³⁵ *Europe*, Feb. 15, 1990, p. 14; *European Report*, No. 1599 (June 30, 1990), Business Brief, p. 8.

³⁶ European Parliament Document A3-08/89, a resolution on the 18th report of the EC Commission on competition policy, *OJ* No. C 38/109 (Feb. 19, 1990).

³⁷ 1992 - *The External Impact of European Unification*, vol. 2, No. 6 (June 15, 1990), p. 9. On Feb. 14, 1990, Advocate General G. Tesouro issued an opinion supporting France. *Europe*, Feb. 15, 1990, p. 14.

³⁸ In a similar vein, the Court ruled on May 22, 1990, that the European Parliament is permitted to bring suit to challenge the legal basis for a Council measure. *European Parliament v. EC Council*, Case No. 70/88. In that case, Parliament argued that the Council should have acted under art. 100A of the EEC Treaty rather than art. 31 of the Euratom Treaty to pass a regulation on levels of radioactive contamination of foodstuffs and animal feed. *Common Market Reporter* (CCH), June 7, 1990, p. 1.

Implementation

As the EC Commission, Parliament, and Council complete more and more of their work on single market measures, the issue of implementation of those measures by EC member states assumes greater and greater importance. Some internal market measures are regulations and decisions, which take effect immediately upon their issuance in all member states, but the vast majority of measures are directives, which take effect only upon their transposition into member-state law.³⁹

The Status of Implementation

As of July 13, 1990, only 19 of the 108⁴⁰ single-market directives that should have already been transposed into national law had been fully transposed by all member states.⁴¹ The EC considers that there has been "insufficient" implementation in some member states, and expects that member states will accelerate their implementation efforts.⁴² At the Dublin summit on June 25-26, 1990, the Council stressed the importance of timely implementation, and urged the EC Commission to increase its supervisory procedures.⁴³

The EC Commission, the agency responsible under the Treaty of Rome for ensuring that directives are implemented by the EC's member states, considers 1990 to be a pivotal year in that the emphasis must shift from the creation by the EC of the framework for integration to the enforcement of EC rules against noncomplying member states.⁴⁴ The framework cannot lead to integration in practice without member state compliance, and "[t]oo often in the past, good EC law on paper has had less effect in practice."⁴⁵

According to the EC Commission's March 28, 1990, report, implementation of plant and animal health controls measures at that time left much to be

³⁹ Terminology in this area is sometimes confusing. The term "implementation of a directive" is used in this section and elsewhere as a synonym for the process by which member states transpose, or translate, EC directives into their national law. However, on occasion "implementation" is used to mean the carrying out, usually by the EC Commission, of directives issued by the EC Council, often involving the issuance by the EC Commission of directives of its own. EC Council directives are often couched in general terms, necessitating the issuance by the EC Commission of more specifically worded measures. See, e.g., EC Commission, "Fifth Report," Com (90) 90, p. 18.

⁴⁰ This number is less than the total of directives issued because most directives provide a period of time between issuance and the deadline for implementation.

⁴¹ U.S. Department of State Telegram, July 19, 1990, Brussels, Message Reference No. 11035, p. 1; EC Commission, "Fifth Report," Com (90) 90, p. 4.

⁴² Ambassador Andreas van Agt, address to ABA-EC conference, "Europe 1992," June 7, 1990.

⁴³ *European Report*, No. 1598 (June 27, 1990), Document, p. 3.

⁴⁴ *EC-US Business Report*, Apr. 1, 1990, p. 3.

⁴⁵ Peter Allgeier, Assistant United States Trade Representative for Europe and the Mediterranean, testimony before the House Foreign Affairs Committee Subcommittee on International Economic Policy and Trade and Subcommittee on Europe and the Middle East, Feb. 20, 1990, "EC 1992: An Update on U.S. Views," p. 10.

desired.⁴⁶ The EC Commission's report also stated that member states had failed in their obligations with respect to technical harmonization, as evidenced by the fact that only two member states had transposed the toy directive into national law.⁴⁷ With respect to foodstuffs, some measures remained unimplemented by any member state, and France, Portugal, and Ireland were the most dilatory, according to the EC Commission's report.⁴⁸ Pharmaceuticals measures had been implemented by all member states except Spain, Italy, Ireland, and Portugal. Most chemicals directives had been satisfactorily transposed, according to the EC Commission,⁴⁹ and implementation of measures on customs and tax formalities, motor vehicles and tractors, had been satisfactory.⁵⁰ In the area of public procurement, the EC Commission stated that all member states except Italy and the Netherlands had transposed the public supplies directive into national law.⁵¹ Belgium, West Germany, Italy, and the Netherlands were behind schedule with respect to the two directives on securities transactions. Except for Italy, all eight of the affected member states had taken significant steps toward implementing the measures on the liberalization of capital movements. Finally, the report noted that the European Economic Interest Grouping had been introduced in all member states except Spain, Greece, Italy, Luxembourg, and Portugal. All member states but Greece had transposed into national law the two extant measures on intellectual property.⁵²

The EC Commission has stepped up its monitoring efforts. Whereas previously the EC Commission only required that member states notify it of implementing measures, now member states must also provide a detailed table showing when and how each provision of EC law is transposed into national law.⁵³

⁴⁶ Thirty percent of implementing measures remain to be taken, with Portugal having fallen behind on more than half of the directives. EC Commission, "Fifth Report," Com (90) 90, p. 12.

⁴⁷ The toy safety directive is the first such measure to have reached its implementation deadline. Consequently, member-state performance with respect to that measure is seen as an indication of how they will do with subsequent enactments, such as the measure on pressure vessels. EC Commission, "Fifth Report," Com (90) 90. Since the report's issuance, the number of implementing states has risen to five, consisting of Denmark, Greece, France, Portugal, and the United Kingdom. EC Commission data base Info92, July 25, 1990.

⁴⁸ *Ibid.*, pp. 17 and 18. This poor showing on foodstuffs has led the EC Commission to call for an investigation by the EC Commission's Advisory Committee on Foodstuffs. *Ibid.*, p. 18.

⁴⁹ The liquid-fertilizer directive had been transposed only by West Germany and Denmark, and eight member states had failed to implement the measure on good laboratory practices. *Ibid.*, p. 19.

⁵⁰ Greece and to a lesser extent Belgium are behind schedule with respect to emission standards. *Ibid.*

⁵¹ The EC Commission warned that transposition must be followed by continued compliance with the rules, such as the proper use of tender notices, and noted that four cases of noncompliance have already been referred to the Court of Justice. *Ibid.*, p. 20.

⁵² *Ibid.*, pp. 24 and 25.

⁵³ Martin Donnelly, Advisor to EC Commissioner Brittan, address to ABA EC conference, "1992 in Europe," June 7, 1990.

When a member state fails to implement a directive, the EC Commission can take the member state to court under article 169 of the Treaty of Rome. This right of action is an important tool in the EC Commission's effort to achieve full implementation, although the Court of Justice has no power to enforce a judgment against a member state. On more than one occasion, the Court has issued a judgment that a member state had violated its treaty obligations by failing to transpose a directive, then had to issue a second judgment holding that the violation of treaty obligations was now double, based both on the failure to transpose and the failure to obey the first judgment. This suggests that suing a member state under article 169 is a useless endeavor. However, once a member state has been found in violation of treaty rules, the other member states bring political pressure to bear to encourage obedience to the treaty, and the noncomplying state eventually implements the directive. Thus, although the Court of Justice has several times had to issue a second judgment to a member state in a single case, instances of a third judgment have been very rare.⁵⁴

As of December 1989, the EC Commission was conducting 60 infringement proceedings against member states for failure to implement directives.⁵⁵ The increasing number of article 169 infringement actions is straining the ability of the Court to issue prompt decisions. This suggests to some that member states are deliberately using the fact that infringement procedures are lengthy to delay the effect of EC measures they do not agree with.⁵⁶ According to the EC Commission, however, most failures to implement are due to administrative difficulties, political interests, and economic problems.⁵⁷ Nevertheless, the European Parliament has warned that some member states have attempted "rearguard actions" to modify the thrust of a directive by incorrect transposition into national law.⁵⁸

⁵⁴ Sir Gordon Slynn, Judge, European Court of Justice, address to ABA EC conference, "1992 in Europe," June 8, 1990.

⁵⁵ *Ibid.*, p. 4. The EC Commission delivered to member states in 1989 242 warning letters and 76 reasoned opinions concerning member-state noncompliance, and the Court of Justice issued 44 opinions on the subject. *European Report*, No. 1562 (Feb. 10, 1990), Internal Market, p. 5.

⁵⁶ *Financial Times*, June 6, 1990, p. 18.

⁵⁷ For example, in the case of directives relating to the mutual recognition of diplomas, the EC Commission stated that the delay in implementation "appears in general . . . due to the lengthy nature of the legislative procedures involved." EC Commissioner Martin Bangemann, answer to written question No. 832/89 by Francois de Donnea, *OJ* No. C 125 (May 21, 1990), p. 17.

⁵⁸ European Parliament Directorate-General for Research, Fact Sheet on the European Parliament and the Activities of the European Community, En III/D/10, p. 2. Pressure to block implementation of a controversial measure can also come from outside a member state. In the case of the broadcasting directive that sets guidelines for minimum EC content, the United States has urged member states on a bilateral basis not to implement the guidelines. Peter Allgeier, Assistant United States Trade Representative for Europe and the Mediterranean, testimony before the House Foreign Affairs Committee Subcommittee on International Economic Policy and Trade and Subcommittee on Europe and the Middle East, Feb. 20, 1990, "EC 1992: An Update on U.S. Views," p. 10.

The EC Commission seeks to improve implementation by a variety of means. The EC Commission has warned that funding may be withheld for member-state projects that are not in line with the public procurement directives and the goal of abolishing border controls.⁵⁹ EC Commissioner Carlo Ripa di Meana, who is responsible for environmental matters, has complained about the low level of member state compliance with EC environmental measures, and has suggested that the EC Commission should also consider withholding EC funding for environmental projects as a lever to force implementation.⁶⁰

EC Commission Vice President Martin Bangemann, who is in charge of internal market matters, warned member states that failure to transpose a directive into national law does not preclude the directive from having effect. Where a directive leaves a member state little room for maneuver, as in technical harmonization, companies and individuals can directly invoke the targets set by the directive even if a member state has failed to timely transpose the directive.⁶¹ Indeed, the EC Commission encourages private parties to bring actions in national courts for member state noncompliance with EC measures, in order to speed implementation and relieve some of the backlog of cases before the European Court of Justice.⁶²

The EC Commission intends to rely more on public opinion to speed implementation both by keeping Parliament informed of infringement actions and by encouraging a wider knowledge of EC law.⁶³ The EC Commission has undertaken to provide public access to "precise details of all national transposition measures" in its public databank Info 92.⁶⁴ That data base, which began working on January 1, 1990, lists the national laws that transpose EC directives by title, number, and date of publication, although it does not contain the actual text of the laws.⁶⁵ The EC Council has

⁵⁹ EC Commission, "Fifth Report," *Com* (90) 90, p. 10.

⁶⁰ *European Report*, No. 1562 (Feb. 10, 1990), Internal Market, p. 5.

⁶¹ Martin Bangemann, EC Commission Vice-President, *Target 1992*, EC Commission newsletter on the single internal market, February 1990, p. 2.

⁶² *EC-US Business Report*, Apr. 1, 1990, p. 3. In a recent example of successful private action, six women forced to retire by a British public utility obtained a ruling that the British Government had violated an EC anti-sex-discrimination directive, even though the Government had never transposed the directive into British law. *Financial Times*, July 13, 1990, p. 22.

⁶³ U.S. Department of State Telegram Mar. 5, 1990, Message Reference No. 03499, p. 2.

⁶⁴ EC Commission, "Application of Instruments for Completing the Internal Market," *Sec* (89) 2098, Dec. 4, 1989, p. 4.

⁶⁵ EC Commission, "Implementation of the Legal Acts Required to Build the Single Market," *Com* (89) 422, Sept. 7, 1989, p. 11; EC Commission official, interview by USITC staff, Brussels, Jan. 10, 1990.

expressed satisfaction that Info 92 is online.⁶⁶ However, examination of Info 92 reveals that the databank has been far from complete, with implementation data on only some of the directives.⁶⁷

Implementation in Individual Member States

The status and pace of implementation varies widely from member state to member state. Figure 1-1 shows the status of implementation in each member state. Member states such as the United Kingdom generally implement rapidly, whereas Spain, Portugal, and Greece continue to obtain derogations that permit delay in implementation, with some deadlines pushed back as far as 1997.⁶⁸

⁶⁶ *Europe*, No. 5160 (new series), Dec. 23, 1989, p. 1.

⁶⁷ Evaluation based on USITC staff use of Info 92, May to July, 1990.

⁶⁸ *Europe Report*, No. 1581 (Apr. 25, 1990), supplement, p. 1.

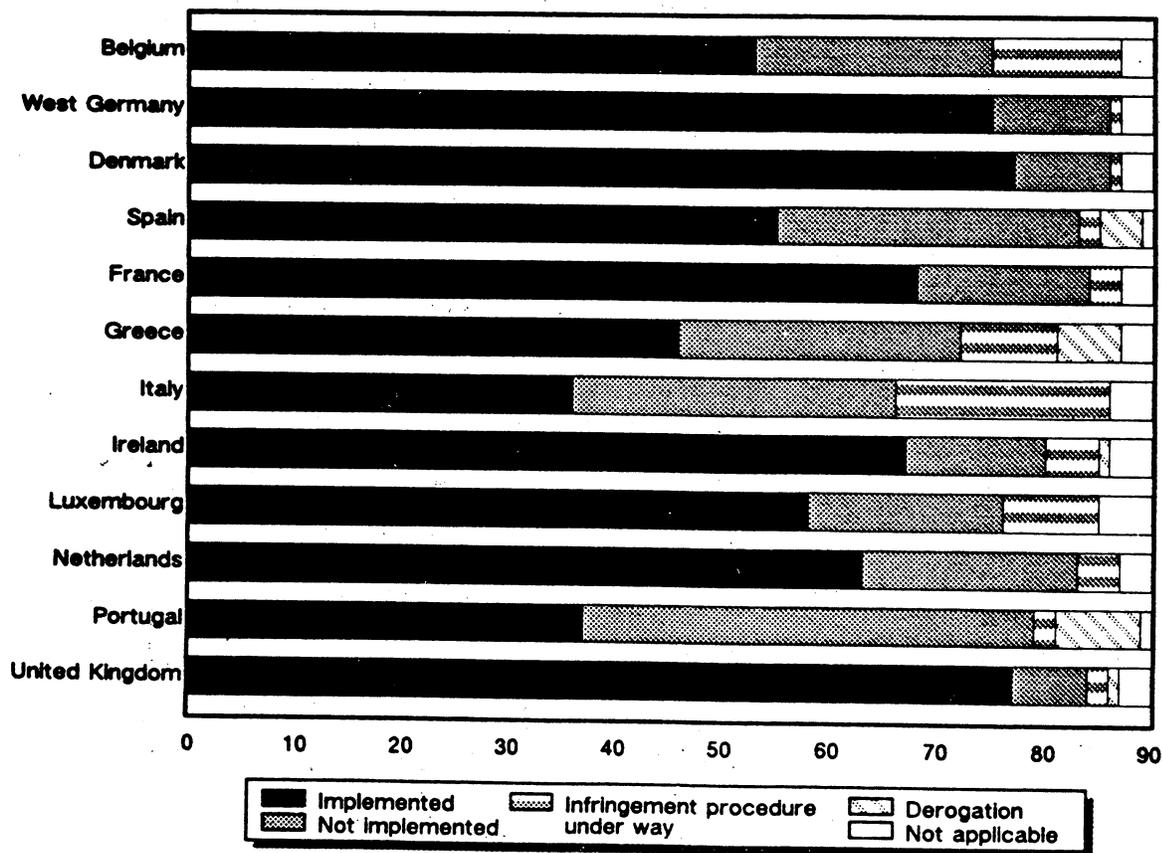
Ireland will not fully implement the EC nonlife insurance directive until the late 1990s.⁶⁹ Methods of implementation also vary among member states. For example, France has on occasion come into conflict with the EC Commission by implementing a directive using an interpretation of the text that the EC Commission does not share.⁷⁰ The Irish Parliament tends to transpose EC directives rather more directly, by issuing a law the text of which is identical to that of the directive with references to the "EC" crossed out and replaced with "Ireland."⁷¹

⁶⁹ *Financial Times*, Feb. 19, 1990.

⁷⁰ One example concerned the directive on the protection of birds. Official of French Secretariat of State for the Environment, interview by USITC staff, Neuilly-sur-Seine, June 8, 1990.

⁷¹ The European Parliament has expressed approval of this method. Staff of Chairman, European Parliament Environmental Committee, interview by USITC staff, June 4, 1990.

Figure 1-1
Breakdown of implementation by member state



Source: EC Commission, *Fifth Report of the Commission to the Council and the European Parliament Concerning the Implementation of the White Paper on the Completion of the Internal Market*, Mar. 28, 1990, Com (90)90.

U.S. firms have on occasion encountered difficulties due to unequal implementation among member states. For example, U.S. toys have been blocked at the Italian and French borders because Italian and French customs officials have refused to recognize certifications of conformity to standards issued by other member states, arguably in violation of the toy directive.⁷² In France, officials also require documentation to be in French, but only for products originating outside the EC.⁷³ The EC Commission has asked France to clarify its position and has warned that French procedures may be in violation of the directive.⁷⁴

As in the past, an EC member state's success at implementation continues to show little correlation to the amount of support the state's citizens have for membership in the EC. According to a recent survey,⁷⁵ Denmark and the United Kingdom rank first in implementation of 1992 measures,⁷⁶ although they rank lowest in public enthusiasm for the EC. In contrast, Italy, Greece, and Belgium score high in public support for EC membership, yet rank low in success at implementation.⁷⁷ Italy and to

⁷² Wendell Wilkie II, General Counsel, U.S. Department of Commerce, address to ABA-EC conference, "Europe 1992," June 7, 1990. U.S. producers complain that in the United Kingdom large retailers and wholesalers are insisting that toys be certified by a third-party organization rather than accepting the producer's self-certification. This insistence leads to increased expense and delays, particularly because no recognized U.S. certification bodies exist. Apparently, the British firms fear they will lose product-liability suits because of their failure to seek third-party certification. Official of the Toy Manufacturers Institute, interview by USITC staff, July 13, 1990.

⁷³ Some affected U.S. producers are responding to this by abandoning the French market or trying to "get in the back door" through other EC countries. In the United Kingdom large retailers and wholesalers are not accepting self-certification but have rather insisted upon receipt of third-party certification from a notified body. This is not illegal, since it is not the British Government, but rather private purchasers who are doing so. However, U.S. suppliers have complained about delays and the added expense involved, particularly since there are no U.S. notified bodies (i.e., none are permitted to issue the required marks). It was because the British retailers fear lawsuits in the event a product is found unsafe if they relied upon manufacturers' assurances (manufacturers' declaration of conformity) alone. They thought such a course would open them up to claims that they had not exercised due diligence by obtaining a third-party certification of conformity. Official of the Toy Manufacturers Institute, interview by USITC staff, July 13, 1990.

⁷⁴ 1992 - *The External Impact of European Unification*, vol. 2, No. 8 (July 13, 1990), p. 3.

⁷⁵ *The Economist*, June 23, 1990, p. 48.

⁷⁶ EC Environment Commissioner Carlo Ripa di Meana has dubbed Denmark the EC's environmental "vanguard" for its top record in implementation of environmental measures, although even Denmark faces 5 infringement proceedings (compared to Spain's 57). He suggested that this record would help Copenhagen's bid to be the headquarters of the European Environmental Agency. *European Report*, No. 1562 (Feb. 10, 1990), Focus, p. 1, and Internal Market, p. 5.

⁷⁷ *The Economist*, June 23, 1990, p. 48. According to *The Economist*, the ranking of member states by implementation record is as follows, starting with the most successful and with some states tied for the same rank: Denmark and the United Kingdom, West Germany, France and Ireland, the Netherlands, Luxembourg, Spain, Belgium and Greece, Portugal, and Italy.

some extent Belgium are among the member states most frequently brought before the Court of Justice for failure to implement directives.⁷⁸

The previous USITC report focused on the implementation efforts of certain member states, i.e. Italy and Greece, because of their poor implementation record; and federal states, where decentralization can be a problem for consistent implementation.⁷⁹ In this report, we continue our survey of member state implementation by looking at the United Kingdom, Spain, West Germany, and France.

United Kingdom

In the United Kingdom, each ministry is responsible for the implementation of directives with regard to its area of competence.⁸⁰ The responsible ministry drafts implementing legislation and presents it to Parliament. To be enacted, a bill must pass through both Houses of Parliament (Commons and Lords), after hearings have been held, and is then sent back to the Commons to take into account the changes made by the Lords. The system is unlike that in the U.S. in that the Commons need not take into account the Lords' changes, as these are only "suggestions." In general, Members of Parliament vote the party line except with regard to such issues as the death penalty and abortion. In essence, the Government prevails if it has a large enough majority. The *London Gazette*, a daily publication, publishes the laws enacted by Parliament.

Although the central Government handles most aspects of implementation, some responsibilities are delegated. In particular, the British Government has traditionally placed such responsibilities as consumer protection in the hands of local authorities at the county level.⁸¹

⁷⁸ Sir Gordon Slynn, Judge, European Court of Justice, address to ABA EC conference, "1992 in Europe," June 8, 1990.

⁷⁹ USITC, *Effects of EC Integration* USITC Publication 2268, March 1990, ch. 1. In a new development concerning implementation by federal states, the Court of Justice ruled against Belgium for failure to implement several waste disposal directives in *EC Commission v. Kingdom of Belgium*, Joined Cases Nos. 227-230/85. Belgium argued that certain provisions of the directives fell within the competence of regional authorities that the Belgian Government had no power to force into implementation. The Court held against Belgium on the basis of the established rule that a member state may not plead the circumstances of its internal legal system to justify a failure to comply with treaty obligations. *Common Market Reporter* (CCH), July 5, 1990, p. 5-6.

⁸⁰ For example, the Ministry of Agriculture, Fisheries, and Food deals with the implementation of measures relating to public health and safety in those areas. Each Government ministry is composed of up to five junior ministers, who hold no cabinet rank. Each department has a permanent secretary, a deputy secretary, and undersecretaries and their equivalents. There are legal groups at the undersecretary level (under the legal advisor and solicitor), which determine if implementation is proceeding correctly. Public analyst, Lyne, Martin & Radford, interview by USITC staff, London, June 5, 1990.

⁸¹ Under the Central Government are 36 counties (Oxfordshire, Devonshire, etc.). Below the county level are districts (usually four to five within each county). Recently, metropolitan counties were abolished, with entities such as London, Birmingham, and Manchester becoming metropolitan

The United Kingdom has one of the best records for implementation of the member states.⁸² While reluctant to cede sovereignty to the EC, and willing to contest the issuance of unpopular directives, the United Kingdom will generally, and rapidly, implement a directive once it has been issued.⁸³ This leads some to express concern that if a country is fairly diligent in enforcing its laws, whereas other countries are not, the diligent country discriminates against its own companies. For example, the British rarely set standards without having already put in place enforcement measures, in contrast with Italy, where, for instance, there are many laws on food additives, but little routine testing.⁸⁴

On occasion, obstacles can block implementation even in the United Kingdom. In the area of meat hygiene, for example, slaughterhouses that have operated under a system of livestock slaughter and meat distribution largely unchanged during this century must now comply with expensive new requirements set by EC legislation. It is expected that by 1993 hundreds of firms will have to go out of business. One reason is that meat must be kept refrigerated at all times, including during transportation to the point of sale. This requires a large economic outlay for refrigerated vans and the like for retailers, wholesalers and sandwich bars. Lack of funding also affects enforcement, which can be uneven at the local level where money is lacking for frequent and adequate inspections. Parliament is considering passing new legislation to rectify this problem.⁸⁵

Lack of financial resources also provides an obstacle to British implementation of the EC directive on water quality. The United Kingdom has been reluctant to expend the significant funds necessary to privatize the water industry.⁸⁶

Spain

Each Spanish Government ministry is responsible for transposing into national legislation directives relating to its area of expertise.⁸⁷ Within

the Ministry of Foreign Affairs, the Secretariat of State for the EC coordinates implementation and maintains contacts with the other ministries. As discussed in the previous report, the autonomy of provincial governments can hamper effective implementation.⁸⁸ In theory, the local governments must report to the central administration. However, they "sometimes" do not follow this practice. When EC representatives from Brussels come to check on the status of Spanish implementation, the Foreign Affairs Ministry tries to have them meet with the autonomous authorities.⁸⁹

Competing interests between ministries and between industry and consumer groups can cause delays in the legislative process,⁹⁰ but Spain appears to have a good record in implementation. Although the number of its failures to implement is greater than that of such member states as the United Kingdom, Spain does significantly better than Italy. Spanish implementation of the value-added tax, for example, was rapid and efficient. Prime Minister Felipe Gonzalez is strongly committed to EC integration, as in general is the Spanish public.⁹¹

The fact that Spain is a relative newcomer to the EC does cause problems. Spain has had to rewrite almost all of its commercial legislation to comply with EC law. Aside from the 1992 program, Spain already had to adopt several thousand new pieces of legislation pursuant to its 1986 entry into the Community. Spain has just about completed this initial process.⁹²

Spanish judges do not always apply EC commercial law in a comprehensive way, because they have not had time to become fully acquainted with it. Moreover, Spanish institutions sometimes find themselves overwhelmed by the increased burden of EC requirements, such as the Registro Mercantil that is now required to file the accounts of all Spanish companies, but that has lacked the resources to accomplish the task.⁹³

In the environmental area, Spain seeks to approach the level of protection achieved by other member states, of which Denmark is the leader, but

⁸¹ - Continued

bowers, which are one level below metropolitan counties. In the cities, the bowers have the same status as districts, a concept dating from the 12th century. Public analyst, Lyne, Martin & Radford, interview by USITC staff, London, June 5, 1990.

⁸² EC Commission, "Fifth Report," Com (90) 90.

⁸³ Even subsequent to implementation, certain member states can exhibit a lack of willingness to recognize the EC's authority. Although Denmark has a good record for implementing EC environmental directives, the Danes resist inspection of their facilities by EC officials, in spite of the EC Commission's duty to inspect under the Treaty of Rome. Staff of Chairman, European Parliament Environmental Committee, interview by USITC staff, June 4, 1990.

⁸⁴ Official of the British Health and Safety Executive, London, interview by USITC staff June 3, 1990.

⁸⁵ U.S. Embassy personnel, interview by USITC staff, London, June 4, 1990.

⁸⁶ Staff of Chairman, European Parliament Environmental Committee, interview by USITC staff, June 4, 1990.

⁸⁷ The following ministries are the ones that regularly deal with EC measures: transportation, tourism and communications; economy and finance; industry and energy; justice; education and science; health and consumption; public works and urban problems (responsible also for environmental

⁸⁷ - Continued

matters); labor and social security; and agriculture, fishing and food. Official of Spanish Office for Coordination with the European Community, Secretariat of State for the European Community, Foreign Affairs Ministry, interview by USITC staff, Madrid, June 12, 1990.

⁸⁸ USITC, *Effects of EC Integration* USITC Publication 2268, chapter 1.

⁸⁹ Ibid.

⁹⁰ 1992 - *The External Impact of European Unification*, vol. 2, No. 7 (June 29, 1990), p. 11.

⁹¹ Officials of U.S. Embassy, interview by USITC staff Madrid, June 12, 1990; *Financial Times*, May 29, 1990, sec. IV, p. 2.

⁹² Officials of U.S. Embassy, interview by USITC staff, Madrid, June 12, 1990.

⁹³ *Financial Times*, May 29, 1990, sec. 4, p. 2. The situation is improving, however. The register recently installed a computerized system that decreases to about 48 hours the time it takes to obtain the certificate required to found a company. Previously it could take up to 25 days. *Doing Business in Europe* (CCH), June 21, 1990, p. 3.

must work hard to catch up.⁹⁴ As a possible indication of its resolve, Spain apparently hired a Dane to write its hazardous waste regulation.⁹⁵ Even some U.S. multinationals in Spain who were pioneers in environmental matters are having difficulty complying with EC standards. Spain has received complaints from the EC and has itself been fined for failing to fine companies for noncompliance.⁹⁶

West Germany

Implementation in West Germany is generally done by parliamentary legislation. When the Government receives a directive from the EC, the responsible ministry⁹⁷ consults with industry and examines the directive from a general political view, which is sometimes in conflict with industry's view. The Cabinet then determines whether implementing legislation is needed. There are a number of hearings, during which foreign governments have a chance to provide their input. After the hearings have been completed and the ministry has finalized a draft, the parliamentary process begins. The Cabinet presents its draft to the first house of Parliament, the Bundesrat, which is composed of representatives of the West German regions, the Länder. The Bundesrat makes a recommendation, to which the ministry must respond, and the draft then proceeds to the second house of Parliament, the Bundestag. There are then more discussions and more hearings. The draft then returns to the Bundesrat. When passed by both houses, the legislation is enacted. The *Bundesgesetzblatt* publishes each law, which comes into effect when published. It is available only in German.⁹⁸

It can take anywhere from 1-1/2 to 10 or 15 years to prepare EC legislation. Generally, the timetable is 2 to 3 years. Sometimes the West German ministries act to establish national regulation when there is no governing EC legislation. Sometimes they prepare national legislation to influence EC legislation. This was the case with the seventh amendment to the basic EC chemical directive. The West German Ministry of the Environment wanted to push Europe towards better protection of the environment.⁹⁹

⁹⁴ Officials of American Embassy, interview by USITC staff, Madrid, June 12, 1990.

⁹⁵ Officials of Waste Management, interview by USITC staff, Europe, London, June 4, 1990.

⁹⁶ Official of Spanish Office for Coordination with the European Community, Secretariat of State for the European Community, Foreign Affairs Ministry, interview by USITC staff, Madrid, June 12, 1990.

⁹⁷ Various ministries implement different EC directives depending on subject matter. For instance, the Ministry of the Environment would take the lead on chemical directives and the Ministry of Health would handle pharmaceuticals and drugs for human and animal use.

⁹⁸ *Das Parlament*, a weekly publication, publishes what occurs in Parliament; it too is published only in German. Official of the West German Federal Ministry for Youth, Family, Women, and Health, interview by USITC staff, Bonn, June 11, 1990.

⁹⁹ Official of the West German Chamber of Industry and Commerce (DIHT), interview by USITC staff, Bonn, June 12, 1990.

German unification is of concern in the area of implementation. Although it is likely that what is now East Germany will adopt West Germany's laws, discussions are under way between the Germanies regarding transitional legislation, which would be in effect from several months to a year or so. Consequently, the new German Government might need to seek derogations from the deadlines of EC directives in order to protect East German agriculture, many sectors of which have been protected by import quotas.¹⁰⁰ The West German Government expects these derogations to be temporary and does not consider that unification with East Germany will materially slow efforts to comply with the 1992 program's mandates.¹⁰¹

France

In France, each Government ministry is responsible for implementation in its own sector. Under French law, a minister can delegate significant responsibility for implementation to local authorities. However, the EC Commission prefers for France to implement by ministerial decrees, which become national law. The problem with this approach is that the issuance of a ministerial decree involves a lengthy approval process.¹⁰² French implementation is overseen by the SGCI (Secretariat General de la Comite Interministeriel Pour Les Questions de Cooperation Economique Europeenne). That body is France's inter-ministerial committee on EC affairs. It is similar to a U.S. government task force, and is composed of people on loan from the various ministries of the French Government. Its members maintain close contact with the French members of the various working groups in Brussels, and liaise between the French ministries and the working groups.¹⁰³

France does not always manage to fully implement EC law. According to a report issued on July 10, 1990, by the French Council of State, France ranks fourth among member states in the transposition of EC directives into French law, but ranks much lower, along with Italy and Greece, in the actual application of EC law.¹⁰⁴ The report found that most French civil servants are ignorant of EC law and recommended that they be given better training in such matters. The report also recommended that each ministry create an EC section reporting directly to the minister, and that each new French implementing law be accompanied by the corresponding EC text and a

¹⁰⁰ Ibid.

¹⁰¹ Officials of the West German Federal Ministry for Economics, interview by USITC staff, Bonn, June 12, 1990.

¹⁰² Official of French Secretariat of State for the Environment, interview by USITC staff, Neuilly-sur-Seine, June 8, 1990.

¹⁰³ Official of American Embassy, interview by USITC staff, Paris, June 8, 1990.

¹⁰⁴ 1992 - *The External Impact of European Unification*, vol. 2, No. 8 (July 13, 1990), p. 4.

guide to the situation in the other member states.¹⁰⁵ In the environmental area, for example, the EC Commission is currently prosecuting 47 infringement actions against France. Of the 47 cases, 7 are before the Court of Justice, and 3 are reprimands. In early 1990, however, the French Council of State issued a ruling that all French high courts must ensure the direct effect of EC law, a development that may improve France's implementation record.¹⁰⁶

Such disputes do not always involve a simple failure to implement. In the case of the directive for the protection of birds, for example, France interpreted the directive differently from the EC Commission, finding that the directive was not as specific as the EC Commission claimed. The Commission brought an infringement action before the European Court of Justice.¹⁰⁷ The environmental areas in which France is having difficulty passing decrees are water quality, marine life, and water analysis techniques.¹⁰⁸

External Relations

Countries around the world are responding with interest and apprehension to the challenges posed by the EC's quest to create a single, integrated market. The nations of the European Free Trade Association (EFTA),¹⁰⁹ which represent the EC's largest trading partner, are pursuing a more structured partnership with the Community through negotiations to establish a European Economic Space (EES). Certain EFTA countries, as well as other third countries, are seeking membership in the EC in order to take full advantage of the benefits of the internal market process. Japanese officials are wary that the EC's barriers to third countries will remain unchanged or worsen after 1992. Developing countries, particularly those benefiting from the Lome Convention, continue to be concerned that the EC will abandon its commitments to them as the EC's attention is redirected toward the EC 92 process as well as events occurring in central and Eastern Europe. Indeed, German reunification is adding a new dimension to EC integration. However, although both German reunification and the reforms taking place in central and Eastern Europe are demanding EC attention, the Community remains determined to meet the goals of the single market process on time.

Central and Eastern Europe and the U.S.S.R.

EC relations with the countries of central and Eastern Europe and the U.S.S.R. intensified rapidly during the first 6 months of 1990 with the conclusion of bilateral trade and economic

¹⁰⁵ Ibid.

¹⁰⁶ EC Commission, "Fifth Report," Com (90) 90, p. 4.

¹⁰⁷ Official of French Secretariat of State for the Environment, interview by USITC staff, Neuilly-sur-Seine, June 8, 1990.

¹⁰⁸ Ibid.

¹⁰⁹ EFTA countries include Austria, Finland, Iceland, Norway, Sweden, and Switzerland.

cooperation agreements with all of the European nations of the Council for Mutual Economic Assistance (CMEA)¹¹⁰ except Romania. This network of agreements is only the first step towards building relations between the two blocs of countries. During a special summit meeting in Dublin in April, EC leaders agreed to begin negotiations for second-generation association agreements that would offer more extensive cooperation and trade concessions, as well as an institutional framework for political dialog.¹¹¹

Status of Trade and Economic Cooperation Agreements

By the end of 1989, the EC had concluded bilateral trade and economic cooperation agreements with Hungary, Poland, and the Soviet Union.¹¹² These agreements entered into effect in 1988 for Hungary, 1989 for Poland, and on April 1, 1990, for the U.S.S.R. During the first half of 1990, the EC signed additional agreements with Bulgaria and East Germany, and upgraded an existing accord with Czechoslovakia. A bilateral agreement with Romania was initialled on June 8, but political developments have prevented the EC from signing it.¹¹³

The agreements with Bulgaria, East Germany, and Czechoslovakia were signed in early May and are similar to the agreement concluded with Hungary in 1988. They cover trade in both industrial and agricultural products, with a few exceptions, over a 10-year period. Each country agreed to grant the other most-favored-nation status. Under these accords, the EC will suspend or eliminate national quantitative restrictions imposed on their exports to the EC in exchange for improved market access for EC products and investment guarantees for Community firms. The agreements also improve economic cooperation in a wide range of areas.

The EC-East Germany accord will "retain its validity as long as German unification has not been finalized."¹¹⁴ Furthermore, the agreement would

¹¹⁰ CMEA (also abbreviated as COMECON) consists of the U.S.S.R., Czechoslovakia, Hungary, Poland, Romania, East Germany, Bulgaria, Mongolia, Cuba, and Vietnam. The European CMEA includes all of the CMEA countries except Mongolia, Cuba, and Vietnam.

¹¹¹ Delegation of the Commission of the European Communities, Office of Press and Public Affairs, "The European Community Welcomes German Unification, Reinforces Guidelines for Internal and External Activities and Confirms Commitment to Political Union," *European Community News*, Apr. 30, 1990.

¹¹² The EC signed more limited agreements with Romania in 1980 and Czechoslovakia in 1988. For more information on all of these agreements, see U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States—First Follow-Up Report* (Investigation No. 332-267), USITC Publication 2268, March 1990, pp. 1-7 to 1-8.

¹¹³ "EEC/Romania: Doubts Thrown on Trade Agreement and Extension of PHARE," *European Report*, No. 1595 (June 16, 1990), sec. 5, p. 10, and EC Delegation official, telephone conversation with USITC staff, Washington, DC, July 19, 1990.

¹¹⁴ "GDR, EC Sign Trade and Cooperation Agreement," *The Week in Germany*, May 11, 1990, p. 5.

not affect the special trading arrangements between the two Germanies outlined in the 1957 Protocol on inter-German trade,¹¹⁵ which provides for the duty-free entry of East German goods into West Germany.

German Reunification

The rapid pace of German reunification during the first 6 months of 1990 culminated July 1 in the economic, monetary, and social union of the two Germanies. Negotiations for political unification are now taking place.

At the special Dublin Summit on April 28, 1990, originally convened for the purpose of analyzing the implications for the Community of German reunification, EC ministers announced that the integration of East Germany into the Community will become effective as soon as unification is legally established, subject to the necessary transitional arrangements. EC summit leaders confirmed that East Germany will not be required to formally apply for membership in the EC, nor will revision of the treaties of Rome and Paris be required.¹¹⁶

President of the EC Commission Jacques Delors outlined a proposed three-stage process for integrating East Germany into the Community. He stressed the importance of requiring East Germany to meet its obligations to the EC from the beginning of the reunification process. In the first phase—the period prior to unification—East Germany will focus on adapting its laws to those of the EC. In particular, the EC aims to monitor state aid policies, state monopolies, and public procurement operations. EC ministers also made available loans from the European Investment Bank and other EC institutions as East Germany introduces a market economy. The second phase that begins after unification has taken place foresees the gradual application of EC rules during a transition period, as well as the implementation of foreign policy that is compatible with the EC's external commitments. Those internal rules that East Germany should apply include the Common Agricultural Policy, competition policy, and policies covering fisheries, trade, transport, and the environment.¹¹⁷ The third phase calls for the full application of EC laws in East Germany. Community leaders at the regular summit meeting on June 25-26 announced the EC Commission's intention to submit in September proposals for transitional arrangements for East

¹¹⁵ EC Council, press release 6249/90 (Presse 58), May 8, 1990.

¹¹⁶ These treaties established the European Economic Community and the European Coal and Steel Community. Delegation of the Commission of the European Communities, Office of Press and Public Affairs, "The European Community Welcomes German Unification, Reinforces Guidelines for Internal and External Activities and Confirms Commitment to Political Union," *European Community News*, Apr. 30, 1990.

¹¹⁷ "German Unification: Commission Proposes Three-State Process for Integrating East Germany Into EEC," *European Report*, No. 1580 (Apr. 19, 1990), sec. 1, p. 1.

German entry into the EC following official German unification.

On June 28, the EC Council adopted a regulation establishing a customs union between the Community and East Germany as of July 1, 1990. The customs union will remain in effect until Germany reunifies, at which time East Germany will automatically become a member of the EC. The customs union provides that both East Germany and the EC lift all tariffs and quantitative restrictions on industrial imports originating in the other trading partner. At the same time, East Germany must introduce measures to implement the EC's Common Customs Tariff on trade with third countries, which should prevent the flow of third-country goods into the EC through the open inner-German border.¹¹⁸ Both sides are permitted to invoke safeguard measures should a domestic industry be adversely impacted by imports. The EC Commission also proposed lifting similar restrictions on farm and fish products.

Aid to Central and Eastern Europe

The two most notable developments in the area of aid to central and Eastern Europe were the extension of the PHARE program to new countries and the establishment of the European Bank for Reconstruction and Development (EBRD). PHARE—Poland Hungary Aid for Restructuring of Economies—is a special program established to coordinate economic aid to Hungary and Poland from the group of 24 industrialized nations. The EC is coordinator of the program. On July 4, ministers of the Group of 24 agreed to extend the G-24 assistance to East Germany, Czechoslovakia, Bulgaria, and Yugoslavia based on progress in political and economic reform.

On May 29, officials from 40 countries and 2 European institutions¹¹⁹ signed a charter establishing the EBRD that will provide financial assistance to the countries of central and Eastern Europe. The target date for operation is early 1991. The 12 EC member states and European institutions hold a majority stake of 51 percent in the new bank, whereas the United States is the single largest shareholder, with a 10-percent share.¹²⁰

¹¹⁸ The EC will not lift its restrictions imposed on East German imports until a special committee established by the regulation verifies that East Germany has complied with its obligations. These obligations include the introduction of the Common Customs Tariff and other EC common commercial policy measures, as well as measures guaranteeing free access for EC goods. Council Regulation No. 1794/90 on Transitional Measures Concerning Trade with the German Democratic Republic, OJ No. L 166 (June 29, 1990), p. 1.

¹¹⁹ The participants include the 24 nations of the Organization for Economic Cooperation and Development; the 8 countries of central and Eastern Europe, including the Soviet Union and Yugoslavia; 2 institutions including the EC Commission and the European Investment Bank; as well as Cyprus, Malta, Egypt, Israel, Liechtenstein, Morocco, South Korea, and Mexico.

¹²⁰ Overseas Development Council, "The European Bank for Reconstruction and Development," *Policy Focus*, No. 3, 1990, pp. 1 to 2 and 5 to 6.

The bank, which is intended "to align development with democracy,"¹²¹ is the first international financial institution to stipulate that its borrowers commit themselves to the principles of multiparty democracy, pluralism, and market economics.¹²² Other unique features are its explicit commitment to environmental protection and that the majority of its exposure will be to the private sector, through loans and equity investments. At least 60 percent of its 10 billion ECU of capital will be lent annually to private-sector borrowers.¹²³

Future Relationship

In April 1990, the EC Commission presented a proposal on the future development of EC relations with the countries of central and Eastern Europe by establishing association agreements. Eligibility to negotiate and the timeframe for implementing such an agreement would depend on whether a country meets certain conditions of a market economy and democratic principles. Association agreements would provide an institutional framework for political dialogue; intensify economic, scientific, and technological cooperation; and would aim for free trade through further reforms in areas such as taxation, pricing systems, subsidies, and monetary policy.¹²⁴ Although the association agreements drawn up with Greece, Portugal, and Spain explicitly offered ultimate accession to the EC, a similar statement will not be included in the agreements to be concluded with the European CMEA countries.¹²⁵

Certain European CMEA members including Poland, Hungary, and Czechoslovakia have already announced a desire to become members of the EC. Although the plan to draw up association agreements does not refer to the possibility of these countries eventually joining the EC, Community officials have indicated that the agreements could act as stepping stones toward EC membership.¹²⁶ The Community has hinted, however, that negotiations for an association agreement—the next step closer to membership—could be easier for Hungary and Czechoslovakia than Poland because their economies are stronger.¹²⁷ East Germany, a special case, will become an EC member upon

reunification of the two Germanies. Yugoslavia, which is not a CMEA member, has also announced its goal to replace the current EC-Yugoslavia cooperation agreement negotiated in 1980 with an association agreement with the view of becoming a full member of the EC.¹²⁸

Options other than EC membership are available, however. For example, on June 13 the EFTA signed three joint declarations of cooperation with Czechoslovakia, Hungary, and Poland. These accords cover a range of topics—subject to change in the future—including trade promotion; economic, industrial, technical, and scientific cooperation; and issues such as tourism, transport, and environmental protection. Joint committees will implement in practical forms the cooperation outlined in the agreements. Also, provisions in the declarations call for joint examination later this year of the possibilities of establishing free-trade areas with the three countries.¹²⁹ These cooperation pacts, as well as an existing agreement with Yugoslavia, reflect the "harmonization of relations" between EFTA and European CMEA countries with a view to future negotiations,¹³⁰ although EFTA nations have not yet discussed the possibility of any European CMEA countries becoming an EFTA member.¹³¹

Furthermore, central and Eastern European countries may aspire to join the European Economic Space (EES) currently under negotiation between the EFTA and EC nations. Indeed, on June 22 the Soviet ambassador to the EC called for EFTA and the EC to include central and Eastern European countries as well as the Soviet Union in negotiations to establish a EES.¹³²

Relationship to EC 92

Fears have been strong among the member states that rapid German reunification and the reform process in Eastern and central Europe are diverting the EC's attention away from the 1992 integration process.¹³³ However, it is unlikely that these events will sidetrack the EC from meeting its goal to create a single market by 1992. In fact, even side issues to the core 1992 process, such as economic and monetary union and political union, are progressing smoothly.

Some observers argue that the scale of potential gains in trade with Eastern and central Europe are not sufficient to turn the EC from its path towards

¹²¹ Comment by French President Mitterrand. Bureau of National Affairs (BNA), "New East European Development Bank Formally Launched with Paris Signing," 1992: *The External Impact of European Unification*, June 1, 1990, p. 1.

¹²² Lafayette Publications, "New Bank Head Aims for Quick Start," *Europe-1992*, June 13, 1990, p. 678.

¹²³ "The European Bank for Reconstruction and Development," p. 3.

¹²⁴ "EEC/Eastern Europe: Commission Prepares Talks on Closer Cooperation," *European Report*, No. 1578 (Apr. 10, 1990) sec. 5, p. 8.

¹²⁵ Bureau of National Affairs (BNA), "EC Economic and Financial Cooperation in Eastern Europe," 1992: *The External Impact of European Unification*, May 4, 1990, pp. 13-16.

¹²⁶ Bureau of National Affairs (BNA), "In Brief," 1992: *The External Impact of European Unification*, Apr. 20, 1990, p. 9.

¹²⁷ Lafayette Publications, "Poland Sees Eventual E.C. Membership," *Europe 1992*, June 27, 1990, p. 694.

¹²⁸ "EEC/Yugoslavia: Membership Application Expected in Two or Three Years' Time," *European Report*, No. 1586 (May 9, 1990), sec. 5, p. 2.

¹²⁹ EFTA, Press and Information Office, "Background Press Information on the Signing of Joint Declarations of Cooperation With Czechoslovakia, Hungary and Poland," *EFTA Information*, June 13, 1990. Finland has already concluded free-trade agreements with some East European countries.

¹³⁰ "EEC/USSR: Soviet Union Wants Inclusion in EES," *European Report*, No. 1598 (June 25, 1990), sec. 5, p. 1.

¹³¹ "Poland Sees Eventual E.C. Membership," p. 694.

¹³² "EEC/USSR: Soviet Union Wants Inclusion in EES," *European Report*, No. 1598 (June 25, 1990), sec. 5, p. 1.

¹³³ "European Integration: Member States Call for EEC of Twelve To Be Strengthened," *European Report*, No. 1574 (Mar. 22, 1990), sec. 1, p. 2.

greater EC integration.¹³⁴ Frans Andriessen, Vice President of the EC Commission, has reconfirmed that "However breathtaking the events in Eastern Europe and however urgent the need for response to these events have been, we have not allowed them to deflect us from our internal objectives."¹³⁵ The success to date of the single market initiative on the EC's economy is likely to set a standard to be pursued by the Central and Eastern European countries.¹³⁶ Indeed, Frans Andriessen stated that "The role model the EC has provided for Eastern Europe has been an instrumental factor in triggering economic reform in these countries."¹³⁷

Another EC Commission official has argued that the EC would not deviate from its path towards a single market because the strength of the integrated market would be the best source for aid and technical assistance to the nations of Central and Eastern Europe. Sir Leon Brittan, Vice President of the EC Commission, claims that the economic efficiencies created by the single market will offer Eastern and Central European producers a more attractive market and will be the source of more official resources to aid these same countries.¹³⁸

Indeed, it is argued that —

*The changes in Central and Eastern Europe and the corresponding commitment of the EC can also act as a spur to the EC integration process. Energetic steps towards deepening the EC are now to the good, in order to ensure the lasting incorporation of Germany, in order for the EC to enhance its scope for positive action relative to the USA and the USSR, and not least, to meet the demands which the Central and Eastern European sphere has imposed on the Community.*¹³⁹

The intergovernmental conference recently planned for December 1990 to discuss political union "is a clear indication of the stronger political dynamics of the integration process resulting largely from the recent events in Central and Eastern Europe."¹⁴⁰

Concerns that German reunification would slow the momentum towards the single market have been partially addressed by West German Chancellor Helmut Kohl, who has been quick to reaffirm his support for EC integration. Indeed, "For the German Government, the ultimate objective of European integration has always been political union. In that regard, the single market . . . is

considered a further step toward the much more ambitious goal of a politically united Europe."¹⁴¹ In a joint statement issued with French President Francois Mitterrand, he urged that progress toward economic and monetary union be accelerated as well as political integration, which ultimately resulted in the decision to convene the intergovernmental conference on political union in December 1990.¹⁴²

Fears about EC integration taking a back seat to German unity have somewhat subsided since the earlier part of the year when the reunification process remained unsettled.

*The speed of European integration has not been slowed, as some feared. In fact it appears to have been speeded up. The Germans want to demonstrate that they are not so preoccupied with absorbing East Germany that they are turning their backs on the rest of Europe. And the other Europeans seek to bind Germany even more tightly in a strong Western European economic and political network.*¹⁴³

Some observers feel that progress towards European monetary union may have been accelerated by German reunification because of the desire to anchor Germany with the EC.¹⁴⁴ Furthermore, recent polls of West Germans indicate strong support for EC integration. For example, a May 22 poll of 597 West German business executives showed that 63 percent rate the EC single market more important than German unification.¹⁴⁵

Patterns of Trade and Investment

The increased cooperation among EC, EFTA, and the European CMEA countries to build a large European economic sphere is likely to increase intra-European trade in the long run. As border restrictions continue to ease among these nations, trade and investment flows will increase.

The potential for increased trade and investment with Eastern and Central Europe is enormous. In addition to large domestic markets, the workforces of the European CMEA countries demand relatively low wages and are generally more skilled and literate than those in other developing countries. The proximity to the EC is also particularly attractive to potential investors, especially with the creation of the EC single market in 1992. The network of bilateral trade and economic cooperation agreements, soon to be replaced by even more wide-ranging association agreements, dismantle EC trade restrictions on imports from the European CMEA countries and provide a backdoor to the EC market.

¹⁴¹ Carola Kaps, "A United Germany in the New Europe," *Europe*, July/August 1990, pp. 19-21.

¹⁴² "Dublin European Council, June 25/26, 1990," *European Report*, No. 1598, supplement (June 27, 1990), p. 1.

¹⁴³ Robert D. Hormats, statement before the Joint Economic Committee, June 21, 1990.

¹⁴⁴ C. Michael Aho, statement before the Joint Economic Committee, June 21, 1990.

¹⁴⁵ "Managers: EC More Important than Unity," *The Week in Germany*, May 25, 1990, p. 5.

¹³⁴ National Association of Manufacturers, *Update on EC-92*, April 1990, p. 11.

¹³⁵ Frans H.J.J. Andriessen, "Europe 1992: The U.S. Role in a United Europe," speech before the Columbia Institute Conference, Washington, DC, Feb. 23, 1990 (Andriessen speech).

¹³⁶ National Association of Manufacturers, *Update on EC-92*, April 1990, p. 10.

¹³⁷ Andriessen speech.

¹³⁸ Keith M. Rockwell, "E. Europe Reforms Won't Delay '92 Program, EC Official Says," *Journal of Commerce*, Mar. 23, 1990, p. 3A.

¹³⁹ Rudolf Hrbek, "The EC and the Changes in Central and Eastern Europe," *Intereconomics*, May/June 1990, p. 139.

¹⁴⁰ *Ibid.*, p. 132.

However, these effects will not emerge significantly in the short run. Most companies, including those of West Germany, are responding cautiously to events in the European CMEA. Because of the lack of adequate infrastructure as well as severe structural problems, large amounts of Western exports or investment in the short run are improbable. Of particular concern is the European CMEA's chronic shortage of foreign exchange that will limit their ability to finance imports or allow repatriation of profits earned from investment.¹⁴⁶

East Germany presents a special case. In addition to those benefits attributed to all of the Central and Eastern European countries—a large untapped domestic market and a low-wage and highly skilled labor force—East Germany also provides guaranteed access to the EC's market and prospects for a more short-term infrastructural boom.¹⁴⁷ Most observers are very optimistic about trade and investment opportunities in East Germany. "Once a large volume of West German capital begins flowing into the eastern part of the country, today's East Germany could become what South Korea and Taiwan have become for Southeast Asia: a dynamic engine of export driven growth."¹⁴⁸ One U.S. observer claims that "East Germany will add an immediate boost to U.S. export growth Especially as East Germany will be fully integrated in the EC and endowed immediately with a strong and convertible currency, U.S. industry will find many direct and indirect export opportunities."¹⁴⁹

Although the implications for trade and investment flows to the region as a whole are limited in the short run, foreign investors are optimistic over long-term prospects. "Anticipating a higher real rate of return for their money in the east than in the west, firms are already flocking in. Double-digit economic growth in East Germany is possible in the next few years," with growth prospects in neighboring CMEA countries only slightly less optimistic.¹⁵⁰ A survey of top U.S. and European companies conducted by the KPMG consulting firm indicated that 90 percent of all companies questioned see potential new business opportunities in central and Eastern Europe and are willing to exploit them.¹⁵¹ Eighty percent of the U.S. firms believe German reunification will provide new commercial opportunities.¹⁵²

The prospects for exports in general to the European CMEA countries will be limited until economic reforms are implemented.¹⁵³ However, exports to West Germany are likely to increase in the nearer term in order to satisfy increased demand from East Germans.¹⁵⁴ Efforts to rebuild the broken economies of Central and Eastern Europe will increase the demand for capital goods in particular.¹⁵⁵ Exports of capital goods are likely to increase most to West Germany but also directly to the European CMEA countries or through certain other nations with traditional ties to Eastern Europe such as Austria.¹⁵⁶ Because reforms are not likely to increase the purchasing power of the European CMEA countries in the short run, exports to these nations are likely to outweigh imports over the next few years.¹⁵⁷

Certain member states of the EC remain concerned that increased competition from the European CMEA countries will adversely affect EC producers, particularly in the poorer regions where there are strong similarities in production.¹⁵⁸ These less developed EC member states could find themselves in competition with central and Eastern European countries for export markets and in attracting new investment and aid funds.¹⁵⁹ Furthermore, certain member states on the periphery of the Community may be disadvantaged as the EC's center of gravity shifts towards Eastern Europe.¹⁶⁰

Developing countries have similar concerns. They fear that increased economic aid and investment to the European CMEA nations will reduce the EC's commitments to them, at least in the short run.¹⁶¹ Furthermore, there are long-run implications as well. Once the infrastructure for a market system is installed, the nations of central and Eastern Europe could become serious competitors to third-world producers.¹⁶²

Many third countries are wary of the EC's response to dislocation within the Community that is likely to emerge from a number of events—the internal-market process, increased imports from Central and Eastern Europe, and competition for aid funds.¹⁶³ Should serious dislocation result, the

¹⁴⁶ "Europe's Horn of Plenty," p. 72.

¹⁴⁷ *Ibid.* In order to satisfy increased demand, West Germany is likely to divert some of its exports to the domestic market and increase imports.

¹⁴⁸ Hormats, Statement, June 21, 1990.

¹⁴⁹ *Ibid.*

¹⁵⁰ "Europe's Horn of Plenty," p. 72.

¹⁵¹ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 1-10.

¹⁵² Gary Clyde Hufbauer, *Europe 1992, An American Perspective* (Washington: The Brookings Institution, 1990), p. 18.

¹⁵³ Hrbek, "EC and Central and Eastern Europe," p. 139.

¹⁵⁴ "The Big Switch," *South*, April 1990, p. 13.

¹⁵⁵ Overseas Development Council, "The European Bank for Reconstruction and Development," *Policy Focus*, No. 3, 1990.

¹⁵⁶ Hufbauer, *Europe 1992*, p. 18.

¹⁴⁶ Other structural obstacles to trade and investment include cultural differences, questions surrounding private property ownership, and an uncertain legal environment. See Hormats, Statement, June 21, 1990.

¹⁴⁷ "Europe's Horn of Plenty," *The Economist*, June 2, 1990, p. 72.

¹⁴⁸ John J. LaFalce (Democrat of New York), "The U.S. Stake in Reunification," *New York Times*, Apr. 1, 1990.

¹⁴⁹ Stephen Cooney, Statement before the Joint Committee, June 21, 1990.

¹⁵⁰ Aho, Statement, June 21, 1990.

¹⁵¹ "Eastern Europe: KPMG Study Investigates Potential Business Investment," *European Report*, No. 1586 (May 10, 1990), sec. 3, p. 3.

¹⁵² Leader Publications, *Europe 1992*, vol. 1, No. 5 (May 1990), p. 1.

EC may limit its trade-liberalizing measures to the rest of the world.¹⁶⁴ Third countries are also watching West Germany to determine whether its preoccupation with German reunification will decrease its economic activities elsewhere in the world.¹⁶⁵

EFTA

Since the EC and EFTA are each other's largest trading partner, EFTA is concerned about any aspect of the EC's internal-market process that could erode its privileged position relative to the EC and adversely affect bilateral trade flows after 1992. EFTA nations are particularly concerned that EC 92 could disadvantage its companies in relation to EC firms and that the EC could become a trade fortress. Evidence already shows that investment flows by foreign as well as EFTA firms are being redirected away from EFTA to the EC.¹⁶⁶

Currently, the EC and EFTA are negotiating a more structured relationship based on the creation of a EES.¹⁶⁷ The purpose of the EES is "to enable to the greatest possible extent, the free movement of goods, persons, services and capital"¹⁶⁸ between the 18 EC and EFTA countries, as well as Liechtenstein.¹⁶⁹ An EFTA statement issued on May 18 declared that establishment of the EES would create more jobs, increase global competitiveness between Europe and the rest of the world, and enable European business and industry to plan and invest within a predictable trade policy framework within a short time.¹⁷⁰ EFTA nations hope that such a structured partnership will ensure that they maintain their privileged position relative to the EC.¹⁷¹

Last December, EC and EFTA foreign ministers agreed to begin formal negotiations aimed at further economic integration and eventual creation of the EES envisioned in the Luxembourg Declaration.¹⁷² Between January and March 1990, the EC and EFTA conducted exploratory talks to clarify the possible scope, content, and form of a future EES treaty. The topics discussed included the four freedoms and

flanking policies such as education, research and development, environment, consumer protection, and the social dimension. Such issues as the legal basis for the EES and the decisionmaking process were also covered. A common body for EFTA parliamentarians and representatives of the European Parliament is foreseen.¹⁷³

At an informal EFTA ministerial meeting in April, EFTA ministers declared themselves ready to begin formal negotiations with the EC without delay.¹⁷⁴ They also agreed to seek certain exceptions, although the EC has indicated that it is unwilling to honor exceptions and derogations except on a very limited basis. Some of the exceptions listed by EFTA officials cover the areas of free movement of capital; immigration; agriculture; fisheries; the right to buy private, commercial, and financial property; and lorry transit. EFTA ministers also cited the need to create a mechanism for joint decisionmaking so that EFTA interests are taken fully into account.¹⁷⁵

On June 18, the EC Council approved a negotiating mandate outlining the EC's objectives in talks with EFTA countries. The EC's mandate states that special exceptions and transitional measures for EFTA countries should be limited to possibly agriculture and fisheries.¹⁷⁶ The mandate also requires EFTA to create a supranational structure capable of implementing competition and state aid policies and "enabling it to speak with one voice."¹⁷⁷ The EC also insists that it will retain its autonomy over internal decisions but foresees consultation and joint decisions by consensus over matters concerning the EES.¹⁷⁸

On June 20, the EC and EFTA launched formal negotiations to establish the EES. However, the two sides only agreed to a schedule of talks and a working program. Real negotiations are not expected to start until the next meeting at the end of July.¹⁷⁹ Both sides aim to reach an agreement by 1991 so that the EES can enter into effect on January 1, 1993, the deadline for the completion of the EC's internal market initiative.¹⁸⁰

Three major obstacles to the creation of the EES have been cited by President of the EC Commission Jacques Delors. First, he argues that EFTA needs a supranational structure "which would enable it to

¹⁶⁴ Ibid.

¹⁶⁵ Richard Lawrence, "Export Offensive' Looms as West Takes Aim at East," *Journal of Commerce*, Mar. 19, 1990, p. 11B.

¹⁶⁶ Peter Montagnon, "Why EFTA Is Worried," *Financial Times*, July 2, 1990, p. 5.

¹⁶⁷ For a historical perspective of the EES, see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 1-11 to 1-12.

¹⁶⁸ "EEC/EFTA: Joint Declaration Calls for Launch of EEC Negotiations," *European Report*, No. 1550, (Dec. 18, 1990), sec. 5, p. 8.

¹⁶⁹ EFTA countries agreed in April to include Liechtenstein as a party to the EES negotiations with a view to Liechtenstein's becoming a contracting party on the EFTA side. EFTA, "Liechtenstein To Reinforce Ties With EFTA," *EFTA News*, No. 3, May 10, 1990, pp. 3-4.

¹⁷⁰ "EFTA-EC Relations: EFTA Paper Outlines Stance on Relations with Community," 1992-*The External Impact of European Unification*, June 1, 1990, p. 6.

¹⁷¹ Montagnon, "Why EFTA Is Worried," p. 5.

¹⁷² For further information, see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990.

¹⁷³ EFTA, "HLSG Meeting Concludes Satisfactory Exploratory Phase," *EFTA News*, No. 2, Mar. 26, 1990, pp. 1-2.

¹⁷⁴ EFTA, "EFTA Welcomes EC Draft Mandate," *EFTA News*, No. 3, May 10, 1990, p. 1.

¹⁷⁵ "EEC/EFTA: EFTA Defines Negotiating Platform," *European Report*, No. 1578 (Apr. 5, 1990), sec. 5, p. 3.

¹⁷⁶ "EEC/EFTA: Commission Adopts Negotiating Mandate," *European Report*, No. 1585 (May 8, 1990), sec. 5, p. 4.

¹⁷⁷ "EFTA-EC Relations: Negotiating for EES Seen as Providing Flexibility," 1992-*The External Impact of European Unification*, May 18, 1990, p. 3.

¹⁷⁸ "EEC/EFTA: Commission Adopts Negotiating Mandate."

¹⁷⁹ "EFTA-EC Relations: Two Blocs Launch EES Talks; Next Meeting Set for July," 1992-*The External Impact of European Unification*, June 29, 1990, p. 11.

¹⁸⁰ "EEC/EFTA: EES Negotiations Start With No Surprises," *European Report*, No. 1597 (June 21, 1990), sec. 5, p. 1.

speaking effectively with one voice with the Community."¹⁸¹ Second, Delors opposes EFTA's numerous requests for exemptions from Community rules.¹⁸² Lastly, Delors cited disagreements over the level of participation by EFTA in the decision-making process.¹⁸³ On May 4, Delors said that "EFTA should join the EC if they want to have direct influence and take part in its decision-making process."¹⁸⁴

Several EFTA countries are considering membership in the EC, although Community officials have indicated that the EC 92 process must be complete before new members can join. Austria applied for membership in 1989 and noted on May 18, 1990, that it was not unrealistic to anticipate Austrian accession by 1994.¹⁸⁵ According to a public opinion poll taken earlier this year, the majority of Norwegians favor joining the EC for the first time since 1972.¹⁸⁶ Although the ruling party in Sweden opposes EC entry, both of the leading opposition parties support EC membership.¹⁸⁷ Finland¹⁸⁸ and Switzerland¹⁸⁹ continue to object to full EC membership on grounds that they could not maintain their politically neutral position.

The liberalization of Eastern Europe has placed an added burden on EC/EFTA talks. Many East European countries view EFTA membership as a stepping stone to full EC membership. Both the U.S.S.R. and Hungary have approached EFTA for possible membership.¹⁹⁰ However, EFTA officials are concerned that negotiations to create an EES would be hindered should East European countries join EFTA.¹⁹¹

Japan

The Japanese are largely responding to the EC integration process with apprehension. Many firms fear that EC 92 will bring dramatic changes within the Community itself, but that external barriers will remain unchanged or will increase against third countries.¹⁹² Japanese officials often cite the

automotive sector as an example of rising protection against third countries.¹⁹³ As a result, many Japanese firms are setting up local subsidiaries in the EC. In the field of public procurement, Japanese officials are concerned that the EC will invoke the principle of reciprocity, which will hamper the ability of Japanese firms to access the EC's public procurement market.¹⁹⁴ Most Japanese firms agree that the harmonization of standards across the EC will benefit those doing business in more than one Community country.¹⁹⁵

According to the results of a Keidanren poll¹⁹⁶ conducted in September 1989, Japanese firms have mixed feelings about the EC 1992 integration program. Some feel that the EC might take discriminatory action against Japanese firms. Of particular concern are rules of origin, local content requirements, reciprocity, and antidumping measures. Others feel that integration will benefit their European operations through standards harmonization and simplification of customs clearance procedures and documents. Corporations in general feel that recovery of the EC economy will benefit them positively, either directly or indirectly, although respondents predicted increased competition with EC enterprises. According to the survey, the majority of Japanese firms are responding to the EC 92 process by expanding their local bases or establishing new ones. Their responses indicate, however, that their plans for organizational expansion and reform are aimed not only at responding to EC market integration but also at promoting ongoing localization and globalization of their operations.

A more recent survey of Japanese manufacturing companies in Europe was conducted by the Japan External Trade Organization.¹⁹⁷ This survey found that the number of Japanese manufacturers in the EC and EFTA countries more than quadrupled over the last year. According to the poll, few Japanese companies cited EC integration in 1992 as the primary reason for greater investment in Europe. The most common reason cited for the sudden increase in Japanese investment was a general expansion in global business strategies. However, the EC feels that the increase in the number of Japanese manufacturers

¹⁸¹ "EEC/EFTA: Gloom Deepens Over Agreement Prospects," *European Report*, No. 1582 (Apr. 26, 1990), sec. 5, p. 7.

¹⁸² "EEC/EFTA: EFTA Defines Negotiating Platform," *European Report*, No. 1578 (Apr. 5, 1990), sec. 5, p. 3.

¹⁸³ *Ibid.*

¹⁸⁴ "EEC/EFTA: Delors Continues To Be Tough on EFTA," *European Report*, No. 1584 (May 5, 1990), sec. 5, p. 6.

¹⁸⁵ "EEC/Austria: Mock Wants Accession for 1994," *European Report*, No. 1589 (May 24, 1990), sec. 1, p. 1.

¹⁸⁶ "EEC/Norway: Support for Accession to EEC Growing," *European Report*, No. 1565 (Feb. 19, 1990), sec. 5, p. 2.

¹⁸⁷ David Buchan and Robert Taylor, "Talks With EC Will Mean All Change at EFTA," *Financial Times*, June 11, 1990, p. 4.

¹⁸⁸ David Buchan, "Finland Sees Prospect of EC Membership Receding," *Financial Times*, May 14, 1990, p. 2.

¹⁸⁹ "EFTA-EC Relations: Swiss Government Committed but Businesses Waver on EES," *1992-The External Impact of European Unification*, May 18, 1990, p. 4.

¹⁹⁰ "EC and EFTA Countries Move Closer to Establish the European Economic Space," *EC-US Business Report*, vol. 2, No. 2, Feb. 1, 1990, p. 13.

¹⁹¹ Rene Schwok, "EFTA Is No Answer for Europe," *The Journal of Commerce*, Mar. 22, 1990, p. 8A.

¹⁹² For example, Fujitsu and Hitachi officials, interviews by USITC staff, Tokyo, June 4 and 8, 1990.

¹⁹³ The EC is currently negotiating a new EC-wide voluntary restraint arrangement on automobiles with Japan. For more information, see ch. 20 of this report.

¹⁹⁴ Hitachi officials, interview by USITC staff, Tokyo, June 8, 1990.

¹⁹⁵ *Ibid.*

¹⁹⁶ The Japan-EC Committee of Keidanren conducted a poll of 925 member corporations on the 1992 EC market integration program. "How Japanese Business Looks at EC Market Integration - A Report on Results of Keidanren Poll," *Keidanren Review*, No. 120, December 1989, pp. 4-7.

¹⁹⁷ This survey was conducted between September 1989 and January 1990. See Roy Garner, "Japanese Investment: Prompted by a Global Outlook," *Financial Times*, June 5, 1990, p. 5.

in the EC is due to the Community's measures taken against Japan, which include stringent regulations on cut-price dumping, local content, and rules of origin.¹⁸⁸

Schengen Countries

The Schengen Agreement was signed in June 1985 by five countries¹⁸⁹ to get a headstart on the other EC member states in forming policies and judging the workability of the EC 92 proposed integration measures.²⁰⁰ Its aim is to eliminate all controls at their common borders covering the movement of people, goods, and services.²⁰¹ On April 27, 1990, the Schengen countries met for the first time since December 15, 1989, to negotiate a treaty to abolish border controls.²⁰² Negotiations had broken down in December when West Germany refused to sign an agreement unless East Germany was covered by it.²⁰³

In late November 1989, West Germany insisted that a provision be included to ensure that East Germany's 18 million citizens have free circulation throughout the entire Schengen Community.²⁰⁴ Initially, the other Schengen countries opposed the West German demand, but with the announcement that East Germany would become a member of the EC upon reunification with West Germany, the Schengen countries changed their position. At a May 17, 1990, meeting, the rest of the Schengen countries joined West Germany in allowing East German nationals free movement in all of the Schengen countries as of June 1. However, the agreement does not permit East Germans to take residence in France, Belgium, the Netherlands, or Luxembourg.²⁰⁵

¹⁸⁸ "EEC and Japan: Set Up or Stay Out," *The Economist*, Feb. 18, 1989, p. 52.

¹⁸⁹ The Schengen Agreement was signed by France, West Germany, Belgium, the Netherlands, and Luxembourg.

²⁰⁰ U.S. Department of State memorandum, "The Schengen Agreement: The EC Trendsetter for 1992," Nov. 14, 1988.

²⁰¹ "Movement of Persons: Five-Nation Pact Nears Stage; East German Visa Question Resolved," *1992-The External Impact of European Unification*, May 18, 1990, p. 1.

²⁰² "Free Movement: The Schengen Five Still Have Reservations About Eastern Europe," *European Report*, No. 1583 (May 2, 1990), sec. 4, p. 4.

²⁰³ USITC, *The Effects of EC Integration*, USITC Publication 2268, March 1990, p. 1-14.

²⁰⁴ *Ibid.*

²⁰⁵ "Schengen Convention: The Schengen Five Assimilate East Germany," *European Report*, No. 1588 (May 18, 1990), sec. 4, p. 8.

The decision to allow the free movement of East Germans was made contingent upon three clauses to be attached to the treaty. The first clause will define the area of free movement to include the current territory of East Germany. The second requires East Germany to guarantee the "watertightness" of its borders with Poland and Czechoslovakia. The third requires West Germany to keep the other Schengen countries informed about the progress of German reunification.²⁰⁶ Only 24 hours after this announcement, East Germany abolished its visa requirements for nationals from France, Belgium, Luxembourg, and the Netherlands, to take effect on June 1.²⁰⁷ These nationals can stay up to 3 months in East Germany without a visa. For longer visits, visas will be required.

On June 19, the five Schengen countries signed the accord. Ratification by all five National Parliaments is expected by the end of 1991.²⁰⁸ Under the agreement, the Schengen members undertake to abolish all checks on people travelling across their common borders and to enforce controls to a common standard at their frontiers with third countries. In return, the convention provides for legal and police cooperation as well as the creation of the Schengen Information System (SIS).²⁰⁹ The issue of bank secrecy for Luxembourg, which stalled negotiations in December 1989, seems to be settled.²¹⁰ Luxembourg has agreed to reveal depositors if they are suspected of organized crime.²¹¹

²⁰⁶ *Ibid.*

²⁰⁷ "Schengen Agreement: East Germany Opens Its Borders to the Five," *European Report*, No. 1590 (May 28, 1990), sec. 4, p. 1.

²⁰⁸ "Bonn Signs Accord Ending Border Checks for Five States," *The Week in Germany*, June 22, 1990, p. 2.

²⁰⁹ The SIS is a data base that is housed on a computer in Strasbourg. The data base will include information collected from the five countries on people for whom they have issued extradition orders, non-EC citizens they consider undesirable, people who are missing, and people cited in a judicial or regular police inquiry. "Movement of Persons: Five-Nation Accord Opens Borders to Citizens," *1992-The External Impact of European Unification*, June 29, 1990, p. 11.

²¹⁰ David Buchan, "Five Go Off to Schengenland," *Financial Times*, June 19, 1990, p. 18.

²¹¹ *Ibid.*

CHAPTER 2
REVIEW OF CUSTOMS UNION THEORY
AND RESEARCH ON THE 1992 PROGRAM

CONTENTS

	<i>Page</i>
Introduction	2-3
Customs union theory	2-3
Early research on the 1992 program	2-3
Recent research on the 1992 program	2-3
Merton Peck	2-4
Rudiger Dornbusch	2-5
Richard Baldwin	2-5
Vittorio Grilli	2-6
Dieter Helm and Stephen Smith	2-7
Peter Isard	2-7
References	2-8

CHAPTER 2

REVIEW OF CUSTOMS UNION THEORY AND RESEARCH ON THE 1992 PROGRAM

Introduction

This chapter reviews recent economic research that focuses on the expected impact of completing the integration of the EC internal market by December 31, 1992. Before this review the chapter discusses the underlying economic theory of market integration—customs union theory—and highlights the results of early research on the probable effects of the 1992 program.

Customs Union Theory

Customs unions are geographical trading areas wherein the member states reduce trade barriers among themselves and adopt common barriers against the rest of the world. The 1992 EC economic integration program contains elements of both reduced internal barriers and harmonized border policies against other, nonmember countries.

Economists have long assessed the effects of customs unions. As internal trade barriers are lowered, consumers in each member country find that imports from other member countries are now less expensive than both domestic products and imports from nonmember countries. Thus, consumers in each country may buy more imports from other member countries and decrease consumption of domestic products and nonmember imports. On the other hand, the creation of a customs union may result in an increase in trade with nonmember countries if the harmonized barrier against nonmember countries is lower than the average individual national barriers prior to the formation of the union. This increase in trade with nonmember countries will be at the expense of domestic production intended for domestic consumption.

The two primary trade effects of a customs union are (1) trade creation: the shift away from production for domestic consumption toward member imports and production for export to other member countries; and (2) trade diversion: the shift away from consumption of nonmember imports and from exports to nonmember countries in favor of trade with member countries.

This conventional dichotomy serves to highlight the gains to efficiency arising from trade creation, which shifts production toward low-cost producers, and the offsetting losses to efficiency arising from trade diversion, which shifts production away from low-cost producers. Whether, on balance, economic welfare increases or decreases depends on the relative strength of the two effects and has to be assessed empirically.

Finally, customs unions tend to enhance competition by creating a larger market under liberalized trading rules. By allowing production to migrate to relatively efficient locations, economies of scale and learning-curve effects are more readily realized in select industries—in particular, those industries that tend to have high fixed costs. The achievement of size-related economies is one of the chief rationales offered for the EC integration plans. Moreover, to the extent the customs union spurs additional economic growth related to scale or location economies, the member countries will become wealthier. This increase in wealth may, in turn, increase imports from nonmembers as EC consumers spend their additional income.

Since the United States is outside of the EC, measures that reduce internal barriers but leave external barriers unchanged cause trade diversion, that is, increased trade among EC member states at the expense of trade between the United States and the EC. Diversion hurts both U.S. export producers, who lose export markets in the EC, and U.S. consumers, who must compete against increased internal EC demand for European exports. U.S. import-substitution industries, however, benefit from trade diversion because European exports are diverted, to some extent, for internal EC consumption. On the other hand, measures that reduce the harmonized EC barriers against nonmember countries, including the United States, lower the price of U.S. goods in Europe and thus benefit U.S. exporters.

Early Research on the 1992 Program

Early research conducted for the EC Commission, commonly referred to as the Cecchini Report, predicts that the total gains from completion of the internal market would be an increase in EC GDP of between 3.2 and 5.7 percent, a reduction of inflation of between 4.5 and 7.7 percent, and an easing of domestic budget balances and trade balances of between 1.5 and 3.0 percent of GDP and between 0.7 and 1.3 percent of GDP, respectively, over the medium term (5 to 10 years). It is also estimated that the labor market would improve, with the creation of between 1.3 million and 2.3 million jobs in the EC as a whole over the medium term. However, it is expected that the unemployment rate would fall by only 1 to 2 percent in the medium term.

Recent Research on the 1992 Program

This section presents a review of recent economic research on the EC 1992 market-integration program. Much of this research focuses on the assumptions and results reported in the Cecchini Report. Several of the authors, Dornbusch, Grilli, and Peck, are skeptical about the magnitude of the projected welfare gains from completing the EC internal market. On the other hand, some researchers, such as Baldwin, believe

that since dynamic economic effects are ignored, the estimates presented in the Cecchini Report are too low. Although researchers disagree on the magnitude of the expected welfare gains from EC 1992, they all agree that completing the internal market will lead to positive real effects in the EC economy.

Merton Peck

In the paper "Industrial Organization and the Gains from Europe 1992," Merton Peck reviews the Cecchini Report. First he examines how the report arrives at its empirical estimates, and second, how it handles the looming problem of political cooperation among the EC member states. Peck also examines the impact of the EC 1992 program on U.S. firms operating in Europe.

Peck reviews the general methodology used in estimating the partial equilibrium results for the various sectors in the report. He does not dispute the fact that a single European market will raise real incomes in the EC. However, he believes that certain economic assumptions, limitations, and omissions make the Cecchini Report's estimates of the gains optimistic. To illustrate his apprehension regarding the magnitude of the gains projected for the 1992 program, Peck examines the results for the automobile sector.

Peck points out that the estimates for the automobile sector are significantly influenced by two economic assumptions. These assumptions include whether the firms behave as Cournot or Bertrand oligopolists and whether the market is assumed to be segmented or integrated.¹ (A Cournot oligopolist sets its output while taking the other firms' output as given; whereas a Bertrand oligopolist sets its price while taking the other firms' prices as given.) Given these two assumptions, Peck notes the wide range of estimates possible depending on which two assumptions are paired together. If the estimates are made assuming Cournot behavior and integrated markets, then the welfare gains are 12 billion ECU; for Cournot behavior and segmented markets the welfare gains are 1.33 billion ECU; for Bertrand behavior and integrated markets the welfare gains are 0.89 billion ECU; and for Bertrand behavior and segmented markets the welfare gains are 0.88 billion ECU. Peck is critical of the fact that the largest gains are reported given the wide range of estimates arrived at with different underlying assumptions. Moreover, he notes that the Cecchini Report does not specify the distribution of the welfare gains among the EC nations and assumes that the gains flow to consumers. He concludes that the Cecchini Report overestimates the gains of the 1992 program by a factor of two or three.

¹ If markets are assumed to be segmented, then firms will retain their market positions in their national markets. Alternatively, if markets are assumed to be integrated, then consumers are assumed not to prefer goods produced in their home market.

Peck questions the assumptions concerning the political obstacles of completing the 1992 program. Peck notes that a major source of the gains is the reorganization of European industry to take advantage of economies of scale. He argues that some nations will be losers in this process. For example, the simulations project that the United Kingdom will lose 46 of its 65 footwear firms, 31 of its 52 carpet firms, and 1 of its 3 automobile firms. Peck argues that an examination of industrial policy in Europe will reveal that National Governments do not sit idle while firms close, but rather initiate efforts to save some of the losers. Although the 1992 program has made efforts to restrain or forbid state subsidies, Peck believes that once one nation falters, others are likely to follow. He is also skeptical about the EC's ability to resolve the many differences in technical regulations and standards, and the likelihood of EC governments procuring from nonnational sources.

Peck notes that U.S. firms operating within the European Community should also benefit from the larger, integrated market. He points out that the elimination of border formalities should mean Community nations will not be able to single out products of U.S. firms manufactured in the EC from those manufactured by Community firms. In fact, many U.S. firms are already selling in most of the EC states and have Europe-wide marketing and production strategies. Peck contends that due to this European prominence, U.S. firms may actually be better positioned to take advantage of the single market.

Peck points out that U.S. firms may be at a disadvantage relative to EC firms in two areas: public procurement and research support. He contends that liberalization in public procurement is usually formulated to favor Community firms. Peck believes that given the difficulty an EC government has in procuring from a firm in a neighboring EC member, it is even more difficult to imagine them procuring from a non-EC firm, such as one from the United States. In the area of research and development, Peck notes that EC firms are also likely to be given preference for research support. He points out that the objective of EC R&D spending is to improve European competitiveness in high-technology industries relative to the United States and Japan.

Peck concludes his paper by making several observations. He believes that the Cecchini Report overestimates the microeconomic welfare gains of the EC 1992 program. He notes that the estimates are predicated on a certain set of assumptions that are unlikely to be implemented. Also, he points out that the Cecchini Report assumes that there will be no dramatic changes in the world economy as the EC implements its 1992 program. Even given these reservations, Peck believes that the central points of the Cecchini Report are accurate. Namely, that real incomes will rise, that some reorganization to realize economies of scale will occur, and that increased competition will result in many EC industries. Finally, Peck argues that the primary

obstacles to completing the market integration are political and if the members of the EC are committed to changing their past behavior, then the EC 1992 program might just succeed.

Rudiger Dornbusch

In the article "Europe 1992: Macroeconomic Implications," Rudiger Dornbusch examines the macroeconomic implications to the 1992 program estimated by the EC Commission. His assessment focuses on the sources of improved macroeconomic performance in the EC. Other areas explored in his paper are the prospects for European protectionism, the implications of financial integration, and the fiscal effects of the present exchange-rate system.

Dornbusch notes that the direct effects of the EC 1992 program, as estimated by the EC Commission, show a significant fiscal improvement. However, he wonders if these projections are plausible. For instance, he asks, Will EC governments be willing to use these additional resources for infrastructure or environmental improvements or will they use them to contain the buildup of public debt? He notes that in most European countries debt ratios have not stabilized and in some cases they are quite high. Therefore, he concludes that the assumption of increased government spending on such projects or tax reductions resulting from the benefits of EC 1992 may be optimistic.

Dornbusch also has doubts about the projections concerning employment gains in the EC. He notes that the EC Commission projects employment gains of between 1.8 million and 5.7 million jobs in the EC depending on macroeconomic policies. Dornbusch sees even 1.8 million new jobs, approximately a 1-percent gain in total employment, as an ambitious projection.² Moreover, the EC Commission's estimate does not allow for the fact that part of the output growth is due to productivity gains that result in lowering employment. Hence, he believes that the projected employment gains reported by the EC Commission are too optimistic.

Dornbusch addresses the question of whether the 1992 program will result in a more protectionist Europe. Or, more generally, he asks, Is EC 1992 good or bad for the rest of the world, in particular, the United States? Even without overt protectionist measures, Dornbusch expects EC 1992 will have some adverse effects on the rest of the world. For example, he notes that when border regulations are liberalized, the ease of shipping within the EC will bring about trade diversion at the expense of non-EC suppliers. He also wonders about the opening up of public procurement in the EC. He points out that it is one thing to allow cross-border competition in Europe, but it is quite another to open procurement to outside suppliers. Dornbusch

² An estimate by Dornbusch for the EC over the period 1961-88 found that a 5-percent increase in output is necessary for a 1-percent increase in employment.

argues that multinationals are currently making preemptive relocation decisions. The effect of these investments is to move production away from the rest of the world. He notes that once plants have located inside the EC, production has been relocated to the EC whether or not trade barriers are present.

Dornbusch believes that the "social dimension" of the 1992 program may ultimately lead to a higher level of protection. The social dimension of EC 1992 involves a harmonization of labor market arrangements. Currently, notes Dornbusch, cost disparities, unadjusted for productivity, are quite large. If these disparities are significantly reduced by increases in labor costs in the low-wage countries, then he believes that the low-wage countries will become uncompetitive relative to outsiders and will likely call for protection. Dornbusch expects that European protection, if it does occur, will be directed primarily at Asia rather than the United States.

Dornbusch argues that the formation of a European financial block will have a major impact on world financial markets because it will create a viable and perhaps attractive alternative to the U.S. capital market. Dornbusch is concerned what a convenient market for a mark (or equivalent) money market instrument will do to the dollar. He believes that the relative demand for dollar-denominated assets will decline. He also believes that the creation of a viable European asset competing in world financial markets portends significant depreciation for the value of the dollar in the 1990s.

Richard Baldwin

In the paper "On the Growth Effects of 1992,"³ Richard Baldwin argues that the greatest benefits of market liberalization are not in the one-time effects on resource allocation, but rather in its dynamic effects of more innovation, faster productivity gains, and higher growth rates for output and income. He notes that studies such as the Cecchini Report ignore these dynamic effects. Baldwin attempts to estimate the total impact of the EC 1992 program on EC Gross Domestic Product (GDP) by taking into account the above dynamic effects.

Baldwin notes that the theoretical portion of his model is relatively straightforward, whereas the quantitative part poses more problems. He points out that many results involve factors that are unobservable or have data that are unreliable. To alleviate this problem, Baldwin uses empirical methods introduced in recent economic research to estimate these parameters. Thus, he warns that his calculations are rough at best. Given these caveats, his analysis suggests two main points:

1. The Cecchini Report numbers significantly underestimate the economic benefits of

³ This paper and the following one, also by Baldwin, are quite technical in nature; therefore a brief review of this research is given here highlighting the basic results. See the text of these papers for a complete explanation of the theoretical models and accompanying econometrics.

1992, perhaps by as much as an order of magnitude; and

2. The long-term growth effects of 1992 could be very significant, adding between two-tenths and nine-tenths of one percentage point to the EC's long-term GDP growth rate.

Baldwin asserts that broad-based liberalization makes investment more profitable and leads to an endogenous rise in the equilibrium capital-to-output ratio. Therefore, he argues that incomes rise above and beyond the rise due to the initial static gain. He terms this indirect effect as a medium-term "growth bonus" since its size is proportional to the size of the static gain.

Baldwin argues that by ignoring the medium-term growth effects of EC 1992, previous studies have seriously underestimated the potential impact on EC GDP. His analysis suggests that the impact on EC GDP due to the 1992 program—including the medium-term dynamic effects—could be between 40 and 3,900 percent greater than current static estimates.⁴ Furthermore, his estimates suggest that the market integration could permanently add between one-quarter and one full percentage point to the EC growth rate. Baldwin concedes that the high ends of these ranges may be unrealistic, but he asserts that they reflect the fact that even small dynamic effects can lead to far larger gains than those when only static effects are investigated. He concludes by noting that the largest effects of liberalization programs, such as EC 1992, are likely to be dynamic not static.

In a related paper, "Measuring 1992's Medium-Term Dynamic Effects," Baldwin attempts to measure the gains to EC GDP due to one type of dynamic effect. The source of dynamic gain is straightforward. According to Baldwin, the rise in overall EC efficiency due to EC 1992 will raise the marginal product of capital in the EC. This will lead to an endogenous rise in the equilibrium capital stock. Hence, he argues that output rises more than the static effect. He finds by ignoring this dynamic effect that existing empirical estimates of the rise in EC GDP due to EC 1992 are between 30 and 136 percent too small. Thus, he estimates that 1992 will raise EC GDP between 3.1 to 25.4 percent over the medium term if this dynamic effect is taken into account.

Vittorio Grilli

In the article "Financial Markets and 1992," Vittorio Grilli explores the impact of the 1992 initiative on financial markets. He notes that the Cecchini Report estimates the gains from

⁴ This translates into a percent rise in EC GDP over the medium term (including the "growth bonus") of 2.86 to 9.29 percent as a lower bound and 80 to 260 percent as an upper bound. Baldwin bases these calculations on an EC Commission estimate of an increase in EC GDP of 2 to 6.5 percent over the medium term.

integrating financial markets are quite large, ranging from 11 billion ECU to 33 billion ECU. He is skeptical about these gains because the financial directives contain "safeguard clauses" that allow member states to suspend temporarily their obligations to liberalize their financial markets. Moreover, he notes, member states are also allowed to take protective measures in case of an emergency. He regards the decision to include safeguard measures as unwise for two reasons. First, uncertainty is generated about the commitment of the member states. Second, the temporary reintroduction of capital controls may not protect the monetary authorities against the speculative flow of funds.

Grilli questions the accuracy of the welfare gains estimated in the Cecchini Report. He notes that the welfare gains are measured by calculating the increase in consumer surplus that results from the equalization of the prices of financial services within the European Community. Grilli is skeptical that liberalization will result in a convergence of prices for financial products as assumed in the Cecchini Report. He points out that countries (such as West Germany and the United Kingdom) that are supposed to be large beneficiaries of the EC 1992 program due to increased competition already have the most liberalized financial markets in the Community. He argues that liberalization will not necessarily result in price equalization. In fact, he continues, financial markets may remain segmented and geographically separated even without formal controls and trade barriers. He contends that cross-country price comparisons may not be very meaningful. He notes that many banking products are bundled, so that it would be misleading to interpret the price differences of single products as evidence for potential gains from trade. Therefore, he argues, assuming the convergence toward the lowest prices in the EC would result in an overestimation of the consumer gains. He does not doubt that there will be gains, however, he believes that the available data are not sufficient to make reliable forecasts as to the size of the gains.

Grilli sees other problems that have yet to be resolved by the EC. They include banking secrecy, withholding taxes on bank deposits, and the level of bank reserves. Withholding tax rates on interest earned and dividends paid to nonresidents varies substantially by country in the EC. To further complicate matters, EC residents are treated as nonresidents in some EC states. Similarly, banking secrecy laws vary widely across the Community. Grilli points out that the EC is at a complete deadlock on the issues of taxation and secrecy, which raises further doubt about the extent of the benefits of the 1992 program. He also points out that a common level for bank reserves has not been agreed to for banks in the Community. He notes that cross-country disparities in the deposit and loan interest rates are partly due to the variation in reserve requirements across the Community.

Grilli concludes by noting that financial markets in Europe are highly regulated and distorted. He believes that the 1992 program will eliminate some of these distortions but that others will remain in place. He argues that an unambiguous evaluation of the welfare effects of the 1992 initiative is quite difficult.

Dieter Helm and Stephen Smith

In the paper "The Assessment: Economic Integration and the Role of the European Community," Dieter Helm and Stephen Smith consider the implications of the EC 1992 program in the context of policy functions between the member states and the EC. They divide the issues into areas concerning microeconomic policy and macroeconomic policy. The microeconomic issues they examine include competition policy, capital-market integration, and labor mobility. From a macroeconomic perspective, they review issues from an overall viewpoint.

Helm and Smith contend that the removal of physical and governmental barriers to competition may not, for example, be sufficient to encourage new entry into an industry. They note that in many markets characterized by oligopolistic structure, strategies exist for firms to deter entry and inhibit competition with or without economic liberalization. Moreover, they point out, in several markets firms have been merging with competitors ahead of complete implementation of EC 1992.

Helm and Smith note that capital-market integration would appear to imply a need for uniform tax treatment of the products in the financial sector. However, it is not clear to them whether the objective of such tax treatment is to achieve neutrality in investment decisions or to prevent tax evasion. On the issue of neutrality in investment decisions, they believe that the application of taxes on investment income should be according to the place of residence of the investors. On the other hand, if the objective is to prevent tax evasion, then they advocate a system of notification between EC revenue authorities in which the authorities are supplied with information concerning the amount of bank interest earned by EC residents. Helm and Smith advocate a system such as this as opposed to some sort of withholding arrangement.

On the issue of labor mobility in the EC, Helm and Smith argue that in the short-to-medium term, cultural and linguistic differences and diverse influences such as housing and labor unions effectively make labor in the EC a fixed factor. They point out that with fixed labor factors, the near term result of EC 1992 may be that production migrates to the cheapest source of labor supply. They note that high-cost labor countries such as West Germany may experience a loss of locational advantage to low-cost labor countries such as Greece or Spain.

In terms of overall macroeconomic policy, Helm and Smith point out that there are generally two schools of thought on the issue. The first school

argues that monetary integration should be imposed as the first step in the integration process. The monetary union would then constrain domestic macroeconomic policy, encouraging wider economic union. The second school argues that economic integration through completion of the internal market and coordinated macroeconomic policy must precede monetary integration. Therefore, they note that the first school is a Community-led collusive approach, and the second relies on the effects of the 1992 program to eventually work their way through to monetary integration.

Peter Isard

In the article "Corporate Tax Harmonization and European Monetary Integration," Peter Isard considers the question of how the success of monetary integration in Europe may depend on harmonizing the taxation of business profits. More specifically, he focuses on how fiscal conditions influence the choice of where to locate production facilities, and how other macroeconomic variables must change to be consistent with trade flows that are counterpart to net movements of physical capital. In the context of EC 1992, he notes that the dismantling of internal barriers to trade in goods and services could provide strong incentives, other things being equal, for firms to make direct investments in expanding markets and that the differential in corporate tax rates may strengthen or weaken these incentives.

Isard notes that the concept of harmonization is difficult to define precisely but has the general connotation of setting tax rates at levels that do not provide strong incentives for tax bases to shift from one tax jurisdiction to another. Hence, tax harmonization does not necessarily mean the absolute equality of tax rates among countries. Similarly, Isard continues, harmonization does not mean invariant tax rates, since adjustments to exogenous events may have different implications for different countries. Therefore, what may be required, in Isard's view, is an agreement on a set of broad understandings relating to the conditions under which, and the amounts by which, countries may adjust their tax rates to affect the relative attractiveness of locating productive facilities within their boundaries.

Isard concludes that the location of physical capital is affected by changes in fiscal conditions. For example, he points to changes in the differentials among the rates of corporate income taxation imposed by different countries or by divergent fiscal budget imbalances that fuel expectations of change in relative tax rates. He argues that this implies that it may be important for the EC to consider guidelines intended to discourage unharmonized changes in tax rates and undisciplined budget positions. Moreover, Isard sees this as an opportunity to promote internal stability in the EC by differentiating fiscal policies across countries to offset any destabilizing influences of exogenous shocks.

References

- Baldwin, Richard. "Measuring 1992's Medium-Term Dynamic Effects." NBER Working Paper Series, Working Paper No. 3166, National Bureau of Economic Research, November 1989.
- Baldwin, Richard. "On the Growth Effects of 1992." NBER Working Paper Series, Working Paper No. 3119, National Bureau of Economic Research, September 1989.
- Dornbusch, Rudiger. "Europe 1992: Macroeconomic Implications." *Brookings Papers on Economic Activity*, No. 2, (1989), pp. 341-362.
- Grilli, Vittorio. "Financial Markets and 1992." *Brookings Papers on Economic Activity*, No. 2, (1989), pp. 301-324.
- Helm, Dieter and Stephen Smith. "The Assessment: Economic Integration and the Role of the European Community." *Oxford Review of Economic Policy*, vol. 5, (Summer 1989), pp. 1-19.
- Isard, Peter. "Corporate Tax Harmonization and European Monetary Integration." *Kyklos*, vol. 43, (1990), pp. 3-24.
- Peck, Merton. "Industrial Organization and the Gains from Europe 1992." *Brookings Papers on Economic Activity*, No. 2, (1989), pp. 277-299.

CHAPTER 3
U.S. TRADE AND INVESTMENT IN THE EC

CONTENTS

	<i>Page</i>
Developments covered in the previous followup report	3-3
Trade	3-3
Investment	3-3
Developments since the first followup report	3-4
Trade with the EC	3-4
Introduction	3-4
Analysis of trends in EC trade	3-4
Internal EC trade	3-4
Trade Relations with Eastern Europe	3-4
Investment	3-4
U.S. direct investment in the EC	3-4
Foreign direct investment in the United States	3-5
Analysis of trends in investment	3-7
Trends in EC direct investment	3-7
Government support for investment	3-7
Investment support	3-7
Programs for investment	3-8
Support for Eastern Europe	3-8
Mergers, acquisitions, and joint ventures	3-8
Analysis of effects of integration on private investment	3-9
 Tables	
3-1 U.S. direct investment position abroad, by partner and by industry sector, at yearend 1988 and 1989	3-5
3-2 Foreign direct investment position in the United States, by partner and by industry sector, at yearend 1988 and 1989	3-6
3-3 Mergers and acquisitions in the EC, involving the top 1000 European firms and firms with sales over 1 billion ECU, by industry, 1985-87	3-9

CHAPTER 3 U.S. TRADE AND INVESTMENT IN THE EC

Developments Covered in the Previous Followup Report

Trade

The U.S. trade balance for all commodities traded between the United States and the EC was a deficit of \$1.5 billion during 1989. This figure compares favorably with a deficit of \$12.7 billion recorded in 1988 and indicates a substantial reduction of the U.S. trade deficit with the EC in 1989.

The individual SITC divisions that provided the largest impact on the current trade balance were U.S. exports of Office Machines and Automated Data Processing Equipment (SITC division 75), as well as various other SITC divisions (79, 87, and 22) encompassing primarily manufactured goods. Exports of Office Machines and Automated Data Processing Equipment, which exceeded imports by about \$8.0 billion, provided the greatest trade surplus with the EC during 1989. Road vehicles (SITC division 78) provided the greatest trade deficit primarily as a result of U.S. imports of automobiles from West Germany, the United Kingdom, and Italy.

EC imports from Eastern Europe, as defined by the country grouping of Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and the Soviet Union, fluctuated between 1984 and 1987. EC imports from these countries decreased from \$28.3 billion in 1984 to \$25.0 billion in 1986 before increasing to the 1987 level of \$28.0 billion. The overall decrease recorded in imports for 1984-87 was about 1 percent. The largest supplier in this country grouping was the Soviet Union, which accounted for slightly more than 53 percent of total imports. The next largest supplier was Poland, which supplied 12 percent of total EC imports from Eastern Europe.

EC exports to the Eastern European countries amounted to \$17.3 billion in 1984, rising significantly to \$22.1 billion in 1987. Exports increased by 27 percent during this period, or by an average of about 9 percent per year. In 1987, exports to the Soviet Union made up 48 percent of total EC exports to Eastern Europe. Hungary, Poland, and Czechoslovakia each received 11 to 13 percent of total EC exports to Eastern Europe.

Investment

As a result of investment growth, EC member states as a group experienced a GNP growth rate of 3.5 percent in 1989. Studies sponsored by the EC Commission indicate that the elimination of physical, technical, and fiscal barriers within the EC will result in GNP growth, the creation of new jobs, and consumer price decreases. As economies throughout the EC grow, governments are expected to spend more on telecommunications, power generation, and transport, with the largest growth and investment expected in the electrical and heavy engineering sectors.

Overall, U.S. direct investment in Europe made up approximately 47 percent (\$126.5 billion) of total U.S. direct investment abroad in 1988. U.S. direct investment in other industrialized nations made up a sizable proportion of total foreign direct investment, including Canada (18 percent, or \$61.2 billion) and Japan (5 percent, or \$16.9 billion). Foreign investment, then, does not seem largely limited to developing countries as a means of shifting production to lower cost areas of the world. Total U.S. direct investment in developing countries, as designated by the Bureau of Economic Analysis, amounted to 24 percent, or about \$76.8 billion, in 1988.

U.S. direct investment in the 12 EC member states, \$131.1 billion (revised) in 1988, represented an increase of 9 percent from \$120.1 billion in 1987. Growth in U.S. direct investment in the EC was slightly less than the overall U.S. direct investment growth rate of 6 percent. The largest levels of investment were in the United Kingdom (\$49 billion) (revised), West Germany (\$22 billion), and the Netherlands (\$16 billion) (revised). The U.S. direct investment position in the EC was the greatest in the area of manufacturing, reaching a level of \$68 billion (revised), about 1 percent higher than the 1987 position. Direct investment in manufacturing in 1988 made up approximately 52 percent of total U.S. direct investment in the EC, followed by Finance and Insurance (\$22.8 billion (revised), 17 percent of total), and Petroleum (\$15.5 billion (revised), 12 percent of total).

Direct investment in the United States by the 12 EC member states attained a level of \$193.9 billion in 1988, or 59 percent of total foreign direct investment in the United States. Among the EC member states, the largest foreign direct investment position was held by the United Kingdom (\$101.9 billion, or 53 percent of total EC investment), followed by the Netherlands (\$49 billion, or 25 percent of total EC investment) and West Germany (\$23.8 billion, or 12 percent of total EC investment). The foreign direct investment position held by the EC in 1988 was over three times the position held by Japan (\$53.4 billion, or 16 percent of total foreign direct investment) and

over seven times that of Canada (\$27.4 billion, or 8 percent of total).

Developments Since the First Followup Report

Trade With the EC

Introduction

Two significant trends both in current and future development of trade in the EC are changes in internal EC trade and EC trade with Eastern Europe. Although internal EC trade is continuing a trend observed in the last 5 years, other developments external to the EC could have significant impact on this trend. One such trend is trade with Eastern Europe, that may become a more significant factor in overall EC trade, depending upon EC directives which may aid the development of economic policy and infrastructure in Eastern Europe which would in turn promote a market economy.

Analysis of Trends in EC Trade

Internal EC Trade

A recent study analyzing effects of integration of the European market examined the issues and developments surrounding patterns of intra-EC trade and the resulting gains from such trade. Producers who specialize in certain sectors of industry within member countries would cause greater levels of intra-country trade for that industry sector. Areas where the greatest gains would likely occur are in the highly specialized electronics and pharmaceuticals sectors.¹

The historical trends of intra-EC trade as a percentage of EC world trade were covered in the first followup ITC report.² In a discussion of the likelihood of a "Fortress Europe" arising as a result of an increasing percentage of intra-EC trade, a recent study has stated that intra-EC trade has risen to about 57 percent of total EC trade, largely as a result of a reduced share of EC oil imports since the OPEC oil price decline. Overall EC trade rose during the 1980s largely due to increased EC import penetration by rapidly growing sectors of manufacturing, as well as continuing penetration by slower growing manufacturing sectors. It has been speculated that over a much longer period of time a rise in import penetration by faster-growing, higher technology industries may lead to an increasing external import dependence on such

¹ Luigi Bocconi Commercial University President Fabrizio Onida, paper presented at the Conference of the American Enterprise Institute for Public Policy Research at Washington, DC, Mar. 5-8, 1990.

² U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States—First Follow-Up Report* (Investigation No. 332-267), USITC Publication 2268, March 1990, pp. 3-4 to 3-5.

higher technology products, and thus reduce the likelihood for a "Fortress Europe."³

Further, the study suggests that the idea of "Fortress Europe" is wanted by only a few European producers. These producers, often in infant industries, may seek protection against imported products that compete directly with their own while attempting to lower costs for any basic or intermediate goods required for their production processes. The result for many sectors of industry is an unstable set of conflicting interests of protection against end-product competition but ease of obtaining basic or intermediate materials used to make the final product.⁴

EC Trade Relations With Eastern Europe

EC experts recently completed an economic assessment on reforms that are currently under way in Eastern and central Europe. A focus of the assessment was some of the specific problems arising as Eastern Europe moves away from a centrally planned economy towards to a market-oriented system. The EC has advocated that Eastern and central Europe implement some broad policy reforms that would ensure economic progress. These policy reforms form part of a recommended integrated package dependent on establishing relationships with Eastern European governments and concentration of resources in certain areas to attain central objectives.

Some policy recommendations were based on the need for Eastern European countries to improve their access to the international market. The EC noted that stabilization of the economies of Eastern Europe could be achieved in some part through improving budgetary controls and eliminating financing through expanding the money supply. Fiscal reform through the administration of taxes and subsidies was also suggested. Also noted was the possibility of establishing exchange rates between Eastern European currencies and the ECU as part of a wider stabilization program.⁵

Investment

U.S. Direct Investment in the EC

U.S. direct investment abroad, as a measure of U.S. private assets held in foreign markets, was at a level of \$333.5 billion in 1988 (table 3-1). Increases in the direct investment position in 1988 totalled nearly \$40 billion, resulting in a cumulative total of \$373.4 billion in 1989, or an increase of almost 12 percent. The 1989 rate of increase was greater than that recorded in 1988, particularly due to sustained economic growth overseas, especially in Europe and in the Far East. Overseas interest rates also rose, narrowing the gap between U.S. and

³ Fabrizio Onida paper.

⁴ Ibid.

⁵ "EEC/Eastern Europe: Commission Experts' Economic Analysis on Reform Process Sees Central Role for ECU," *European Report*, No. 1585 (May 9, 1990), pp. 2-3 to 2-4.

Table 3-1
U.S. direct investment position¹ abroad, by partner and by industry sector, at yearend 1988 and 1989
(In millions of dollars)

Partner	All industries	Petro- leum	Manu- facturing	Whole- sale trade	Bank- ing	Fi- nance	Real estate	Other services
1988 ²								
European Community:								
Belgium	7,448	513	3,917	1,791	427	569	195	36
France	13,150	957	8,749	2,132	241	598	184	288
Italy	9,540	496	6,933	1,144	262	477	170	56
Luxembourg	850	3	552	5	204	85	0	0
Netherlands	16,017	2,306	6,163	2,312	173	3,529	1,102	432
West Germany	21,742	2,296	14,018	1,140	1,372	2,155	(29)	791
United Kingdom	49,274	8,628	19,739	2,246	3,036	13,499	1,351	774
Other EC	13,094	338	8,181	1,430	716	1,928	1,736	120
Total, EC	131,115	15,537	68,252	12,200	6,431	22,840	3,358	2,497
Canada	62,610	11,679	28,859	3,516	778	10,868	1,272	5,638
Japan	17,927	3,356	8,941	3,485	263	1,291	224	366
All countries	333,501	57,745	139,584	33,812	19,072	60,477	7,786	15,025
1989								
European Community:								
Belgium	8,290	502	4,407	1,945	335	796	267	38
France	14,747	1,050	9,490	2,531	211	872	275	318
Italy	10,634	574	6,830	1,417	281	1,055	189	288
Luxembourg	904	5	543	6	253	97	0	0
Netherlands	17,168	1,907	7,541	2,471	177	3,798	1,088	185
West Germany	23,059	2,600	14,430	1,285	1,456	2,515	(46)	820
United Kingdom	60,810	10,063	22,097	2,464	2,884	20,599	1,748	955
Other EC	14,363	333	9,555	1,611	889	1,445	408	122
Total, EC	149,975	17,034	74,893	13,730	6,486	31,177	3,929	2,726
Canada	66,856	10,912	32,333	3,917	945	11,680	1,385	5,684
Japan	19,341	3,194	9,959	3,381	214	1,981	248	363
All countries	373,436	57,945	155,704	37,735	19,875	77,112	8,812	16,253

¹ Direct investment as measured by valuation adjustments plus capital outflows. Capital outflows are defined as the net equity capital plus reinvested earnings plus net intercompany debt. The overall position is also generally regarded as the book value of U.S. direct investors' equity in, and net outstanding loans to, their foreign affiliates. A foreign affiliate is a foreign business enterprise in which a single U.S. investor owns at least 10 percent of the voting securities, or the equivalent.

² Revised.

Source: Official economic data compiled from U.S. Department of Commerce BEA statistics.

foreign interest rates. Because of the strong economic growth, higher overseas earnings were available to many overseas affiliates of U.S. parents, allowing for a higher percentage of foreign affiliate's earnings to be reinvested.

Overall, U.S. direct investment in the EC made up approximately 40 percent (\$150.0 billion) of total U.S. direct investment abroad in 1989. U.S. direct investment in other industrialized nations made up a sizable proportion of total foreign direct investment, including Canada (18 percent, or \$66.9 billion) and Japan (5 percent, or \$19.3 billion). U.S. direct investment in Canada and Japan as a percentage of total investment did not change appreciably from 1988 levels.

U.S. direct investment in the 12 EC member states of \$150.0 billion in 1989, represented an increase of 14 percent from \$131.1 billion in 1988. Growth in U.S. direct investment in the EC, therefore, was slightly greater than the overall U.S. direct investment growth rate of 12 percent. The largest levels of investment were in the United Kingdom (\$60.8 billion), West Germany (\$23.1

billion), and the Netherlands (\$17.2 billion). The U.S. direct investment position in the EC was the greatest in the area of General Manufactures, reaching a level of \$75 billion, an increase of about 10 percent from the 1988 position. Direct investment in General Manufactures in 1989 made up approximately 50 percent of total U.S. direct investment in the EC, followed by Finance and Insurance (\$31.2 billion, 21 percent of total), and Petroleum (\$17.0 billion, 11 percent of total).

Foreign Direct Investment in the United States

New foreign direct investment in the United States in the form of capital outlays by foreign countries increased by 11 percent from \$65 billion in 1988 to \$72 billion in 1989, according to statistics reported by the BEA. The strong growth in new outlays primarily reflected the large number and size of acquisitions of new U.S. affiliates, and repayment of loans to U.S. financial affiliates by foreign parent companies. The existing U.S. affiliates of foreign companies also experienced

improved performance, further contributing to the increase.

The total foreign direct investment position in the United States in 1989 was at a level of \$400.8 billion for all industries (table 3-2). Of this figure, direct investment by the 12 EC member states was \$234.8 billion in 1989, or 59 percent of the total. Among the EC member states, the largest foreign direct investment position was held by the United Kingdom (\$119.1 billion, or 51 percent of total EC investment), followed by the Netherlands (\$60.5 billion, or 26 percent of total EC investment) and West Germany (\$28.2 billion, or 12 percent of total EC investment). The foreign direct investment position held by the EC in 1989 was over three times the position held by Japan (\$69.7 billion, or 17 percent of total foreign direct investment) and over seven times that of Canada (\$31.5 billion, or 8 percent of total).

The largest areas of investment by the EC in the United States continue to be in manufacturing, wholesale trade, and petroleum. The foreign direct investment position attained by the EC in manufacturing was \$79.5 billion in 1988 and increased by 40 percent to \$106.4 billion in 1989. The investment position held by the EC in the area of wholesale trade increased by 33 percent from a level of \$32.9 billion in 1988, to \$36.5 billion in 1989. The investment position in petroleum reached \$30.2 billion in 1989, decreasing by 3 percent from the 1988 figure of \$31.2 billion. Changes in the major industrial categories as compiled by the BEA are due primarily to increased equity capital flows into the United States by the United Kingdom and the Netherlands, although reinvested earnings declined, particularly in the petroleum and chemicals manufacturing sector.

Table 3-2
Foreign direct investment position¹ in the United States, by partner and by industry sector, at yearend 1988 and 1989

(In millions of dollars)

Partner	All Industries	Petro- leum	Manu- facturing	Whole- sale trade	Bank- ing	Fi- nance	Insu- rance	Real estate	Other services
1988									
European Community:									
Belgium	4,024	(²)	989	695	34	56	(³)	12	(²)
France	11,364	(²)	9,908	520	687	(764)	139	95	(²)
Italy	667	(²)	107	515	446	(²)	(²)	(²)	(²)
Luxembourg	525	(²)	346	(²)	12	15	0	10	46
Netherlands	48,991	(²)	17,153	5,153	2,729	3,190	4,685	3,340	(²)
West Germany ..	23,845	172	13,268	6,851	293	(626)	1,776	1,079	1,034
United Kingdom ..	101,909	18,779	37,021	18,647	3,669	870	6,863	5,323	10,737
Other EC	2,587	(²)	733	(²)	935	(²)	(²)	(²)	(²)
Total, EC	193,912	31,169	79,525	32,898	8,804	1,745	13,535	10,016	16,220
Canada	27,361	1,614	9,391	3,513	1,458	600	2,993	4,169	3,624
Japan	53,354	(79)	12,222	18,736	3,895	2,863	(²)	10,017	(²)
All countries	328,850	34,704	121,434	64,929	17,453	2,124	20,252	31,929	36,024
1989									
European Community:									
Belgium	4,534	(²)	1,205	872	35	26	(³)	28	(²)
France	16,375	(²)	13,916	763	870	(468)	134	73	(²)
Italy	1,586	(²)	264	494	506	(²)	(²)	(53)	(²)
Luxembourg	935	(²)	94	89	8	198	0	512	(²)
Netherlands	60,483	10,660	24,101	5,550	3,148	4,507	5,266	3,410	3,842
West Germany ..	28,223	250	15,232	7,393	699	(351)	2,089	1,173	1,737
United Kingdom ..	119,137	16,811	50,704	21,013	3,748	822	7,222	5,234	13,584
Other EC	3,519	73	896	373	1,405	(²)	(²)	209	202
Total, EC	234,794	30,244	106,411	36,548	10,420	4,903	14,787	10,586	20,896
Canada	31,538	1,679	11,586	3,189	1,493	876	3,483	3,921	5,310
Japan	69,699	68	17,255	21,005	4,441	5,830	(²)	14,294	(²)
All countries	400,817	35,089	160,216	71,350	19,581	11,403	22,713	35,853	44,611

¹ Direct investment as measured by valuation adjustments plus capital outflows. Capital outflows are defined as the net equity capital plus reinvested earnings plus net intercompany debt. The overall position is also generally regarded as the book value of U.S. direct investors' equity in, and net outstanding loans to, their foreign affiliates. A foreign affiliate is a foreign business enterprise in which a single U.S. investor owns at least 10 percent of the voting securities, or the equivalent.

² Suppressed to avoid disclosure of data of individual companies.

³ Less than \$500,000.

Source: Official economic data compiled from U.S. Department of Commerce BEA statistics.

EC member states as a group are forecast to experience a nominal GNP growth rate of 3 percent in 1990.⁶ Although somewhat lower than growth rates of 4 to 6 percent recorded in prior years, this rate is still higher than the average level recorded during 1982-84. Due to some tightening of policies and some deceleration of demand, investment is not expected to increase as in prior years. However, investment is expected to continue growing at the rate of about 5 percent during 1990. In addition, exports are expected to increase by about 6 percent over 1989.⁷

Analysis of Trends in Investment

Trends in EC Direct Investment

Recent reports⁸ indicate that the EC experienced an improved economy in 1989 and continues to experience more rapid economic growth than in the past 20 years. Total intra-EC investment averaged a drop of about 0.1 percent from 1982 to 1984. The average increase in investment during 1985-87 was 3.6 percent per year, followed by an increase of 8.4 percent in 1988 and 7 percent in 1989. Investment is expected to grow by 4.75 percent during 1990.

A recent study on the integration of the European market discussed the role of intra- and extra-EC direct investment.⁹ The industrial restructuring in preparation for 1992 is believed to have caused greater flows of intra-EC direct investment. Although the EC is and likely will be more integrated than in the past, many physical barriers, such as national borders and language still exist. Firms in the EC presently place greater emphasis on strengthening marketing positions. A greater effort to coordinate marketing efforts will tend to lower operations of diversified or multiplant operations in the EC. This slowdown in operations results in faster flows of information and ultimately reduces any cultural and national barriers to trade. The recent prospect of the consideration of other non-EC-member countries, especially Eastern European nations, for some preferential treatment, is believed to spur growth in areas where local resources, such as low-cost labor, abound.

In addition to increased intra-EC direct investment, greater investment would likely occur from outside the EC. U.S. and other foreign multinational firms are typically well-established in the EC, and U.S. parent companies may relocate EC production to exploit certain local advantages.

⁶ Council Decision of 21 December 1989 Adopting the 1989 to 1990 Annual Report on the Economic Situation in the Community and Economic Policy Guidelines To Be Followed in the Community for 1990, Com(89) 685, pp. 5-7.

⁷ "Total Foreign Investment in US Tops American Investment Abroad," *EC Business Report*, vol. 2, No. 4, pp. 19-20.

⁸ Council Decision Adopting the Annual Report, Com(89) 685, pp 5-7.

⁹ Luigi Bocconi Commercial University President Fabrizio Onida, paper presented at the Conference of the American Enterprise Institute for Public Policy Research at Washington, DC, Mar. 5-8, 1990.

Government Support for Investment

Investment Support

Government-supported financing within the EC in 1989 reached a total of nearly 14.9 billion ECUs (\$12.9 billion). This level represents a change of 33 percent from a total of 11.1 billion ECU lent in 1988. Approximately 7 billion ECU were distributed under the Regional Development EC program objective in 1989. Other EC program objectives, such as Community Infrastructure (2.7 billion ECU), Environment and Quality of Life (1.7 billion ECU), and Energy (1.7 billion ECU) also were major development categories in 1989.¹⁰

The activity of the European Investment Bank (EIB)¹¹ increased during 1989 and for the first part of 1990. The Bank, which funds development projects in the EC and in other countries, distributes principally within the EC and other associate countries located in the Caribbean, African, and Pacific areas of the world. The activity of the EIB, measured both in terms of the number of loans and the scope of lending, increased to an all-time high of 12.25 billion ECU, representing a 20 percent increase from 1988. The Bank now ranks among the world's largest lending and borrowing institutions.¹²

Of the 12.25 billion ECU lent out by the EIB, approximately 11.6 billion ECU was received by the EC and 612 million ECU was loaned to associate countries. Development of small- and medium-sized businesses, the so-called Small and Medium Enterprises and Small and Medium Companies (SMEs and SMCs) continue to be a priority for the EIB, as 36 percent of monies destined for regional development were made to SMCs and SMEs.

The EIB is currently working on preparations for the creation of the European Bank Reconstruction and Development Bank (EBRD). This bank will be used to provide financing to Eastern European countries in order to boost or to help restructure the market economy. In the short term, officials of the EIB expect that much of the Bank's activities will concentrate on the EC member states, with some consideration given to associate countries and sustained support for Eastern European countries.

The maximum lending capacity of the EIB may not exceed two and-one half times its capital. Because the lending activity of the EIB has increased rapidly over the past few years, the Finance Ministers of the EIB have approved capital increases. On February 20, 1990, the vice president of the EIB indicated that it is currently necessary to make the EIB more effective in EC development and

¹⁰ "European Investment Bank: Record Lending Activity in 1989," *European Report*, No. 1562 (Feb. 10, 1990), sec. 2, p. 3.

¹¹ For a discussion of the history behind the European Investment Bank, see "Trade and Investment," ch. 3 of *Effects of EC Integration*, USITC Publication 2268, March 1990.

¹² "European Investment Bank: Record Lending Activity in 1989," p. 3.

to allow for increased lending activity. Finance Ministers are expected to raise the bank capital from 28.8 billion ECU to 57.6 billion ECU. With the additional capital, lending activity may increase to the EC and to associate African, Caribbean, and Pacific countries, as well as to Eastern Europe.¹³

Programs for Investment

The recent adoption of proposals concerning a new framework program for development of the EC has placed additional emphasis on research and technological development. As a result, six specific programs related to research and technological development were identified for investment. These include information and communications technologies (3 billion ECU), industrial and materials technologies (1.2 billion ECU), environment (700 million ECU), life sciences and technologies (1 billion ECU), energy (1.1 billion ECU) and human capital and mobility (700 million ECU). The proposed new framework program is scheduled for implementation during 1991-94.¹⁴

The EC Commission recently adopted a list of regions under an objective of promoting the development of rural areas. The EC is expected to adopt a series of projects to fund rural development. The European Social Fund, European Regional Development Fund, and the EACGF-Guidance were granted with 2.943 billion ECU for the period 1989-93 in order to fund development. Targeted areas include the development of primary agriculture, forestry, and fisheries industries by assisting in the diversification of production. Other areas include assisting the development of small and medium-sized firms in rural areas, tourism, and recreational activities, as well as the development of rural infrastructures.¹⁵

The EC has also introduced a new program to label private European financial investment firms as "Eurotech Capital," so that the firms may gain recognition in the EC as an EC-backed and "approved" company. The qualifications of the investment firm are based on certain requirements. The privileged label "Eurotech Capital" is assigned to a financial company that has a minimum investment capability of 50 million ECU and is willing to invest at least 20 percent of this in firms involved in high technology projects. Preferably the firms should be transnational small or medium-sized. A financial firm that has the "Eurotech Capital" label can effectively invest more in the high-technology, higher risk projects because of additional backing by the EC. In addition, the firm is entitled to use two high-technology product

information databases, Eurotech Project and Eurotech Data.¹⁶

Support for Eastern Europe

In a recent EC economic assessment,¹⁷ the necessity of certain economic policies that would encourage investment was asserted. A vital point stressed by the EC was the establishment of a strong independent central banking system to avoid rising inflation in Eastern Europe. As Eastern Europe is introduced to a market-based economy, restraints on the money supply would stimulate savings and maintain positive interest rates. The central bank would also establish efficient financial services to accompany newly established money and capital markets.

A conclusion of the assessment was the recommendation of the introduction of a 'sequencing' system, which would aid the establishment of market economies by staging the liberalization of economic reforms. Some harmful side effects such as a high inflation rate and distorted income levels could be avoided or reduced. The report warned that long-term goals of economic reform should not be sacrificed to obtain short-term objectives.

The study also noted that the EC and other western countries could play a vital role in the conversion of Eastern Europe to a free economy. Involvement of western governments would ultimately attract private investment, the study maintains. The EC has already laid some foundation for assistance to Eastern Europe with the administration of loans through the European Bank for Reconstruction and Development. Such funding extends to areas such as improved medical aid, food, and agricultural project assistance. The EBRD is also supportive of project loans in areas such as the environment and industrial renovation, as well as direct assistance dealing with exchange-rate difficulties and balance of payments.

Mergers, Acquisitions, and Joint Ventures

A recent compilation of data shows the number of mergers and acquisitions that have resulted primarily due to the international integration of the EC market (table 3-3). Among the top 1,000 European firms, total mergers and acquisitions reached 383 during 1987, representing an increase of 26 percent from 1986 and an increase of 68 percent from 1985. The greatest number of acquisitions during 1987 was in the chemical industry, amounting to a total of 85, followed by acquisitions in the food industry (51) and metal manufacturing (40). Other important sectors of industry that experienced fairly large numbers of acquisitions among the top 1,000 European firms were the electrical and electronics (36); machinery (38);

¹³ "European Investment Bank: Bank Capital Set to Double," *European Report*, No. 1566, (Feb. 24, 1990), sec. 2, pp. 2-3.

¹⁴ European Communities, Economic and Social Committee, *Economic and Social Consultative Assembly Bulletin*, No. 11, 1989, pp. 4-13.

¹⁵ "Rural Development: 2.5 Billion ECUs for Rural Areas," *European Report*, No. 1581, (Apr. 25, 1990), sec. 4, p. 9.

¹⁶ "SMES: European Commission Issues First 'Eurotech Capital' Label," *European Report*, No. 1573, (Mar. 21, 1990), sec. 3, p. 11.

¹⁷ "EEC/Eastern Europe: Commission Experts' Economic Analysis on Reform Process Sees Central Role for ECU," *European Report*, No. 1585 (May 9, 1990), pp. 2-3 to 2-4.

Table 3-3

Mergers and acquisitions in the EC, involving the top 1000 European firms and firms with sales over 1 billion ECU, by industry, 1985-87

Industry	Mergers and acquisitions involving the top 1,000 European firms			Mergers and acquisitions involving firms with sales over 1 billion ECU		
	1985	1986	1987	1985	1986	1987
Food	34	52	51	17	35	40
Chemicals	57	71	85	33	51	57
Electrical and electronics	13	41	36	9	12	23
Machinery	29	31	38	17	20	26
Computers	1	2	3	0	1	3
Metal manufacturing	17	19	40	4	11	32
Vehicles	10	21	15	3	11	14
Wood, paper, and furniture	27	25	34	5	8	18
Mining	10	9	12	7	4	9
Textiles, clothing, and footwear	9	6	14	2	2	4
Building	14	9	33	8	11	29
Other	6	7	22	3	5	13
Total	227	303	383	108	171	268

Source: EEC, 1989.

wood, paper, and furniture (34); and construction (33) industries.

Of a total of 268 mergers and acquisitions in 1987 involving EC firms with sales over 1 billion ECU, 57, or 21 percent were in the chemical industry sector, with a somewhat smaller number of acquisitions in the food industry (40) and metal manufacturing industry (32). Together, these three industry sectors made up approximately 49 percent of all merger and acquisition activity in 1987.¹⁸

Recent data indicate that the total number of EC-Eastern Europe joint ventures currently numbered about 2,760 in 1989.¹⁹ Over 1,000 joint ventures were created between EC-based firms or subsidiaries and the Soviet Union. Approximately 12 percent of these EC-Soviet joint ventures were above the equivalent of \$7 million, and 65 percent were below \$1.4 million. Large numbers of joint ventures were also recorded in that year for Hungary (608) and Poland (411). The EC-based firms with highest rates of participation were those based in West Germany, which formed 15 percent of total joint ventures, and Italian-based firms, that formed 5.7 percent of total joint ventures. Firms that operate in the EC but are U.S.-based formed 9.3 percent of total EC-Eastern Europe joint ventures, and those that are subsidiaries of Austrian firms formed 5.7 percent of the total.

Analysis of Effects of Integration on Private Investment

A recent study of the impact of the 1992 integration on investment analyzed short-term

effects associated with reactions of firms to the integration of the EC market, as well as some medium-term effects resulting from the implementation of directives related to investment.²⁰ In the short-term analysis, 31 percent of industrial firms surveyed expected that completion of the internal market would have favorable effects on investment. Rapid increases in investment occurred in 1988 and 1989 over prior years, leading to speculation that this may have been caused by anticipation of passage of EC directives related to investment. Expected increases in total private investment due to an internal market effect were compared with expected increases using the investment function of the Compact model. The results suggest that anticipation of 1992 by businesses accounts for a 17-percent growth in private investment.

Medium-term effects were measured using simulation based on the assumptions that (1) abolition of frontier controls and the removal of controls on public procurement would not have an effect before 1993, and that (2) the effects of financial services would be felt from 1990 onwards. Lastly, the reactions of firms in the new environment was assumed to be in progress. Based on the EC Compact model, the macroeconomic effects of the integrated market should aid in the growth of private investment by 5.6 percent in 1993. The average annual growth in private investment should be about 6.3 percent. Based on comparisons between investment with and without the effect of 1992 integrations, the resulting forecasts call for a growth in private investment by at least 1 percent per year during 1990-95.

¹⁸ Fabrizio Onida paper.

¹⁹ European Communities Communications Corporation, "Joint Ventures with Eastern Europe...", *Europe 92*, vol. 1, issue 4, p. 2.

²⁰ European Communities, Directorate-General for Economic and Financial Affairs, *European Economy*, No. 42, 1989, pp. 201-202.

PART II
ANTICIPATED CHANGES IN THE EC AND
POTENTIAL EFFECTS ON THE UNITED STATES

CHAPTER 4
STANDARDS, TESTING, AND CERTIFICATION

CONTENTS

	<i>Page</i>
Developments covered in the previous reports	4-7
Background and anticipated changes	4-7
Possible effects	4-8
Part 1. Overall developments in testing and standards during the first 6 months of 1990	4-8
Introduction	4-8
Overview	4-8
Standards development	4-9
The Green Paper on standards	4-10
Background	4-10
Recommended changes	4-11
EC reaction	4-12
U.S. reaction	4-12
Next steps	4-12
Bilateral discussions	4-13
ANSI meeting	4-13
Sardinia meeting	4-13
U.S. views	4-13
EC views	4-13
Multilateral discussions	4-14
EC views	4-14
U.S. views	4-14
Domestic considerations	4-15
Strengths of the U.S. system	4-16
Shortcomings of the U.S. system	4-16
The roles of the private sector and government	4-16
Prospects	4-17
Standards for public procurement	4-18
Testing and certification	4-19
Nonregulated products	4-19
Structure	4-19
The Council	4-19
Specialized committees	4-20
Sectoral committees and agreements groups	4-20
Operation	4-20
Foreign participation	4-21
Regulated products	4-21
Subcontracting	4-22
Accreditation of U.S.-based labs	4-23
Mutual recognition agreements	4-23
The modular approach	4-25
CE mark	4-27
Implementation	4-28
Part 2. Institutional, legal, and policy framework	4-29
Introduction	4-29
Environmental protection	4-29
Policy	4-29
Member-state differences in environmental priorities	4-31
Institutional framework	4-32
Environmental measures	4-33
EC legislation	4-33
Fiscal incentives	4-34
Member-state implementation	4-35
Implications for U.S. firms	4-36
Consumer protection	4-37

CONTENTS – Continued

	Page
Part 2. Institutional, legal, and policy framework – Continued	
Consumer protection – Continued	
Policy	4-37
Institutions	4-38
Consumer protection measures	4-39
Public health and Safety regulation	4-40
Description of EC health and safety policy	4-40
Institutional framework	4-42
EC measures and court rulings	4-42
Implementation in member states	4-44
Product and other liability	4-44
Policy	4-44
Product liability	4-44
Implementation problems	4-45
Other measures	4-46
Part 3. Industry analysis	
Agriculture	4-46
Overview	4-46
Deep-frozen bovine semen	4-47
Background	4-47
Anticipated changes	4-47
Possible effects	4-47
U.S. exports to the EC	4-47
Diversion of trade to the U.S. market	4-48
U.S. investment and operating conditions in the EC	4-48
U.S. industry response	4-48
Meat: hormones, inspection	4-48
Background	4-48
Anticipated changes	4-48
Possible effects	4-48
U.S. exports to the EC	4-48
Diversion of trade to the U.S. market	4-49
U.S. investment and operating conditions in the EC	4-49
U.S. industry response	4-49
Third country meat directive	4-49
Animal growth stimulants	4-49
Biotechnology	4-49
Processed foods and kindred products	4-51
Overview	4-51
Organic production of agricultural products	4-52
Background	4-52
Anticipated changes	4-52
Possible effects	4-52
U.S. exports to the EC	4-52
Diversion of trade to the U.S. market	4-53
U.S. Investment and operating condition in the EC	4-53
U.S. industry response	4-53
Labeling, advertising, and presentation of foodstuffs	4-53
Background	4-53
Anticipated changes	4-53
Possible effects	4-54
U.S. exports to the EC	4-54
Diversion of trade to the U.S. market	4-54
U.S. investment and operation conditions in the EC	4-54
U.S. industry response	4-54
Labeling of tobacco products	4-54

CONTENTS – Continued

Page

Part 3. Industry analysis – Continued

Processed foods and kindred products – Continued

Labeling of tobacco products – Continued

Background	4-54
Anticipated changes	4-54
Possible effects	4-55
U.S. exports to the EC	4-55
Diversion of trade to the U.S. market	4-55
U.S. investment and operating conditions in the EC	4-55
U.S. industry response	4-55

Advertising of tobacco products

Background	4-55
Anticipated changes	4-56
Possible effects	4-56
U.S. exports to the EC	4-56
Diversion of trade to the U.S. market	4-56
U.S. investment and operating conditions in the EC	4-56

Tobacco excise taxes

Maximum tar yield of cigarettes

Materials and articles in contact with foodstuffs

Chemicals and related products

Overview

Restrictions on the marketing and use of certain dangerous substances and preparation

Background	4-58
Anticipated changes	4-58
Possible effects	4-59
U.S. exports to the EC	4-59
Diversion of trade to the U.S. market	4-59
U.S. investment and operating conditions in the EC	4-59
U.S. industry response	4-60

Classification, packaging and labeling of dangerous substances

Background	4-60
Anticipated changes	4-60
Possible effects	4-61
U.S. exports to the EC	4-61
Diversion of trade to the U.S. market	4-61
U.S. investment and operating conditions in the EC	4-61
U.S. industry response	4-61

Pharmaceuticals

Background	4-61
Update	4-62
Single-market authorization procedure	4-62
Advertising	4-62

Medical equipment

Background	4-62
Update	4-63

Automobiles

Background	4-64
Update	4-64

Other machinery

Telecommunications

Background	4-67
Update	4-67
Telecommunications terminal equipment	4-67
Electromagnetic compatibility	4-67

CONTENTS – Continued

	<i>Page</i>
Part 3. Industry analysis – Continued	
Telecommunications – Continued	
Update – Continued	
Open network provision	4-67
Cellular digital mobile communications	4-68
Background	4-68
Anticipated changes	4-68
Possible effects	4-69
U.S. exports to the EC	4-69
Diversion of trade to the U.S. market	4-69
U.S. investment and operating conditions in the EC	4-69
U.S. industry response	4-69
Pan-European radio paging	4-69
Background	4-70
Anticipated changes	4-70
Possible effects	4-70
U.S. exports to the EC	4-70
Diversion of trade to the U.S. market	4-70
U.S. investment and operating conditions in the EC	4-70
U.S. industry response	4-70
Construction products	4-71
Phytosanitary requirements for wood products	4-71
Background	4-71
Anticipated changes	4-71
Possible effects	4-71
U.S. exports to the EC	4-71
Diversion of trade to the U.S. market	4-72
U.S. investment and operating conditions in the EC	4-72
U.S. industry response	4-72
Construction products directive	4-72
Background	4-72
Anticipated changes	4-72
Possible effects	4-73
U.S. exports to the EC	4-73
Diversion of trade to the U.S. market	4-74
U.S. investment and operating conditions in the EC	4-74
U.S. industry response	4-74

CHAPTER 4 STANDARDS, TESTING, AND CERTIFICATION

Developments Covered in the Previous Reports

Elimination of standards-related barriers is a key component of the 1992 program. The standards framed as part of the process are likely to be an important variable in future competition, not only in the EC market, but in the European Free Trade Area (EFTA) countries, a unified Germany, and Eastern Europe. While strongly supporting the overall thrust of the EC standards agenda, U.S. business has expressed concern about a lack of timely information during the EC standards-setting process and the potential for mischief in product approval. Actions taken in the first 6 months of 1990 appear to warrant optimism that the United States and the EC will resolve at least some of these problems before the regulatory changes being proposed are actually implemented.

Background and Anticipated Changes

There is general consensus that divergent national standards in the EC member states have held back the competitive potential of U.S. suppliers. In practice, these differences mean that U.S. firms may need to supply different products to the 12 national markets or abandon some markets altogether. Even where standards are similar, lack of mutual recognition of testing and certification can result in delays and higher costs.

To a large extent these differences reflect divergent approaches by member states to social, environmental, and consumer concerns, as well as diverse regulatory philosophies and historical circumstances. Up to now, each member state has arrived at different answers to questions such as: must governments prevent quality-related problems, or can the market decide? How are responsibilities for the safe use of products divided between government, employers, consumers, and workers? What is an acceptable environmental risk? How much and what type of information must consumers have before making purchasing decisions?

In its fundamental approach, the 1992 standard agenda represents a major break from the past. In its 1985 White Paper, the EC Commission proposed to systematically eliminate technical barriers in the EC, based on two guiding principles: (1) mutual recognition of existing member-state standards when possible, and (2) harmonization in those exceptional cases in which there are legitimate but conflicting views among the member states on essential public policy matters. The harmonized standards developed as part of the 1992 program

will be used to pursue key EC policy goals. The EC is committed to setting high standards for protecting the environment and consumers and for safeguarding public health and safety. Common standards will also contribute to the liberalization of public procurement, the deregulation of services, and the creation of commercially viable markets for new technologies.

The process involves hundreds of legislative and other actions, covering everything from product-labeling requirements to product liability. Of the 279 directives proposed in the 1985 White Paper, more than half pertain to standards. The scope of some directives is far reaching. A single directive on safety affects an estimated 55,000 types of machines. At the end of the process, the EC will have moved closer to creating EC-wide regulatory agencies similar to the U.S. Food and Drug Administration (FDA), Environmental Protection Agency (EPA), and Consumer Product Safety Commission (CPSC) and will have eliminated a host of legal and technical barriers that have effectively segmented member-state markets from one another.

The stakes for the United States are high. Banner U.S. export industries—such as machinery, auto parts, computers, pharmaceuticals, telecommunications, chemicals, and medical equipment—may be fundamentally affected by the EC's 1992 standards agenda. These manufacturing industries alone represented more than \$40 billion in U.S. exports in 1988. Potentially affected exports of agricultural commodities and processed foods together accounted for another \$1 billion in U.S. sales.

Where it believed EC-level regulation was warranted, the European Community shifted most of its legislation from directives defining all characteristics of particular products toward directives that define broad features that whole categories of products are to have. Not only were 12 different sets of regulations to be fairly rapidly replaced by one, these "new approach" directives would be much more flexible, because manufacturers would only be legally required to meet the key objectives of the legislation, i.e., user safety, as spelled out in so-called "essential requirements." Producers were to be allowed to choose among standards developed in the private sector to achieve conformity with them, and to test innovative products directly against the essential requirements.

Product approval would also be simplified. Manufacturers were to have several options for proving conformity to EC regulations, often being allowed to use a simple self-declaration of conformity. Once a product was approved in one member state, the manufacturer would have a ticket good for entry in all of the 12 national markets.

Because EC-level harmonization was already well advanced, the EC decided to continue regulating some major industries—such as agriculture and autos—differently. Such "old

approach" directives contain binding technical specifications and testing protocols. Products subject to such requirements must be approved by government authorities, and thus private testing and approval is not an option.

Possible Effects

Because divergent standards and testing requirements dampen U.S. sales now, the regulatory harmonization envisaged as part of the 1992 program holds enormous potential for benefiting U.S. firms. Scale economies gained by the acceptability of a single product throughout the EC, and reduced inventory storage costs could provide an immediate, positive boost to these U.S. suppliers. If such standards and approval procedures are biased against U.S. suppliers, however, the United States could experience and erosion of its competitive position and a drop in actual EC sales levels, as time is lost retooling production lines and securing necessary clearances and approvals. Lack of timely information during the EC's standards-setting process and the potential for delays and discrimination in product approval have been a source of concern for U.S. business. Others worry that the growing influence of environmentalists, consumers, and unions could result in stricter EC regulations in areas such as emissions and product safety. In the United States, the EC's unified approach has led some to question the adequacy of the present U.S. standards, testing, and product-approval system. Despite these concerns, most U.S. suppliers expect to benefit from the EC's move to a single set of regulations and standards and a more coherent system of conformity assessment, believing it will be an improvement over the present fragmented regime.

Part 1. Overall Developments in Testing and Standards During the First 6 Months of 1990

Introduction

The previous reports provided background on the nature of technical barriers in the EC,¹ presented a flowchart of the so-called "new approach" to standards harmonization,² discussed in detail the EC "global approach" to testing and certification,³ provided an overview of the EC's overall regulatory thrust in key industries,⁴ and

¹ U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States*, (Investigation No. 332 267), USITC Publication 2204, July 1989, p. 6-8.

² USITC, *Effects of Greater Economic Integration*, USITC Publication 2204, July 1989, p. 6-11.

³ U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States - First Follow-up Report*, (Investigation No. 332-267), USITC Publication 2268, March 1990, pp. 6-17 to 6-32.

⁴ USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, p. 6-19 and USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-15 to 6-16.

presented detailed analyses of some 43 directives that appear to be the most likely to affect U.S. firms. This report summarizes actions taken in the first 6 months of 1990 on the cross-cutting issues of transparency in standards development and nondiscrimination in testing and certification. It also examines the legal, institutional, and policy framework for technical harmonization in the EC. Finally, the report updates the status of directives viewed as having the greatest impact on nine major U.S. industries—agriculture, processed foods, chemicals, pharmaceuticals, medical devices, automobiles, machinery, telecommunications equipment, and miscellaneous manufactures. The following section provides an overview of the major themes covered in greater depth later in the chapter.

Overview

In 1988 and 1989, U.S. Government and business responded to the EC standards agenda by looking outward to gauge the extent of regulatory changes being contemplated within the EC, the size of the potential prize to be won, and the shifts in the competitive landscape likely to occur. By yearend 1989, the broad outlines of the EC's policies were fairly clear, and a number of specific measures finalized. The first 6 months of 1990 saw an intensification in the United States of internal efforts to prepare for such changes, and in the EC, of the difficult and rather daunting task of drafting the thousands of technical standards that will underpin the success of the EC's "new approach" to regulatory harmonization. The EC also took a number of steps to refine its policies towards testing and certification.

The EC continued to make progress during 1990 on developing the regulatory and other requirements for products to be sold in the European market after 1992. A large portion of the directives have been at least initially introduced. While the pace of EC work in the area of animal and plant health accelerated in 1990, progress remained slow. The mechanisms put in place during 1989 to improve transparency and provide U.S. suppliers with some influence over the standards-drafting process appeared to be working reasonably well, although a few spot problems were reported. The entry into force of the first "new approach" directive—that on toys—highlighted the practical difficulties that could await U.S. suppliers as 1992 standards directives are implemented. There was also some evidence that environmentalists, consumers, and workers were exerting greater influence on the EC's standards-development process, resulting, in the view of one EC official, in more "political" decisions in sensitive areas.⁵ Partly because of this tendency, the EC's evolving policy

⁵ See, for example, remarks of Vice President of the EC Commission for Internal Market and Industrial Affairs Martin Bangemann, as reported in U.S. Department of State Telegram, July 16, 1990, Brussels, Message Reference No. 10811.

towards biotechnology and growth-promoting hormones has been watched with increasing U.S. concern.

Success of the EC's new approach depends to a great degree upon the availability of harmonized European standards. Moreover, a working document released in May 1990, links the success of the EC's efforts to liberalize public procurement to the availability of common European standards. The slow rate of progress in developing voluntary standards by Europe's private regional standards bodies was one of the factors prompting the EC Commission to issue during the period a preliminary draft of its Green Paper on standards. Among other things, the paper calls for streamlining the process for drawing up such standards and for a widening of participation, both key U.S. goals.

The unfolding events in Eastern Europe during 1990 heightened the prospects that standards developed by the EC would become the language of commerce in most of Europe and other parts of the world as well.⁶ EFTA appeared to not only be adopting the voluntary standards being developed as part of the 1992 process, but the legal requirements of EC directives.⁷ During the period under review, the EFTA countries adopted legislation substantially the same as the EC's Machinery Safety Directive, according to one report.⁸ The fact that EFTA, Eastern Europe, and a unified Germany will be following the same standards may, in the view of some analysts, enable U.S. exporters to "enjoy the fruits of a truly single European Economic Space encompassing over two dozen countries."⁹

Testing and certification remained a prominent issue in the period under review, as the EC Commission worked to refine its policy towards the acceptance of test results from outside the EC and continued to develop legislation to further

⁶ U.S. Department of State Telegram, Mar. 9, 1990, Brussels, Message Reference No. 03823. The U.S. Mission in Brussels, reporting on a February conference on 1992 and standards, said that "representatives from Poland and Czechoslovakia, among others, indicated their interest in adapting to CEN/CENELEC standards in the future. This suggests the future of the European Economic Space in standards terms will encompass the EC 12, the EFTA and possibly the whole of Eastern Europe."

⁷ In a paper presented to a Nov. 15-16, 1989, CEN seminar on the European harmonization of machinery-safety standards, Nick Blomquist of the EFTA Secretariat stated that, "The EFTA countries follow, whenever possible and suitable for them, the principle to align themselves with decisions taken by the EC as part of its process of harmonizing technical rules and regulations. This principle is of course valid for the machines field.... The policy is to align the national legislation in the EFTA countries and other EFTA conditions to the rules of the EC and to take active part in the European work on harmonization." (p. 2) He continues on p. 6, "EFTA is preparing itself for this by working on sectoral agreements to be compatible to new approach EC directives."

⁸ USITC staff interview with representative the Association for Manufacturing Technology (NMTBA), Washington, DC June 27, 1990.

⁹ U.S. Department of State Telegram, Apr. 13, 1990, Brussels, Message Reference No. 05852.

harmonize conformity-assessment procedures among the member states. The EC Commission began to work with the private sector to build confidence and cooperation in the nonregulatory sphere. In April a Memorandum of Understanding on a new, privately run European Organization for Testing and Certification (EOTC) was signed, a step in the direction of greater coherence in private sector product-conformity schemes.

The prospect of substantially reducing testing-related barriers between the United States and the EC prompted government and private industry on both sides of the Atlantic to intensify efforts to develop negotiating strategies. The EC Commission went to work in earnest on the negotiating "mandates" it will need in order to conclude agreements with third countries on the mutual recognition of test results. The mandates are important because they could open the door to acceptance of U.S.-generated tests, a key U.S. objective. The United States, meanwhile, began to evaluate the institutional and legal underpinnings for such agreements. The two engaged in several fact-finding meetings to discuss their respective approaches to product approval. Moreover, the United States and the EC both participated in discussions taking place in the context of the Standards Code to strengthen multilateral commitments on conformity-assessment procedures. In the private sector, the American National Standards Institute (ANSI) explored the opportunities for cooperation with the EOTC and other private bodies in the testing and quality assurance spheres.

In the United States, the 1992 program was a catalyst for evaluating the operation of the U.S. standards system in today's increasingly global economy. At a series of hearings on the matter, U.S. industry representatives expressed strong support for the privately run, consensus-based U.S. standards system. However, a number of experts called upon such bodies to make greater efforts to include smaller firms; to avoid infighting, duplication of work, and conflicting standards; and to participate in and adopt international standards. Moreover, there was widespread agreement on the desirability of developing a more coherent U.S. approach to conformity assessment. A pressing need for greater public-private cooperation was identified, with the Government being called upon to lend more technical support to the voluntary standards system, underwrite greater private participation in international standards, and develop a coherent strategy for working with the private sector to advance U.S. commercial interests abroad.

Standards Development

In the last reports, it was noted that U.S. suppliers have complained that they have inadequate information about the EC's 1992-related work and few channels to make their interests

known. Moreover, they had little confidence that their comments will be sympathetically considered.¹⁰ A number of improvements were made in 1989. Among other things, the EC began to issue a monthly update on standardization work, agreed to accept comments on draft standards from third-country suppliers, and renewed its pledge to base European standards on internationally developed ones. However, U.S. suppliers still do not have an opportunity to participate directly in the EC's standards-drafting process, and the United States is behind its competitors in adoption of the international standards that will be the starting point for EC standards.¹¹ In 1990, the EC issued a preliminary draft of its "Green Paper on Standards," a think piece on the mechanisms for developing harmonized standards in the private sector. It also held bilateral discussions on the standards-development process and released a working document on the use of common standards in public procurement.

The Green Paper on Standards

During the course of 1990, the focus of interest in the standards-development area shifted from the legislative front to Europe's private regional standardsmaking institutes. Growing concern was voiced over the slow rate of progress by these bodies in developing standards associated with the 1992 program. At present, the regional standards bodies are badly behind in the creation of standards that are essential to the elimination of technical barriers in the EC.¹² Though technically "voluntary," these standards are crucial to the success of the EC's "new approach" to standards harmonization. Conformity with such standards will often provide a "presumption of conformity" with mandatory essential requirements, making it possible for manufacturers to exploit the least time-consuming and easiest methods of obtaining product approval. The EC Commission fears that with progress moving at the current rate, only a small number of the standards needed will have been developed by 1992.¹³ As noted in the previous report, the absence of relevant standards has also been a source of uncertainty and concern by U.S. businesses seeking to prepare for 1992.¹⁴

Largely as a result of these concerns, the EC Commission released in May 1990 a draft of its Green Paper on standardization. Though viewed by many analysts as an opening salvo in what

¹⁰ USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, p. 6-18.

¹¹ For a discussion of improvements made in 1989, their impact on the United States, and outstanding U.S. concerns, see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-32 to 6-36.

¹² See, for example, Lucy Kellaway, "EC Behind Schedule on Standards for 1992," *Financial Times*, May 4, 1990, p. 1.

¹³ *Ibid.*

¹⁴ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 6-12.

promises to be a lively internal debate within the EC, U.S. firms have an interest in the outcome. Among other things, the proposals under discussion could pave the way for wider U.S. participation, improved access to information, and a more rapid pace of European standardization work—all key U.S. objectives. On the other hand, they may signal a more unified European position in international standards bodies and the preeminence of European standards in the emerging East European market, a move that would up the ante in the 1992 standards debate and increase the urgency of steps under way to improve U.S. influence in international standards bodies.

Background

As mentioned earlier in this report, in the mid-1980s a new approach to the development of standards was adopted by the EC. This approach was based on the principle of mutual recognition. It succeeded in reducing the EC Commission's workload by obviating the need for EC-level directives on some three-fourths of the goods entering intra-Community commerce.¹⁵ Mutual recognition, however, did not work well for measures addressing fundamental concerns such as public health and safety, and so these kinds of member-state regulations became the focus of the legislative program spelled out in the EC's 1985 White Paper. A further breakthrough of the "new approach" is that it separated the political work involving the setting of minimum safety levels through directives or other legislation from the more technical process of developing specifications to ensure that products actually meet them. For many products, that task was left to the private regional standardization institutes—the European Committee for Standardization (CEN), the European Committee for Electrotechnical Standardization (CENELEC), and the European Telecommunications Standards Institute (ETSI).

In 1990 it became apparent that the result of this action has been to merely shift the bottleneck to removal of technical barriers in the EC from the governmental to the private sector level. Officials have reportedly admitted, "No thought went into the structure or workload of standards bodies."¹⁶ The political task of agreeing to changes in EC law needed to complete the internal market by 1992 has moved along fairly rapidly since the "new approach" was initiated in 1985; nearly 80 percent of the work on directives has already been completed by the Council, according to the EC Commission. However, around 2,000 technical standards still need to be developed by the more than 250 technical committees operating under the aegis of Europe's

¹⁵ U.S. General Accounting Office, *European Single Market: Issues of Concern to U.S. Exporters*, Report to the Chairman, U.S. Senate, Committee on Finance, Subcommittee on International Trade, GAO/NSIAD 90-60, February 1990, p. 23.

¹⁶ See, for example, Kellaway, "EC Behind Schedule on Standards for 1992," p. 1.

three regional European standardization bodies if the dream of a unified EC market is to become a practical reality.¹⁷

Recommended Changes

The Green Paper laid out a number of recommendations to bring a higher level of coordination, power, and resources to the regional standardmaking bodies and to expand participation by affected interests.¹⁸ The EC Commission called for greater coordination and improved information throughout the system by the creation of a European Standardization Organization (ESO), which would be responsible for overseeing the standardization process. In particular, this organization would supervise rules of the system, allocate work between different technical bodies, and manage publications and information policy. It was suggested that ESO should endeavor to provide interested parties with more information on the development of standards. Bodies such as CEN, CENELEC, and ETSI would continue to do the technical work on developing future standards and then transfer their results to ESO for formal adoption.¹⁹

The EC Commission also asserted that procedural changes need to be made to improve the efficiency of the standards-drafting process. Such changes would most likely include (1) the formation of "project teams" (small groups of qualified experts) to accelerate the drafting of documents, (2) direct input and "fast track" adoption of standards developed by EC-wide industry associations, (3) a shift away from a commitment to consensus to one of majority voting, (4) shorter public enquiry and response to comments periods, and (5) the direct applicability of adopted European standards.²⁰ Presently, regional standards do not exist in their own right and must be transposed into national standards before they can take effect. The EC Commission also called for changing the present policy, which prohibits the regional bodies from making direct sales of published standards.²¹ U.S. suppliers have complained about serious delays in obtaining 1992-related standards because it is often 6 months before such standards become available as national standards in the member states. A mark of conformity to European standards was suggested as one mechanism to achieve greater recognition of the contribution of regional standards to intra-EC trade.²²

¹⁷ EC Commission, *Draft Commission Green Paper on the Development of European Standardization: Action for Faster Technological Convergence in Europe*, Workpaper, Brussels, May 21, 1990 (hereinafter "Green Paper"), p. 6.

¹⁸ *Ibid.* It should be emphasized that the paper has still not been officially released and is likely to undergo some revision in the months ahead as the EC Commission gathers and considers the views of interested parties, notably, the member-state standards institutes and the regional standards bodies.

¹⁹ *Ibid.*, p. 32.

²⁰ *Ibid.*, pp. 24-27.

²¹ *Ibid.*, pp. 28-30.

²² *Ibid.*, p. 34.

A second major theme sounded by the EC Commission was that a greater openness of the system would be necessary to encourage wider public interest and confidence. Participation in the work and management of the system should be offered to more parties, including consumers and unions.²³ The EC Commission also made it known that the standardization process will need to include more participation from both nonmember central and Eastern European countries and international trading partners.²⁴ With the rapid political and economic developments in central and Eastern Europe, questions have arisen as to the direct participation of these countries in European standardization bodies. In the future, technical assistance in standardization to these countries will be a high priority for European standardization bodies, the EC Commission said, and therefore, their pending membership has been closely considered.²⁵ It is highly unlikely though that these countries will be admitted into the system in the near future, because of fear of compromising the EC Commission's primary objective of sustaining the pace of standardization. Instead, the Green Paper suggested that these nonmember European countries should be closely associated with the regional bodies' work so they may quickly adapt to new standards and obtain economic benefits from their use.²⁶ The Green Paper acknowledged that there are policy problems associated with providing preferential access to Eastern European countries, since the GATT Standards Code obligates the EC to ensure nondiscriminatory treatment to code signatories, including the United States.²⁷ One option under consideration is provisional membership for such bodies or a change in CEN/CENELEC rules that would grant observer status to countries with formal applications for membership pending.²⁸

The EC Commission also urged the regional bodies to consider admitting member bodies of international standards organizations such as the International Standards Organization (ISO), the International Electrotechnical Commission (IEC), and the International Telecommunications Union (ITU) to participate as observers in their work.²⁹ To this extent, U.S. firms, through active involvement in ISO/IEC technical committees, would have access to the European standardization process. The presence of members from international standards organizations would also be helpful for the European bodies that have made a policy of taking international standards as a basis for their own, the EC Commission said.³⁰ Furthermore, it has

²³ *Ibid.*, p. 23.

²⁴ *Ibid.*, p. 37.

²⁵ *Ibid.*, p. 37.

²⁶ *Ibid.*, p. 38.

²⁷ *Ibid.*, p. 38.

²⁸ USITC field interview with CEN official, Brussels, Belgium, July 19, 1990.

²⁹ *Ibid.*, p. 39.

³⁰ *Ibid.*, p. 39.

been suggested that international standards bodies take on some of the standards work being done at the European level. Closer coordination might, the paper observed, ensure that the international process is responsive to the EC's internal needs.³¹

The EC Commission admitted that in the development of international standards, there may be some reluctance on the part of countries such as the United States and Japan to participate in international forums because they may view the 18 member countries of the European standardization system as having too great an influence on the process. The EC Commission suggested that such countries are only likely to agree to participate more actively if the whole of the European Community—i.e., all of the 12 member states' national standards institutes—would agree to vote as one.³² It is unclear whether this statement represented tacit EC Commission recognition of the legitimacy of U.S. efforts to shift current voting and funding procedures in international bodies such as ISO/IEC from a one-country-one-vote system to one more closely tied to overall economic interests or, alternatively, represented a call for greater bloc-voting by the 12 national standards institutes of the EC. Bloc voting reportedly has not developed in ISO/IEC³³ but is a source of concern to U.S. industry. Under the present rules, the U.S. delegation, with one vote, could be easily outvoted by the representatives of the 12 national standards institutes, who each participate and vote in these fora.³⁴

Other measures are being proposed to ease the burden on the regional standards bodies. A meeting is planned in October 1990 to review the status of CEN/CENELEC's standardization mandates, at which it is expected that priorities will be rearranged. There is some preliminary evidence that the EC Commission may reduce the scope of work formally assigned to CEN/CENELEC in connection with 1992 directives. It is unclear whether the move is largely cosmetic or will ultimately reduce the actual burden on CEN/CENELEC.³⁵

EC Reaction

Reaction to the preliminary draft of the EC Commission Green Paper has been varied. Member-state standards institutes are reported to be vehemently opposed to many of the measures proposed, partly because they imply a shift in authority and money from the member-state bodies to the regional standards institutes and partly because they could represent a fundamental change

³¹ Ibid., p. 40.

³² Ibid., p. 40.

³³ USITC field interview with representative of ANSI Brussels office, July 18, 1990.

³⁴ See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 6–38 for a discussion of this issue.

³⁵ USITC field interview with CEN official, July 19, 1990.

in the process for achieving consensus on proposed standards. Moreover, many in the standards-development community who are sympathetic to the need for greater efficiency in the process question the wisdom of making organizational and funding changes now, given the press of work that must be completed by the 1992 deadline. The process is, they say, working as well as can be expected under the circumstances but could get derailed if a major overhaul of the system is undertaken. Furthermore, both the regional and member-state standards institutes believe that there is a fundamental tension between the Green Paper's stated goals of ensuring wider participation and speeding the pace of standards development.³⁶ The EC Commission, meanwhile, reportedly remains committed to most of the proposals contained in the Green Paper,³⁷ although one official speculated the goal of improved efficiency in standards development was probably the EC Commission's paramount objective in the near term.³⁸

U.S. Reaction

Because of a desire for greater predictability and wider access to the work of CEN/CENELEC, initial U.S. reaction to the Green Paper has been favorable. However, this assessment is tempered by some concern that if the EC Commission exerts too much pressure to produce standards by the 1992 deadline, the European standards bodies might be even less willing to consider foreign comments and participation in the future. Such pressure also flies in the face of U.S. hopes that the European bodies will await the outcome of international standards-development work in areas such as medical instruments and machinery, where the United States has recently initiated work in the hopes of influencing the 1992 process.³⁹ All representatives in the standards-development community contacted by USITC staff were of the view that caution should be observed to ensure that quality of standards produced by CEN/CENELEC not suffer as a result of pressure to pick up the pace.

Next Steps

The preliminary draft of the Green Paper has stimulated debate and focused discussion on the question of how European standards are developed. Recent reports suggest that the draft will undergo some revision before being officially released by the EC Commission sometime in the fall

³⁶ USITC field interview with CEN/CENELEC officials, July 19, 1990.

³⁷ USITC field interview with staff of the U.S. Mission to the EC in Brussels and the U.S. Department of Commerce, Office of EC Affairs, July 20, 1990.

³⁸ USITC field interview with staff of the EC Commission, July 20, 1990.

³⁹ Based on July 19, 1990, USITC field interview with U.S. EC Mission officer participating in July 16, 1990, meetings between the U.S. Food and Drug Administration and staff of the European standards institutes and the EC Commission.

of 1990.⁴⁰ The elements considered most likely to change are those calling for establishment of ESO as a new umbrella body and permitting participation by international bodies in standards-drafting work. Thereupon, the Green Paper could prove a source of leverage for the EC Commission in its dealings with the private standards bodies and a vehicle for pursuing U.S. interests in the standards-development sphere. Indeed, the EC Commission invited representatives from the U.S. Department of Commerce to attend a conference in Sardinia at which the first major internal discussion of the paper took place (see below), perhaps because of the United States' substantial stake. Nevertheless, if the Green Paper and initial reaction to it are any guide, the debate on these issues is likely to be driven more than anything else by internal dynamics in the EC and by a desire to exploit opportunities for Western European suppliers in the emerging Eastern European market.⁴¹

Bilateral Discussions

ANSI Meeting

On March 12, 1990, a private sector delegation led by the American National Standards Institute held consultations with CEN/CENELEC. The meetings were part of an effort to promote mutual cooperation and communication within the private sector on standards-related issues. The three primary results of the meeting were agreements to exchange information at an earlier stage of the standards process, a reinforcement of the commitment to work primarily through ISO/IEC, and the validation of the ad hoc arrangements made in 1989 that enable U.S. firms to comment on CEN/CENELEC standards work.

Sardinia Meeting

On July 7-8, 1990, officials of the U.S. Department of Commerce met with the representatives of the EC Commission and European regional standards institutes to discuss the Green Paper on standards and to review the functioning of arrangements made in 1989 to improve transparency in the development of voluntary European standards.

⁴⁰ USITC field interview with staff of the U.S. Mission to the EC in Brussels, July 20, 1990.

⁴¹ While it seems to be a "done deal" that Eastern European countries will adopt CEN/CENELEC standards as their own, a key question will be whether such standards will only replace current "export" standards—those for use when domestic producers in Eastern Europe seek to export to third countries—or "import" and "domestic" standards as well. Reportedly, many Eastern European nations maintain three sets of standards, one for export, one for imports, and one for domestically produced and consumed goods. Western European suppliers have an interest in ensuring that import standards in Eastern Europe are replaced with ones developed by CEN/CENELEC. USITC field interview with representatives of CEN/CENELEC, July 19, 1990.

U.S. Views

Assistant Secretary of Commerce Thomas Deusterberg said that despite improvements over the past year, arrangements made in 1989 for sharing information, for allowing indirect input by affected U.S. interests, and for closely coordinating European and international standards work did not appear to be working in selected instances. Particular concern was voiced about areas where U.S. industry had initiated international work in an effort to influence CEN/CENELEC standards. According to Deusterberg, U.S. industry was concerned that in their drive to complete 1992-related supporting standards before the entry into force of EC directives, CEN/CENELEC would either not wait for the outcome of international work or would be unwilling to transfer the relevant portions of their work to the international arena.⁴² The resource constraints of CEN/CENELEC and the national standards institutes essentially mean that there is often not enough staff or money for member-state experts to participate in international and regional standardization efforts simultaneously.⁴³

Assistant Secretary Deusterberg offered several ideas on improving U.S.-EC cooperation in the standards-drafting area. Among other things, he called for joint U.S. Government-EC Commission efforts to identify sectors where the two parties had a strong mutual interest in the furtherance of international standards work. More regular meetings of ISO/IEC subcommittees and working groups could, Deusterberg said, speed the development of international standards in these areas. The Assistant Secretary noted that there was an urgent need not to rebalance the voting and funding structure of ISO and IEC, where Europeans currently account for a disproportionate share relative to the United States. He also urged CEN/CENELEC to permit nonmembers to participate as observers in their work—including in the working groups and project teams charged with developing first drafts—and to more widely distribute working documents to affected U.S. interests. Assistant Secretary Deusterberg urged the European bodies at a minimum to extend observer status to ISO and IEC secretariats and preferably to extend that privilege to ISO/IEC member bodies, such as ANSI.⁴⁴

EC Views

The European standards institutes offered a mixed response to the Deusterberg overture. The

⁴² U.S. Department of State Telegram, July 16, 1990, Brussels, Message Reference No. 10811.

⁴³ A March cable from the U.S. Mission in Brussels notes that "in the standards area, there are concerns about the fast pace of CEN/CENELEC activity which could detract from efforts at the international level. There are also some spot situations where CEN/CENELEC seems to be working at odds with ISO/IEC activity." U.S. Department of State Telegram, Mar. 17, 1990, Brussels, Message Reference No. 04266.

⁴⁴ U.S. Department of State Telegram, July 16, 1990, Brussels, Message Reference No. 10811.

European Telecommunications Standards Institute said that a change in its internal rules was presently under consideration that would permit non-Europeans to join the body as "associate members." Mechanisms had been put in place earlier in 1990 to link the work of ETSI more closely with that of the International Telecommunications Union, and along with U.S. and Japanese standards bodies, ETSI had agreed to table its work items in the ITU first before proceeding at the regional level. Nevertheless, the ETSI representative said, the more decentralized standards structures in the United States and Japan made it difficult to undertake more cooperative efforts at this time.⁴⁵

CEN and CENELEC do appear to be drawing upon existing international standards as the basis for regional standards under development and have established liaison at both the planning and working group level with their international counterparts.⁴⁶ However, the two bodies have thus far not agreed to refer proposed European work to the ISO and IEC first before actually proceeding with regional standards development.⁴⁷ A representative of CENELEC said the IEC usually proceeds too slowly for 1992-related work, pointing to the particular case of electromagnetic compatibility (EMC) standards, where difficulty in reaching consensus on the U.S. side had until recently put the brakes on an IEC effort.⁴⁸ Some 600 IEC standards on EMC have been slated for review by CENELEC for purposes of ensuring that products meet the essential requirements of the EC directive, and the EC has expressed particular concern about the slow pace of European standards development in this area.⁴⁹

Taking note of more recent U.S. forays into the international arena in specific product areas, representatives of CEN and ISO criticized the United States of being a "free rider" in the past on the international standards system, contributing relatively little in the way of funding and expertise, consistently ignoring international standards back home, and placing top priority on domestic standards development. This indifference—rather than the lack of transparency in regional standards development and irrelevance of international standards—was the reason why U.S. industry seemed to be frequently surprised by standards being proposed at both the European and the international level, the representatives said. At the

same time, the EC Commission officials present welcomed greater U.S. participation and suggested that future meetings among the U.S. and regional standards bodies might serve as a forum for airing specific concerns.⁵⁰ For example, CEN/CENELEC has complained that the work programs and other documents submitted by U.S. standards institutes through ANSI are virtually unusable because of their widely different formats and timing.⁵¹

Multilateral Discussions

EC Views

Perhaps to deflect U.S. criticisms about the nontransparency of the EC's process for developing 1992-related standards, the EC also stepped up its criticisms of the U.S. standards-development process on the multilateral front in the first 6 months of 1990, complaining that the large number of organizations and jurisdictions involved in development of U.S. standards makes it difficult for all but the largest EC firms to participate.⁵² Specifically, the EC challenged U.S. bodies to improve the transparency of their work, notably by agreeing to submit semiannual work plans, in a common format, to the ISO's information network. The EC is also seeking formal assurances that such bodies will provide adequate notice of standards to be adopted, will allow reasonable time for affected parties to submit comments, and will use international standards unless there are compelling reasons for not doing so.

In an apparent effort to achieve these aims, an EC proposal for a voluntary "Code of Good Practice" for nongovernmental standards-drafting bodies has been submitted to the GATT Standards Code for consideration as an annex to the agreement. The EC says it is prepared within the context of the nonbinding Code of Good Practice to provide similar assurances to U.S. suppliers with respect to its regional (i.e., CEN) and national standards institutes. The EC argues that even though CEN/CENELEC decided in 1989 to notify ISO of new work items, draft standards, and finally adopted standards, firm assurances of such access in the future might enhance predictability by formally codifying these practices and subjecting them to governmental review in the context of the Standards Code.

U.S. Views

Although they accept the principles of due process and transparency, U.S. standards developers have expressed vehement opposition to the EC proposal, largely out of fears that it will lead

⁴⁵ Ibid.

⁴⁶ CEN passed a resolution in 1990 urging "its Members and TCs (technical committees) to do their utmost to support international standardization" and suggested that the CEN Secretariat should "consider a possible revision of the existing reporting secretariat mechanisms for information and participation in TC work to strengthen further collaboration at [the] technical level." CEN, Resolution CA 8/1990.

⁴⁷ USITC field interview with CEN, July 19, 1990.

⁴⁸ U.S. Department of State Telegram, July 16, 1990, Brussels, Message Reference No. 10811.

⁴⁹ USITC field interview with staff of the EC Commission, July 20, 1990.

⁵⁰ Unless otherwise indicated, all information in this paragraph is based on U.S. Department of State Telegram, July 16, 1990, Brussels, Message Reference No. 10811.

⁵¹ USITC field interview with CEN, July 19, 1990.

⁵² For a summary of these concerns see, for example, report by the EC Commission on U.S. Trade Barriers, 1990 edition.

to greater U.S. Government oversight of their activities, that it will move the U.S. standards system towards centralization, and that it will subject them to significant, prescriptive administrative burdens. The prospect for payoff is questionable, they say, because the proposal falls short of ensuring participation in the early stages of standards preparation work, a key to meaningfully influencing the final outcome of CEN/CENELEC decisions.⁵³ Moreover, the EC proposal could actually weaken the code's present requirements for national and nondiscriminatory treatment in standards development by removing standards from the present body of the code and allowing (indeed, explicitly encouraging) such bodies to ignore the views of bodies not formally signing onto the Code of Good Practice, even if they have a direct and material interest in the outcome of such standards work.

The U.S. Government, meanwhile, questioned the wisdom of the EC's proposed policy of formally preferring adoption of unified national and international standards in all cases. Whereas the EC has apparently decided in launching its 1992 program that coherence could provide a means to achieve economies and facilitate internal trade, the United States has traditionally favored diversity and competition as a means to drive the market to higher levels of efficiency and technical achievement.⁵⁴ The nature of the process for developing standards is the key variable in determining the actual openness of a standards system, according to this perspective, not the degree to which the system results in uniform standards.

Observers had anticipated U.S. manufacturers themselves to weigh in on the debate, particularly given the strong interest of U.S. exporters in improving current access to CEN/CENELEC. It remains unclear, for example, whether a plethora of standards and other technical requirements in the United States is a real concern of U.S. business or whether a move towards more systematic adoption of international standards could be in their long-term strategic interests. Faced with slowing domestic demand, some U.S. suppliers have turned their focus to foreign markets as an avenue for future sales growth. Many of the more promising markets, such as Eastern Europe, Mexico, and the Pacific Rim, are increasingly relying upon international and European standards as a basis for their commercial transactions. A hearing held by the U.S. Department of Commerce in April served as a starting point for the domestic debate (see below).

Domestic Considerations

In the last report it was observed that the 1992 program was serving as a catalyst in the United

States for rethinking how standards should be developed, how they relate to overall industrial competitiveness, and what role governments should play in ensuring that they do not become unnecessary obstacles to trade.⁵⁵ Some analysts suggested that the privately run, highly decentralized U.S. standards system was ill equipped to serve U.S. commercial interests in today's challenging international environment. Others voiced a need for greater cooperation between the U.S. Government and private sector in responding to external events such as the EC 1992 program. During the period under review, the U.S. Government and private sector began a formal dialog on the domestic ramifications of the EC's standards agenda.

The U.S. standards system is essentially divided into two key segments—public and private. The U.S. Government has written more than half of the standards in existence in the United States today, most of them for use in procurement. The remainder have been drafted by a privately funded, voluntary standards system composed of some 250 active organizations. The American National Standards Institute is the umbrella body for that system. It sets ground rules as to how standards should be developed and represents the United States in the ISO and IEC. It has also been the primary liaison with Europe's regional standards bodies.⁵⁶

On April 3-5, 1990, the U.S. Department of Commerce's National Institute of Standards and Technology (NIST) conducted a hearing to discuss U.S. participation in international standards activities and the extent to which the U.S. Federal Government should be involved in those activities.⁵⁷ Points that were addressed included strengths and weaknesses of the current U.S. standards system, proper roles of the Government and private sector, and important global challenges to the U.S. standards system in the future.

The 1992 program served as a catalyst for, and backdrop to, the hearing, which generated a high degree of interest. Oral presentations were made by 65 organizations and individuals; written submissions were received from 257 others. A sizable majority of witnesses at the hearing expressed strong support for the United States' voluntary process for developing standards,

⁵³ For a full discussion of this issue, see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-36 to 6-41.

⁵⁴ See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 6-37 for a more detailed profile of the U.S. standards system.

⁵⁷ The hearing was announced in the Nov. 27, 1989, *Federal Register*. A subsequent communication on Dec. 20 suggested that thought was being given to strengthening the role of the U.S. Government in promoting U.S. standards overseas; in funding U.S. participation in international and regional standards forums; and in accrediting testing laboratories, certification bodies, and quality system assessors. See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 6-40 for a discussion of events leading up to the announcement.

⁵³ USITC field interview with representative of the U.S. Industry Functional Advisory Committee on July 16, 1990.

⁵⁴ USITC staff interview, July 13, 1990.

believing it to be reflective of the United States' free enterprise system and culture because it is decentralized, pluralistic, and market driven.⁵⁸ Nevertheless, the hearing revealed certain problems with the present system and suggested a number of areas in which Government and private sector could take steps to improve it. The hearing underscored a need for greater cooperation in dealing with international issues and for a more coherent U.S. approach to testing and certification.⁵⁹

Strengths of the U.S. System

The United States' private, voluntary standards system was credited with creating numerous high-quality standards within a relatively short period of time, at virtually no cost for the U.S. Government. "No other nation is able to produce as many quality standards at such a low cost," stated Tony O'Neill, of the National Fire Protection Association (NFPA).⁶⁰ Underwriters' Laboratories said that the current system is highly flexible, facilitating the introduction of new and innovative products. ANSI accreditation requirements ensure openness and due process in the development of standards, witnesses said. Divergent views are both allowed and encouraged.⁶¹ A greater Government role in the system would, some speakers said, result in a loss of efficiency in terms of time, cost, and responsiveness.⁶²

Shortcomings of the U.S. System

While supporters outnumbered detractors by a large margin, some speakers called for changes in the current system.⁶³ The present structure is suffering from a shortage of resources and a lack of coordination, some believed.⁶⁴ U.S. industries often find it difficult financially to extend credible representation in standardsmaking forums—especially internationally.⁶⁵ Moreover, the fragmented nature of the U.S. system means that smaller businesses often do not have the time, money, or people to participate⁶⁶ and standards

⁵⁸ NIST, "Government's Role in Standards Related Activities: Analysis of Comments," July 16, 1990, draft, p. 6 states that two-thirds of those who commented endorsed the "voluntary process" for developing standards. Half of the supporters of the voluntary process also expressed support for ANSI; only two standards developers actually did so, however.

⁵⁹ NIST, "Government's Role in Standards-Related Activities," p. 1.

⁶⁰ Transcript of proceedings for Day 1, p. 91.

⁶¹ U.S. Department of Commerce, *Transcript of Hearing on Improving Participation in International Standards Activities*, first day, Apr. 3, 1990, p. 11.

⁶² *Ibid.*, p. 92.

⁶³ NIST, "Government's Role in Standards-Related Activities: Analysis of Comments," July 16, 1990, draft, p. 8 states, "Slightly more than 60 percent of those who commented on the standards drafting process identified specific problem areas and needs for improvement."

⁶⁴ U.S. Department of Commerce, *Transcript of Hearing on Improving Participation in International Standards Activities*, first day, Apr. 3, 1990, p. 65.

⁶⁵ *Ibid.*, p. 21.

⁶⁶ *Ibid.*, p. 206.

writing is, for the most part, the realm of big business.⁶⁷ Mel Green, associate director of the American Society for Mechanical Engineers (ASME), found that due to the dominance of the system by a few players, ANSI has been unable to present an objective and fair forum.⁶⁸ Moreover, greater coordination was considered a priority so as to ensure a unified U.S. position and true representation of U.S. interests in international standards activities.⁶⁹ Others called for greater efforts to adopt international standards and to harmonize domestic standards with international ones.⁷⁰

Mr. Wilgus of the American Council of Independent Labs (ACIL) found that the United States' present system for testing, certification, and accreditation was not working. "Testing laboratories are faced with the necessity of obtaining multiple certifications—each of which has limited utility because each has limited acceptance."⁷¹ A lack of Government coordination has resulted in a variety of terms, approaches, requirements and accreditation procedures, he said, making it difficult for the U.S. system to interface with other national systems. A more coherent approach domestically, as well as a unified and systemic U.S. response to worldwide developments, is a priority if testing-related obstacles to U.S. exports are to be eliminated.⁷²

The Roles of the Private Sector and Government

Various opinions on the roles of the private sector and Government were given. Although admitting that the present system may have "warts," most witnesses believed that the private sector should be trusted to deal with them.⁷³ There was general agreement that it would be counterproductive for the U.S. Government to supplant ANSI as an accreditor of national standards—an action that would not only create more bureaucracy, inefficiency, and confusion,⁷⁴ but would open the door for greater Government regulation. The voice of the private sector in international standards should be, furthermore,

⁶⁷ NIST, "Government's Role in Standards-Related Activities" July 16, 1990, draft, p. 10, suggests that of the participants identifying problems with the present system, 10 percent "complained about domination of the process of standardization by large companies."

⁶⁸ See transcript of proceedings, p. 35.

⁶⁹ U.S. Department of Commerce, *Transcript of Hearing on Improving Participation in International Standards Activities*, first day, Apr. 3, 1990, p. 210-211.

⁷⁰ NIST, "Government's Role in Standards-Related Activities" July 16, 1990 draft, p. 10.

⁷¹ Transcript of proceedings, p. 187.

⁷² Transcript of proceedings, p. 188.

⁷³ U.S. Department of Commerce, *Transcript of Hearing on Improving Participation in International Standards Activities*, first day, Apr. 3, 1990, p. 122.

⁷⁴ U.S. Department of Commerce, *Transcript of Hearing on Improving Participation in International Standards Activities*, first day, Apr. 3, 1990, pp. 15-16.

preserved and enhanced, witnesses said.⁷⁵ Mike Miller from the Association for the Advancement of Medical Instruments (AAMI) argued that "the management and technical knowledge necessary for effectively directing and coordinating international standards exists inherently within the private sector."⁷⁶ A greater commitment on the part of U.S. industry, in terms of both participation and financial support was considered necessary, however.

A number of witnesses urged the Government to play a greater role in funding standardsmaking activities. Due to financial constraints, it has become increasingly difficult for U.S. standards makers to maintain their membership in international organizations and participate in meetings held abroad.⁷⁷ The Government could support the voluntary system by contributing its fair share of money for the standards that it uses, some witnesses said.⁷⁸ Programs to provide funding for attendance by U.S. experts at international meetings and the sponsorship of projects would also be beneficial.⁷⁹ Tax incentives could further encourage participation.⁸⁰ Finally, the Government could increase funding for participation by Government experts in standardsmaking committees.⁸¹

The Government has a vital role to play in negotiating increased access for U.S. participation in standardsmaking activities worldwide, many witnesses said.⁸² The Government could also work with industry to encourage the use of private sector standards.⁸³ This involvement could include taking a proactive role to promote U.S. standards critical to the advancement of U.S. industry overseas and relying more extensively on private standards in public procurement.⁸⁴ Others said the Government should assist in educating corporate America about the strategic importance of standards.⁸⁵

Looking towards the future, many witnesses recognized the importance of the formation of an

⁷⁵ U.S. Department of Commerce, *Transcript of Hearing on Improving Participation in International Standards Activities*, first day, Apr. 3, 1990, p. 68.

⁷⁶ Transcript of proceedings, p. 104.

⁷⁷ U.S. Department of Commerce, *Transcript of Hearing on Improving Participation in International Standards Activities*, first day, Apr. 3, 1990, p. 118.

⁷⁸ *Ibid.*, p. 95.

⁷⁹ *Ibid.*, p. 23.

⁸⁰ *Ibid.*, p. 165.

⁸¹ NIST, "Government's Role in Standards-Related Activities," p. 8, states that, "One third of those making substantive comments on the [standards] process favored Government subsidies through grants to participants or payment of dues to international organizations. Almost one-fourth of those commenting on improvement needs proposed tax credits or other tax incentives to organizations that participate in international standards."

⁸² *Ibid.*, p. 12.

⁸³ U.S. Department of Commerce, *Transcript of Hearing on Improving Participation in International Standards Activities*, first day, Apr. 3, 1990, p. 26.

⁸⁴ *Ibid.*

⁸⁵ As stated by Mr. Lanphier of American Society of Agricultural Engineers, Transcript of proceedings, p. 81.

effective working partnership between the present voluntary system and the Government. The U.S. voluntary system is pressed with the continuing need to remain competitive in a changing world economy—the most immediate concern being Europe 1992. It will be imperative to obtain access to and information about actions being taken abroad so as to protect U.S. interests, witnesses said.⁸⁶ U.S.-EC governmental as well as private sector ANSI/CEN and CENELEC relationships will have to be strengthened and public-private coordination improved.⁸⁷ Perhaps more importantly, the United States must reduce testing-related barriers to U.S. exports,⁸⁸ working towards the acceptance by major U.S. trading partners of U.S. test data and recognition of U.S. labs and accreditation schemes.⁸⁹

Prospects

A number of witnesses suggested that a more cooperative relationship between the Government and private sector would improve the United States' ability to address international standards issues. Unfortunately, the hearing was viewed by many as a referendum on the viability of the U.S. system, in particular whether the U.S. Government should have a greater role in controlling it,⁹⁰ not a first step in a process of constructive adaptation.⁹¹ In the words of NIST, "The magnitude of the response and the intensity of expression of sentiments clearly indicates that the private sector opposes any significant changes to the current [U.S.] standards development system."⁹²

There are indications that ANSI and the U.S. Government are attempting to be responsive to the needs expressed at the April hearing. However, it is unclear how well they are coordinating their efforts. A high-level private advisory group on 1992 standards, proposed in February 1990,⁹³ was formally established but had yet to meet at press

⁸⁶ U.S. Department of Commerce, *Transcript of Hearing on Improving Participation in International Standards Activities*, first day, Apr. 3, 1990, p. 217.

⁸⁷ *Ibid.*, p. 153.

⁸⁸ *Ibid.*, p. 192.

⁸⁹ Of the participants expressing views about conformity assessment, nearly half said that the Government should play a major role, particularly in improving coordination back home and promoting agreements on the acceptance of U.S. tests in foreign markets. NIST, "Government's Role in Standards Related Activities: Analysis of Comments," July 16, 1990, draft, p. 10 and p. 15.

⁹⁰ NIST, "Government's Role in Standards-Related Activities," p. 6, states, "[T]here is considerable evidence that a large number of commenters participated in what they perceived to be a plebiscite on whether the U.S. standardization process should remain voluntary or be taken over by the Government."

⁹¹ See, for example, Donald L. Peyton, "Conduct and Administration of U.S. Participation and Leadership in International Standardization, Testing, and Certification in the Decade of the 1990s," NIST-GCR-90-572.

⁹² NIST, "Government's Role in Standards-Related Activities," p. 14.

⁹³ The committee's formation was announced in the Feb. 1, 1990, *Federal Register*, vol. 55, No. 22, p. 3440.

time for this report. In June testimony, Assistant Secretary for International Economic Policy Thomas Duesterberg said that—

U.S. as well as European manufacturers deserve more coherence and uniformity in the United States regulatory system for product approval and acceptances. There is a need to examine how these differing U.S. systems undercut the competitiveness of U.S. industry in the U.S. market, as well as in the international market. For example, a more uniform and coherent approach to U.S. Federal Government reliance on one consistent set of standards and a unified accreditation program for products regulated by the Federal Government may be a very positive contribution to U.S. competitiveness.⁹⁴

Duesterberg also expressed concern that “we have given scant attention in the United States to the consistence and strength of our quality assurance and quality accreditation system.” Noting that quality systems inspections will “become the basis for international trade with the EC in construction products, medical devices, personal protective equipment, and telecommunications products,” Duesterberg stated that, “we need to develop a program in the United States that responds directly to this need.”⁹⁵

Standards for Public Procurement

Use of common standards in bid specifications has long been recognized as key to the EC’s goal of a more open environment for public purchasing. On May 21, 1990, a working document on EC policy towards use of harmonized European standards in public procurement was released.⁹⁶ As the document points out, “Transparent procedures alone are not sufficient to ensure the opening of procurement markets if the technical specifications used in the purchasing procedures are in practice discriminatory. That is why the use of standards plays a crucial role in the effectiveness of any measures for opening-up procurement markets and in the realization of economies in the marketplace.”⁹⁷

Among other things, the paper reaffirmed the obligation imposed by EC law on public purchasers in the member states to use harmonized European standards, technical specifications, technical approvals, and quality-assurance schemes in their procurement specifications, even though compliance with such standards is normally voluntary.⁹⁸ This obligation is expected to play a

major role in future U.S. access to the public sector market in the EC for products such as telecommunications equipment, power-generation equipment, water supply equipment, and public works construction. The working document explains that requiring products to conform with the essential requirements of EC directives, which are legally binding, would not be sufficient to meet this obligation.⁹⁹ Although derogations are allowed in certain circumstances, the document notes that “contracting entities which use this derogation must inform the competent standardizing organization or body of the reason why they consider the standard inappropriate and request its revision.”¹⁰⁰

In addition, the paper outlined an action program for standardization work in this area. The EC Commission went on record as hoping for “substantial progress in a time horizon of three to five years,”¹⁰¹ with priority placed on standards that either do not pose a particular problem or are of particular importance for European industry. The document notes that mandates have been given to CEN/CENELEC for the establishment of inventories of standards in the sectors of water, energy, and transport and that CEN/CENELEC are now in the process of developing detailed standardization programs and of assigning priorities to the work items envisioned. A report on the appropriate characteristics of such standards has apparently been tabled by CEN/CENELEC and will be debated shortly, to be followed by formal standardization mandates from the EC Commission. ETSI has been asked to develop the standards needed in the telecommunications field. The EC Commission indicated a willingness to assess whether further Community-level legislation is required to achieve its harmonization objectives in the “excluded sectors” and to urge wider participation in European standards efforts.¹⁰² In the meantime, in a 1990 resolution, CEN confirmed that it intends to consider international standards as “the primary source of European standards for public procurement purposes.”¹⁰³

⁹⁴ —Continued

to entities at the central, regional, and local government levels when purchasing most goods and public works construction services. It will also apply to public utilities throughout the EC, whether or not owned or operated by the government, in the fields of telecommunications services, power generation, drinking water, and transportation. See ch. 6 of this report on public procurement for a brief description of these directives, also see USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, pp. 4–17 for a description of this obligation.

⁹⁶ Advisory Committee on the Opening up of Public Procurement, CCO/90/33 and Advisory Committee for Public Procurement, CC/90/29, *European Standards for Procurement*, (working document), May 21, 1990, p. 4.

¹⁰⁰ *Ibid.*, p. 2.

¹⁰¹ *Ibid.*, p. 9.

¹⁰² *Ibid.*, pp. 9–10.

¹⁰³ CEN, Resolution CA 8/1990.

⁹⁴ Statement of Thomas J. Duesterberg, Assistant Secretary for International Economic Policy, U.S. Department of Commerce, House Science Committee Hearings on International Standardization, June 26, 1990, p. 15.

⁹⁵ *Ibid.*, p. 16.

⁹⁶ Advisory Committee on the Opening up of Public Procurement, CCO/90/33 and Advisory Committee for Public Procurement, CC/90/29, *European Standards for Procurement*, (working document), May 21, 1990.

⁹⁷ *Ibid.*, p. 2.

⁹⁸ This obligation is contained in the “supplies,” “works,” and “excluded sector” (or “utilities”) directives, and thus applies

Testing and Certification

Previous reports have indicated that U.S. companies and associations generally support the development of a transparent EC approval process that is fair, equitable, nondiscriminatory, not overly burdensome and that enhances trade. However, some are concerned that the EC's proposed testing and certification policy—formally set out in its July 1989 "Global Approach to Testing and Certification"—may place them at a competitive disadvantage relative to firms producing in the Community. In 1989, U.S. business expressed strong concern about the EC's unwillingness to accept tests generated outside the EC for purposes of demonstrating conformity with EC requirements. Failure to do so, nearly all agreed, would expose foreign suppliers to higher compliance-related costs, greater uncertainty, and lost sales in the EC market.

In the early months of 1990, the EC backed off from its initial refusal, identifying certain circumstances in which it would accept non-EC-generated test results for purposes of regulatory approval. In the nonregulated sphere, the final arrangements for setting up a European Organization for Testing and Certification (EOTC) were made, paving the way for greater internal cooperation in testing-related matters in the nonregulated sphere. The EC also continued to refine its "Global Approach" to testing and certification, notably the conditions under which it would accept tests generated outside the EC for purposes of regulatory enforcement.¹⁰⁴

The evolving policy was being framed in the context of a policy statement issued by the EC Council on December 21, 1989, recognizing the desirability of accepting foreign-generated tests in order to promote international trade.¹⁰⁵ During the first 6 months of 1990, EC officials took pains to reassure the Community's trading partners that foreign suppliers will continue to be accorded national treatment in product-approval schemes consistent with the Community's international obligations under the Tokyo Round Standards Code. According to one spokesperson, the EC "is firmly committed to equal and nondiscriminatory access to all its conformity assessment systems in the regulated or nonregulated area. Put at its simplest, the same rules will apply whatever the origin of the product."¹⁰⁶ EC officials have said that they will

¹⁰⁴ See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-17 to 6-32 for a detailed analysis of the EC's Global Approach to Testing and Certification, formally released by the EC Commission in July 1989.

¹⁰⁵ See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 6 28 for a discussion of the Council resolution, "Council Resolution 90 on a Global Approach to Conformity Assessment," passed Dec. 21, 1989, O) No. C 20 (Jan. 16, 1990).

¹⁰⁶ John Farnell, Head of Division DGIII/B/4 (Internal Market and Industrial Affairs), Feb. 13, 1990, speech at a conference in Brussels entitled 1992: *European Standardization in the International Context*, as reported in U.S. Department of State Telegram, Mar. 9, 1990, Brussels, Message Reference No. 03823.

encourage the arrangements between EC and non-EC parties on the mutual recognition of test results. Such agreements could reduce testing-related barriers between the United States and the EC and could provide material benefits to all signatories.

Nonregulated Products

On April 25, the EC and CEN/CENELEC signed a memorandum of understanding (MOU) establishing the European Organization for Testing and Certification. The EOTC will be a focal point for all testing and certification matters in the EC,¹⁰⁷ although its main aim will be to eliminate testing-related barriers among the member states in the nonregulatory sphere.¹⁰⁸ Such barriers will be removed by building confidence among all affected interests—consumers, users, producers, public authorities, testing laboratories, product certifiers, etc.—through the establishment of common criteria, encouraging the sharing of technical information, and improving coordination. The ultimate objective is to minimize the need for multiple inspections and product tests by buyers, users, and consumers in the EC.

Structure

In terms of structure, the body—which is technically private¹⁰⁹—is to comprise a central council and secretariat, specialized committees of test labs, quality assurance bodies, and product certifiers, sectoral committees, and agreements groups. The functions of each of these components are discussed below.

The council

The council is to provide the superstructure for the various components of the organization. Among other things, it is to ensure that all interested parties are properly involved in conformity-assessment processes, and to develop and ensure the coherent application of "principles and processes in the field of conformity

¹⁰⁷ The body is also to assist "the Commission of the European Communities and the EFTA countries regarding conformity assessment in the regulatory sphere" including "assisting the Commission of the European Communities and the EFTA countries in the definition of the technical conditions for furthering agreements, including those with third countries." Memorandum of Understanding Between the Commission of the European Communities, the European Free Trade Association (EFTA) and CEN/CENELEC for the Setting Up of the European Organization for Testing and Certification, Apr. 25, 1990, (herein after "MOU"), par. I.

¹⁰⁸ The MOU states that the objectives of the organization include: "encouraging, fostering, and managing the development of European certification systems and of mutual recognition agreements for test reports and certificates on the basis of coherent principles and processes which will attract the confidence of all interested parties." MOU, par. I.

¹⁰⁹ As discussed later, CEN/CENELEC is to provide administrative support for the new body, and the EC Commission intends to underwrite the EOTC financially for its initial 3 year startup period.

assessment."¹¹⁰ The council is the element of the organization that brings in the broadest spectrum of affected interests. It will include representatives of European industry organizations, consumer groups, unions, government (the EC Commission and EFTA), and the European standards institutions, as well as one representative of the conformity-assessment community nominated by each of the member states and a representative from each sectoral and specialized committee.

Specialized committees

The nature of the EOTC's specialized Committees apparently changed somewhat from that depicted in our previous report.¹¹¹ Rather than being coequal to the sectoral committees, and having an ongoing and fundamental interaction with them, the specialized committees will be strictly advisory to the sectoral committees and agreements groups and will only render advice upon request. On the other hand, the specialized committees may have more of a role in the regulated sphere than previously thought. The EC Commission reportedly plans to draw upon the specialized committees' expertise as it grapples with conformity-assessment issues in EC regulations and directives. Such a relationship should, the officials said, minimize the degree of conflict between conformity-assessment procedures and requirements in the nonregulated and regulated spheres.¹¹² In addition, the EC Commission has said that it may utilize EOTC expertise to assess the competence of foreign laboratories seeking to have their test results and product certificates accepted under mutual recognition agreements.¹¹³

Moreover, the specialized committees are charged in the MOU with helping to ensure the coherent application of the basic standards of competence and conduct for laboratories and quality-assurance schemes and for updating and elaborating upon those standards.¹¹⁴ Member states have been asked to ensure that the bodies designated ("notified") by them to conduct procedures required by particular 1992 directives conform with these basic standards. The specialized committees will also promote and review agreements on mutual recognition in various disciplines, such as testing, certification, etc.¹¹⁵

¹¹⁰ MOU, par. II.1.

¹¹¹ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-21 to 6-22.

¹¹² U.S. Department of State Telegram, July 3, 1990, Brussels, Message Reference No. 10157.

¹¹³ U.S. Department of State Telegram, Brussels, Message Reference No. 04266, Mar. 16, 1990, reporting on a meeting held on Mar. 13 between representatives of the American National Standards Institute and an official of the EC Commission.

¹¹⁴ The MOU (par. II.4) states that agreements groups are also responsible for "identifying specific needs for the development of standards, either for products, or for the EN29000 and 45000 series."

¹¹⁵ MOU, par. II.2.

Sectoral committees and agreements groups

The sectoral committees will represent "large sectors of industrial activities" and be set up according to the needs of the economy upon a proposal by interested parties.¹¹⁶ As of July 1990, exploratory discussions on the formation of sectoral committees were taking place in some 12 areas.¹¹⁷ Even though non-EC interests cannot formally participate in the sectoral committees,¹¹⁸ the committees may prove a reasonable vehicle for U.S. industry input into the EC's future testing regime. The sectoral committees are formally charged in the MOU with "maintaining dialogue with similar organizations in other countries and regions, with a view to reaching an appropriate state of coordination at the international level."¹¹⁹ Agreements Groups are to be "made up of those interested parties who have established or intend to establish under the auspices of EOTC, a mutual recognition agreement or certification system."¹²⁰ In meetings with U.S. officials in June, officials of the EC Commission stated that the EOTC structure placed most decisionmaking within the agreements groups. Sectoral committees are to ensure uniformity across agreements groups in the same sector.¹²¹

Operation

The EOTC is to be set up in three stages and should be in full operation by the beginning of 1993.¹²² The first stage will be the preparatory stage, culminating in the first formal meeting of the EOTC Council. The second or experimental stage will end on December 31, 1992, and will provide an opportunity for necessary changes to be made in the structure and operation of the EOTC and its various components. During this period, the EC Commission and CEN/CENELEC will provide both organizational and financial support to the EOTC. The third, or mature, stage will be characterized by a stabilized and fully operational EOTC operating under the independent control of its council.

¹¹⁶ MOU, par. III.1.3.

¹¹⁷ Preliminary activity has been reported in the following areas: (1) information technology, (2) steel, (3) low-voltage electrical equipment (including electromagnetic compatibility), (4) high-voltage electrical equipment, (5) medical equipment, (6) gas appliances, (7) aerospace, (8) building products, (9) machinery, (10) electrical components, (11) water supply, and (12) chemicals. As reported by American National Standards Institute, *ANSI Global Standardization Report*, vol. 3, p. 25.

¹¹⁸ The MOU (par. III.1) states that sectoral committees shall be composed of a delegation from each of the member states and that this delegation shall be representative of interested parties (i.e., manufacturers, users, and third parties), as well as a representative from each agreement group falling within the product sector.

¹¹⁹ MOU, par. II.3.

¹²⁰ MOU, par. III.1.

¹²¹ U.S. Department of State Telegram, Brussels, Message Reference No. 10157, July 17, 1990.

¹²² "New European Body for Certification and Testing. *European Report*, No. 1588 (May 19, 1990), sec. 5, p. 5; "News in Brief," 1992 - *The External Impact of European Unification*, vol. 1, No. 22 (Feb. 23, 1990), p. 11.

Organizational steps were taken during the period under review in an effort to get the EOTC up and running by late 1990. On June 1, a small EOTC staff was established within CEN/CENELEC.¹²³ In mid-July, a director of the new organization was selected, and the first meeting of the EOTC Council was scheduled to take place in London in late November 1990.¹²⁴ It is expected that the council will elect the EOTC's president at that time.

Foreign Participation

U.S. industry is very interested in forging bridges to the emerging EOTC system. During the period under review, ANSI urged the EC (1) to encourage sector and specialized committees to develop close working relations with counterpart organizations in the United States, (2) to urge agreements groups to include non-European parties on a nondiscriminatory basis, (3) to promote international agreements on mutual recognition that are open, transparent, and equitable.¹²⁵

The EC Commission has said that the EOTC's sectoral committees would be free to establish informal ties with counterparts in other countries¹²⁶ and that agreements groups of the EOTC could include non-EC firms as full-fledged participants,¹²⁷ provided they meet the criteria for such agreements.¹²⁸ Both statements were well-received in the U.S. private sector, since they could pave the way for elimination of the currently overlapping and duplicative testing requirements imposed by private purchasers in the EC. However, no foreign representation in the EOTC Council, the sectoral committees, or the functional committees is foreseen, EC Commission officials have said.¹²⁹

U.S. trade associations and test houses have been working behind the scenes to establish informal links with the new organization in the hopes of facilitating the acceptance of U.S. tests and certificates after 1992. In March, an ANSI-led delegation discussed possible future cooperation in the conformity-assessment sphere. In August, another ANSI delegation met with leaders of the European Quality System to assess the EC's evolving activities in the field of quality assurance.

¹²³ U.S. Department of State Telegram, July 3, 1990, Brussels, Message No. 10157.

¹²⁴ USITC field interview with CEN officials, July 19, 1990.

¹²⁵ American National Standards Institute, "ANSI Views on Relationships Between the United States and Europe on Testing and Certification," July 23, 1990, p. 1.

¹²⁶ U.S. Department of State Telegram, Brussels, Message Reference No. 04266, Mar. 16, 1990, reporting on a meeting held on Mar. 13 between representatives of the American National Standards Institute and an official of the EC Commission.

¹²⁷ U.S. Department of State Telegram, Brussels, Message Reference No. 10157, July 3, 1990.

¹²⁸ The MOU (par. II.4) does state that members of agreements groups should satisfy the criteria of the EN45000 and EN29000 series as appropriate.

¹²⁹ U.S. Department of State Telegram, Brussels, Message Reference No. 10157, July 3, 1990.

Further meetings are scheduled for October 1 and 2, 1990.¹³⁰

U.S. industry has expressed great interest in learning about emerging sectoral committees and agreements groups so that they may channel their information-gathering efforts. An official of CEN reported that no existing mutual recognition arrangements in Europe will be directly transferred into the EOTC structure. All of them, including the ECITC program for certification of information-technology equipment, will need to undergo changes in order to totally fulfill the criteria set forth in the MOU. Two certification agreements have been established, however, and both include U.S. test labs, the CEN official stated.¹³¹

Regulated Products

In the case of regulated products, the EC Commission has said that acceptance of non-EC-generated tests would depend on several factors. If the EC directive governing the product permits suppliers to issue a manufacturers' declaration of conformity, suppliers are free to work with the testing lab, quality-assurance assessor, or product certifier of their choosing, whether or not located in the EC. For products for which intervention of a third party is actually required by EC standards directives, however, acceptance of non-EC-generated tests, reports, or certificates would, EC Commission officials stated, only be permitted under two circumstances: (1) when they were generated by a foreign firm acting as a subcontractor to an EC-based "notified body," and (2) when the EC has concluded a formal agreement on the mutual recognition of test results. Such agreements are needed, according to a representative of the EC, in order "to ensure, on the one hand, that the competence and responsibility of the non-EEC body concerned is adequate and will be maintained by some form of officially recognized surveillance. It is also needed to make sure (to put it bluntly) that the Community is getting a fair deal."¹³²

In 1990, the United States continued to lobby against a reciprocity criterion for such agreements. Other key U.S. goals include (1) ensuring that U.S. suppliers are able to choose "a means for showing conformity that will not place them at a competitive disadvantage [relative] to European or other suppliers in getting products to the market," (2)

¹³⁰ George T. Willingmyre, Vice President, American National Standards Institute, letter to the Honorable Tim Valentine, Chairman, Subcommittee on Science, Research, and Technology, Committee on Science, Space and Technology, U.S. House of Representatives, July 17, 1990, p. 4.

¹³¹ USITC field interview with CEN official, July 19, 1990.

¹³² Unless otherwise noted, all information in this paragraph is based upon a speech by John Farnell, Head of Division DGIII/B/4 (Internal Market and Industrial Affairs), Feb. 13, 1990, at a conference in Brussels entitled "1992: European Standardization in the International Context," as reported in U.S. Department of State Telegram, Mar. 9, 1990, Brussels, Message Reference No. 03823 (Farnell speech).

avoiding duplicative testing and quality-assurance requirements, and (3) ensuring acceptance of test results from qualified bodies located outside the EC.¹³³ Some in U.S. industry have been lobbying hard for the designation of U.S.-based test laboratories as "notified bodies." Others have warned that the present structures in the EC for assessing conformity "may neither have the staffing nor the expertise to implement the global approach as proposed."¹³⁴

The EC Commission has been hard at work in 1990 drafting for Council approval "negotiating mandates" which will empower the Commission to enter into negotiations with third countries on the mutual recognition of test results, a prime objective of U.S. industry. It is expected that these mandates will further clarify EC thinking on the subject of subcontracting and reciprocity. As of July 1990, EC Commission staff reported that the first drafts of such mandates had been prepared, but were not expected to be finalized much before the end of the year.¹³⁵

Subcontracting

In late 1989, the Council approved in principle subcontracting by testing laboratories, an option provided for under the EN45000 standard.¹³⁶ The prospect that the EC would allow "notified bodies" to subcontract to non-EC labs was viewed as a positive development since it could make it easier for U.S. suppliers to obtain the necessary

inspections and test reports.¹³⁷ Indeed, a relatively liberal EC policy on subcontracting could, some analysts suggested, obviate the need for conclusion of formal mutual recognition agreements.¹³⁸ Larger U.S. laboratories, notably Underwriters' Laboratories, expressed the belief that subcontracting arrangements could go a long way towards easing the need for U.S. exporters to ship their product to the EC to obtain the necessary test reports, and avoid some of the downside risks associated with mutual recognition agreements.¹³⁹ Their optimism may be derived from the fact that larger laboratories are in a better position to negotiate subcontracting arrangements with European notified bodies.¹⁴⁰

However, there remains considerable uncertainty as to the circumstances in which subcontracting will actually be permitted in practice,¹⁴¹ and as the 6-month period progressed, it appeared that the EC was taking a narrower, rather than broader, view on the scope of potential subcontracting arrangements.¹⁴² While the

¹³⁷Willingmyre letter, p. 5.

¹³⁸ U.S. Department of State Telegram, Apr. 13, 1990, Brussels, Message Reference No. 05852.

¹³⁹ These downside risks include the fact that the *quid pro quo* for becoming a notified body or concluding a formal agreement on the mutual recognition of test results would, according to the EC Commission, be agreement by the United States (or U.S. bodies) to accept tests and certification marks from all EC notified bodies. Some suggest that the EC may not have sufficiently comprehensive standards or strong enough surveillance to ensure the competence of EC-based labs, posing the prospect that goods representing a danger from a public safety point of view could be placed on the U.S. market. Moreover, to the extent that such arrangements provided for the U.S. body to affix its own mark of conformity, there is a risk that the commercial value of that mark could be diluted. While the risk associated with improperly evaluated products is emphasized, there is some evidence that part of the concern of U.S. certification bodies is heightened competition in the U.S. market, both from European bodies themselves and from the CE mark.

¹⁴⁰ USITC interview with staff of Underwriters' Laboratory, Aug. 9, 1990.

¹⁴¹ EC Commission officials have elaborated upon their current thinking in this regard, but such thinking is still evolving and must ultimately be endorsed by the Council if it is to have binding effect on the member states. The Council has already agreed in principle to subcontracting by testing labs under the conditions set out in the EN45000 standard. It is expected that endorsement of subcontracting in additional situations will be associated with Council approval of the negotiating mandates currently being prepared by the EC Commission, an act not expected to occur until early 1991.

¹⁴² During bilateral meetings with the United States on June 13, 1990, EC Commission officials reportedly stated that notified bodies cannot delegate their essential roles to others, i.e., those associated with the evaluative functions for which they have been notified. Elaborating upon this condition, the EC Commission officials said that notified bodies may not delegate or subcontract their responsibilities for judging, interpreting, and approving. However, the officials suggested that notified bodies would be permitted to subcontract some technical functions, even if it has the in-house capability to perform them. The decision about whether or not to subcontract would remain at the sole discretion of the notified body. The extent of such subcontracting would ultimately be

¹³³ George T. Willingmyre, Vice President, American National Standards Institute, letter to the Honorable Tim Valentine, Chairman, Subcommittee on Science, Research, and Technology, Committee on Science, Space and Technology, U.S. House of Representatives, July 17, 1990, pp. 3-5.

¹³⁴ EC Committee of the American Chamber of Commerce in Brussels, Feb. 27, 1990, position paper on the global approach, p. 6, which continues, "Clearly the question of resources required to avoid identified bottlenecks needs to be addressed before implementation of legislative conformity assessment procedures." In December 1989, the Council had requested the Commission to propose measures to deal with differences in levels of development in the Community with regard to infrastructure. In March 1990, an EC Commission official indicated that in order to do so the EC Commission would need to conduct a feasibility study, something that had yet to be undertaken. U.S. Department of State Telegram, Mar. 17, 1990, Brussels, Message Reference No. 04266. When queried on this point by USITC staff on July 20, an EC Commission official indicated that no effort to identify bottlenecks had been made as of yet.

¹³⁵ USITC field interview with staff of the EC Commission, July 20, 1990.

¹³⁶ According to an EC Commission official, "The Council decided during the discussion of the Global Approach that [the limits for acceptance of non-EC-generated tests] are determined by the EN45000 standard for testing laboratories. That standard provides for the possibility of subcontracting of testing, subject to certain conditions, such as (1) that only part of the tests may be subcontracted; (2) that the subcontracting body ensures that the body to which it subcontracts meets the EN45000 standard; (3) that records are kept on subcontracting arrangements, and so on. The Council has now agreed that notified bodies can, within these limits, subcontract testing to other bodies, including those located outside the Community, provided they retain full responsibility for their results and that the certificate is delivered by the EC notified body itself." (Farnell speech).

subcontracting of tests per se will be permitted, at least for now, it does not appear that inspections and quality-assurance audits could be conducted by outside vendors and subcontractors would not themselves be permitted to issue certification marks. This is a particular concern in the quality-assurance sphere, since it is anticipated that access to the EC market will hinge to a greater extent on such assurance after 1992.¹⁴³

Smaller U.S. testing labs, meanwhile, charged that subcontracting arrangements were not likely to be widespread and were thus no substitute for the formal designation of U.S.-based labs as "notified bodies." In particular, since European-owned labs were generally free to become accredited by U.S. regulatory agencies¹⁴⁴ and since a number of prospective "notified bodies" have set up affiliated labs in the United States, there was little incentive for such bodies to extend subcontracting relationships to nonaffiliated U.S.-based labs. This is especially true when the tests envisioned in EC

¹⁴² — Continued

linked to the nature of the functions the body itself had been notified for (e.g., testing, certification, etc.). For example, a body that had been notified to perform testing required by an EC directive would not be able to subcontract testing. However, a body notified to issue certification marks based on an evaluation of test results could subcontract the performance of the tests themselves to outside labs.

In all cases, the officials said, the notified body would remain solely responsible for the integrity of all aspects of its recognized duties, whether or not some portion had been subcontracted. Member states, meanwhile, are accountable to the EC Commission for the competence of bodies notified by them. Such bodies are to be able to competently perform at the minimum level specified in each new approach directive and in the EN45000 series of standards. Member states will only be permitted to notify bodies located within their territory, on the assumption that such bodies are within the legal reach of the member-state authorities. As reported in U.S. Department of State Telegram, July 3, 1990, Brussels, Message Reference No. 10157.

¹⁴³ Given the inherently evaluative nature of quality systems inspections, EC Commission officials have observed that it may be impossible for notified bodies to subcontract functions associated with surveillance of quality assurance in the manufacturing process and still meet the policy guidelines set out by the EC. As reported in U.S. Department of State Telegram, July 3, 1990, Brussels, Message Reference No. 10157. Underwriters' Laboratories has set up an arrangement with the British Standards Institute in the quality assurance sphere, but it is unclear at this time whether such an arrangement will be of much use for U.S. manufacturers seeking to meet legally binding EC requirements post 1992. USITC staff interview with Underwriters' Laboratories, Aug. 9, 1990. In a meeting with ANSI representatives on Mar. 13, an EC Commission official stated that the EC Commission intends to be somewhat flexible in handling existing private arrangements, even if they spill over into the regulated area, stating that it had no intention of breaking them up "for sheer intellectual pleasure." U.S. Department of State Telegram, Mar. 17, 1990, Brussels, Message Reference No. 04266.

¹⁴⁴ Others have pointed out that the EC's reciprocity criterion is "not far in concept" from OSHA's National Recognized Testing Laboratory Program, which is "bound to consider advice from the United States Trade Representative" before acting upon applications by laboratories located outside the United States. Willingmyre letter, p. 5.

directives are relatively straightforward, such as in the case of testing for electromagnetic compatibility (EMC).¹⁴⁵ Responding in part to complaints by U.S. labs that they are not competing on a level playing field, Congressman Sam Gjedenson (D-CT) introduced five bills during this legislative session that would preclude agencies such as the Federal Communications Commission and the Consumer Product Safety Commission from recognizing non-U.S. labs in their approval schemes.¹⁴⁶

Others have claimed that the EC's move from 12 separate sets of product approvals to a single one in the 1992 process will sharply reduce demand for testing services for the EC market.¹⁴⁷ This in turn could lead to an intensification of competition among testing labs and a likely shake-out. In theory, at least, this change in the market environment could prompt European notified bodies to aggressively pursue subcontracting arrangements in the United States as a marketing tool.¹⁴⁸

Accreditation of U.S.-Based Labs

Over the course of the 6-month period, the EC did not back off its initial refusal to permit non-EC labs to accredit U.S. labs as "notified bodies." However, efforts to reach an agreement on the subject continued in the context of the Standards Code. How hard to push for accreditation of U.S.-based labs was a source of debate within the United States. Although EC acceptance of U.S.-generated tests remains a prime goal of U.S.-based manufacturers, they have not registered strong views as to whether this acceptance should be of U.S.-owned labs themselves or whether the extension of subcontracting relationships to the U.S. affiliates of EC-based notified bodies would be sufficient to ensure future U.S. access to the EC market. Some large U.S. certification bodies have gone on record as opposing a U.S. push for "notified body" status. Smaller U.S. testing labs, meanwhile, said that the possibility of securing notified-body status in the EC was a key variable in their ability to compete and survive in the years ahead.¹⁴⁹ Officially, the United States continued to urge the EC to extend national treatment to non-EC labs on policy grounds, both bilaterally¹⁵⁰ and in the context of the Standards Code.

Mutual Recognition Agreements

EC policy towards current and future mutual recognition agreements continued to evolve in the first 6 months of 1990. The EC did appear to backtrack from its reassuring statements in 1989

¹⁴⁵ USITC field interview, Aug. 9, 1990.

¹⁴⁶ Four of the bills were referred to the Energy and Commerce Committee of the U.S. House of Representatives; one was referred to the Education and Labor Committee. As of Aug. 24, 1990, no action has been taken in either committee.

¹⁴⁷ USITC field interview with CEN, July 19, 1990.

¹⁴⁸ USITC staff interview, Aug. 9, 1990.

¹⁴⁹ USITC interview with representative of a small U.S. testing lab, June 25, 1990.

¹⁵⁰ U.S. Department of State Telegram, July 3, 1990, Brussels, Message No. 10157.

that, in order to avoid disruptions in trade flows, the EC would allow existing member-state agreements on mutual recognition to stand until such agreements could be transferred into EC-wide arrangements. In terms of agreements on additional products in the future, the United States and the EC held several meetings in the January-June 1990 period to evaluate the current situation and to explore options for U.S.-EC agreements on the mutual recognition of test reports, laboratory accreditations, and product-approval schemes.

In bilateral meetings with a Commerce-led U.S. Government delegation on June 13 and 14, the EC said that regardless of the status of ongoing negotiations, existing mutual recognition agreements with member-state authorities would be nullified upon the entry into force of the relevant EC directive. However, the EC Commission officials intimated that to the extent that such arrangements call for something less than issuing certification marks, evaluating conformance, or otherwise exercising judgment—matters that must, according to current EC thinking, remain in the hands of “notified bodies”—they could be transferred into subcontracting arrangements after 1992.¹⁵¹

It remains unclear how significant a problem the expiry of current agreements would be for U.S. exporters and whether the EC itself may have more to lose. Few bilateral agreements currently exist between the member states and U.S. regulatory agencies, and most of those appear to fall short of providing for the automatic acceptance of each other's approvals. The EC and the United States have about the same amount of trade at stake in the area of medical devices, one product area currently covered by an MOU, but the U.S. side of the arrangement currently provides access to the entire U.S. market, whereas the EC side is limited to the British market. Moreover, it is far from certain that the U.S. regulatory agencies and U.S. industry would find acceptance of the EC's conditions for such agreements—reciprocal market opportunities and the recognition of all of the EC's notified bodies—preferable to the expiry of current arrangements. This may be particularly the case if part of the deal entails an increase in testing and surveillance requirements imposed on all suppliers by U.S. regulatory agencies such as the Food and Drug Administration.

The June bilaterals also served as a forum for exploring the prospects for concluding agreements in the future on products covered by “new approach” directives. Based on those discussions, it appears that the current nature of U.S. regulation of such products and the degree of similarity of existing U.S. requirements to those being proposed in the EC will be key variables in determining the

¹⁵¹ U.S. Department of State telegram, July 3, 1990, Brussels, Message Reference No. 10157.

chances of reaching a successful agreement on the mutual recognition of test results.¹⁵² The issues involved, which were discussed in general terms in the previous report,¹⁵³ can be illustrated by the following examples:¹⁵⁴

- EC regulations and product-approval requirements are most similar to U.S. counterparts in the case of medical devices. Most U.S. Federal Government requirements preempt State requirements, thus the Federal Government plays a leading regulatory role. The FDA's Good Manufacturing Practices requirements are similar to the EC's quality-assurance standards; thus the prospect of mutual recognition in this area is good. Several differences are evident, however. The United States does not currently require preproduction quality assurance, something that will be required by the EC in 1992-related directives. On the other hand, the United States imposes more stringent requirements, such as clinical trials and premarket approvals on some 200 high-risk products. These requirements go beyond safety to include efficacy. FDA is also required by law to reinspect higher risk products at least every 2 years. Thus FDA acceptance of EC tests on medical devices would either have to be limited to non-high-risk products or tied to a change to current U.S. law. Alternatively, both countries could agree to raise their requirements to the highest level, potentially requiring a change in both EC and U.S. laws, but paving the way for mutual recognition in all product areas.
- Building products is an area where the U.S. Federal Government has limited jurisdiction, and at first blush it would appear that a multiplicity of requirements and approving authorities may make agreement with the EC on mutual recognition difficult. Individual States regulate building construction, but most States have delegated their responsibility to local governments. There are thousands

¹⁵² U.S. Department of State Telegram, Apr. 13, 1990, Brussels, Message Reference No. 05852. As explained by the U.S. Mission in Brussels, “the asymmetry between U.S. and EC practices with respect to standards, however, will continue to pose a challenge to the United States in those areas in which we wish to conclude mutual recognition agreements. With some exceptions (such as food and drugs and environmental standards) standards in the United States are primarily set in the private sector domain.” Many products covered by new approach directives are not regulated in the United States. For many of those products that are regulated, EC manufacturers are allowed to self-certify the conformity of their products to U.S. requirements, thus obviating the need for mutual recognition agreements.

¹⁵³ For a discussion of these issues, see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-26 to 6-28.

¹⁵⁴ Based on U.S. Department of State Telegram, July 3, 1990, Brussels, Message Reference No. 10157.

of building codes in the United States. The system is, according to one expert, more coherent than it seems, however. Ninety-seven percent of all jurisdictions use one of three model building codes, which are themselves quite uniform in content. Moreover, these codes often refer to the same nationally developed and widely used voluntary standards for particular products. There is some evidence that the States are moving toward uniformity in their building codes and testing and inspection requirements. Lab accreditation and product certification are reportedly increasing in popularity. Nevertheless, ultimate product approval often rests in the hands of individual building inspectors and their local government authorities, thus making it difficult for the U.S. Federal Government, or any other single entity, to provide assurances of nationwide acceptance of EC goods.

In addition to these factors, there are issues such as surveillance of continued laboratory competence, the legal reach of government, and product liability. For example, there is some concern that U.S. labs or certification schemes would be open to increased liability exposure were they to agree in the context of a mutual recognition agreement to accept other bodies' certifications, because the U.S. laboratory or scheme could be held responsible under U.S. product-liability law.¹⁵⁵

In terms of the reciprocity criterion, statements by EC officials during 1990 suggest that securing opportunities for EC-based labs, and perhaps more importantly, ensuring the removal of current obstacles to EC exports associated with product-approval requirements in foreign markets, remain key goals of the EC.¹⁵⁶ Exactly what the EC is looking for in terms of particular product sectors, the level of assurance that would be necessary (Government versus private, Federal Government versus local government), and the scope of coverage of such agreements remained unclear.¹⁵⁷ EC

¹⁵⁵ See, for example, correspondence of July 17, 1990, and Apr. 25, 1990, between James Pearse, Chairman of the Board, ANSI and Bernard H. Falk, Chairman, ANSI Board Certification Study Group.

¹⁵⁶ Based upon U.S. Department of State Telegram, July 3, 1990, Brussels, Message Reference No. 10157, during the course of discussions between U.S. and EC officials on the subject of testing and certification, when asked by the U.S. side to clarify what the EC would deem to be a "balanced situation," the reciprocity criterion included in the Dec. 21, 1989, Council resolution EC officials suggested that in their view a balanced situation depends on a number of factors including the level of potentially affected trade in a particular product sector and whether testing-related barriers exist in the third-country market, irrespective of whether such barriers are associated with Federal requirements, State and local requirements, or market realities.

¹⁵⁷ In meetings with U.S. officials on June 13, 1990, EC Commission officials said that formal mutual recognition agreements for regulated products will be negotiated sector by sector between the EC Commission and the U.S. Government or U.S. body that the EC Commission deems "equivalent" for its ability to oversee competence of U.S. bodies and ensure

Commission officials continued to complain that the complex, overlapping, and sometimes conflicting testing requirements of U.S. regulatory authorities was a serious source of concern and that the lack of an official, central body to deal with on conformity-assessment issues not only frustrated EC attempts to remove testing-related barriers in the U.S. market, but made it unlikely that a balanced U.S. offer could be put together and would stick. The EC complaint has been informally seconded by trade officials in Hong Kong, Canada, and EFTA.¹⁵⁸ As part of its effort to draft negotiating mandates, the EC Commission is in the process of elaborating upon the reciprocity criteria for the conclusion of mutual recognition agreements.¹⁵⁹ In a formal statement, ANSI urged the EC to be flexible in its approach, taking into account the "fact that both the public and private sectors operate 'conformity assessment' systems in the United States."¹⁶⁰

The Modular Approach

As discussed in our previous report, in 1989 the EC Commission proposed a modular approach to conformity assessment in the form of a draft Council decision on the matter.¹⁶¹ The proposed approach would give manufacturers, whenever practicable, a choice among several methods (or modules) for demonstrating product conformance to "new approach" directives. The options would be spelled out in each individual product directive. More rigorous requirements would be imposed on products representing substantial risks and on products that do not conform with harmonized European standards. The Council reached a common position on the EC Commission proposal in June, 1990. The revised proposal appears to be responsive to U.S. concerns that the requirements under the least burdensome module, that describing self-certification, were overly strict.

U.S. industry has been urging the EC to adopt the current U.S. practice of accepting manufacturers' declarations of conformity and privately generated tests as a rule and to strictly weigh requirements for intervention of third

¹⁶⁷ - Continued

coherence and acceptance of EC-generated tests in the United States. In response to a U.S. question, the EC Commission official said that the U.S. Government did not necessarily have to be the signatory to such agreements, but that the EC was seeking something equivalent to a Government guarantee on the acceptance of EC-generated test results. The EC officials underlined that such agreements would have to provide for adequate safeguard mechanisms to ensure the removal of unsafe products from the market and the continued competence of recognized labs. As reported in U.S. Department of State Telegram, July 3, 1990, Brussels, Message Reference No. 10157.

¹⁶⁸ USITC field interview, Geneva, July 19, 1990.

¹⁶⁹ USITC staff interview, Aug. 9, 1990.

¹⁷⁰ American National Standards Institute, "ANSI Views on Relationships Between the United States and Europe on Testing and Certification," July 23, 1990, p. 1.

¹⁶¹ See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-17 to 6-21 for a description of the modular approach proposed by the EC Commission in October 1989.

parties against actual risks and associated costs.¹⁶² In particular, U.S. business had been lobbying in 1990 for a lessening of the stringent requirements of "module A" (manufacturers' declarations of conformity), embodied in the initial draft decision on modules for demonstrating conformity to EC "new approach" directives.¹⁶³ In June 1990, the EC Commission suggested a number of amendments to the draft decision, taking into account the Parliament's opinion on its first reading.¹⁶⁴ The Council reached a common position on the draft decision on June 23, 1990.¹⁶⁵ Parliament is scheduled to consider the Council's position along with the EC Commission's proposed amendments in September 1990, in line with its second reading. The EC Commission expects final adoption of the decision by late October or early November 1990.¹⁶⁶

The EC Commission's proposed amendments were responsive to a number of U.S. concerns.¹⁶⁷ The EC Commission proposed that language be added to the preamble that underlined the need to ensure that conformity-assessment procedures should be clear and should not impose "unnecessarily onerous conditions on manufacturers." Language was also proposed that would permit the Council flexibility in imposing

additional modules if particular circumstances warrant doing so, but urged that such additional requirements be kept to a minimum so as to avoid undercutting the EC's goal of greater uniformity and predictability in conformity-assessment procedures. The Council's draft common position¹⁶⁸ incorporated these amendments.

A number of other changes appear to be consistent with U.S. objectives. The Council's draft common position¹⁶⁹ breaks module A into two separate modules, the first with no intervention by notified bodies and the second providing for (1) required tests on products before they are placed on the market or (2) random spot checks of the product once it has reached the market, both to be conducted by notified bodies. This division may minimize the likelihood of overly stringent requirements being imposed on products representing little risk to health and safety. On the other hand, the new module opens the door to the imposition of additional requirements for higher risk products, consistent with Parliament's May 1990 opinion. Parliament urged a narrow interpretation of the circumstances in which manufacturers would be permitted to issue self-declarations of conformity for dangerous and sophisticated products, citing a need for production monitoring by an independent "notified" body.¹⁷⁰

Greater flexibility in terms of the types of information that must be contained in technical documentation files was also introduced. The draft common position simply says that such documentation shall be laid down in each directive and "shall enable the conformity of the product with the requirements of the Directive to be assessed." This appears to open the door for a lessening of documentation associated with module A, when appropriate, along the lines advocated by U.S. industry.

Finally, the draft common position makes it clear that in modules requiring type-approval by notified bodies, "a type may cover several versions of the product provided that the differences between the versions do not affect the level of safety and the other requirements concerning the performance of the product."¹⁷¹ Where quality assurance is required, it appears that notified bodies will be required to conduct the initial assessment of the quality-assurance system as well as all scheduled followup audits. It would appear that notified bodies may subcontract tests associated with unscheduled (random interval) visits to manufacturers, however.

¹⁶² See, for example, EC Committee of the American Chamber in Commerce in Belgium, *Position Paper on the Global Approach and the Modules for Conformity Assessment Procedures*, Feb. 27, 1990, pp. 2-4, wherein the committee urged the EC Commission to codify more clearly the notion that required conformity assessment in EC legislation should be kept to the least burdensome alternative and wherein it requested a modification of the modular approach document, particularly the requirements of module A (manufacturer's declaration).

¹⁶³ The key issue here is what the EC Committee of the American Chamber of Commerce termed in p. 4 of its Feb. 27, 1990, policy paper "excessive" requirements for technical documentation associated with module A. The committee advocated altering module A by "expanding the variety [of options] within the module or incorporating new modules, while simplifying the procedures," noting that as originally proposed, module A would "actually represent an increase in the amount of regulation" for many manufacturers. It urged the EC to make the requirements of module A, notably the contents of the technical documentation file, more flexible.

(p. 3) There is also some concern that the technical information that must be filed with designated import agents or other representatives in the EC may result in breaches in protection of proprietary business information. This may be particularly the case when a single importer is handling a variety of competing products, according to a USITC staff interview with a trade association official on June 27, 1990. The individual modules are elaborated in Com (89) 209 final, OJ No. C 267, (Oct. 19, 1989). They are described in USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-20 to 6-21.

¹⁶⁴ The Commission's amendments are contained in Com (90) 284 final, reprinted in the OJ, No. C 179, (July 19, 1990), pp. 13-14. Parliament delivered its opinion on the proposed decision on May 14, 1990, but as of June 18, 1990 it had not been published in the *Official Journal*. The Economic and Social Committee's opinion was reprinted in the OJ, No. C 112(May 5, 1990), p. 4.

¹⁶⁵ National Electrical Manufacturers Association, *EC 1992: Update on the European Community's Single Internal Market Program*, No. 7, July 1990, p. 1.

¹⁶⁶ USITC field interview with staff of the EC Commission, July 20, 1990.

¹⁶⁷ Com (90) 284 final, reprinted in the OJ, No. C 179 (July 19, 1990), pp. 13-14.

¹⁶⁸ The draft being analyzed here is dated June 18, 1990. The final common position was not available as of Aug. 11, 1990.

¹⁶⁹ The draft being analyzed here is dated June 18, 1990. The final common position was not available as of Aug. 11, 1990.

¹⁷⁰ National Electrical Manufacturers Association, *EC 1992: Update on the European Community's Single Internal Market Program*, No. 7, July 1990, p. 1.

¹⁷¹ Module B of the draft common position.

Several other of the EC Commission's proposed amendments that were responsive to U.S. concerns do not appear to have been incorporated into the Council's common position. Among them were amendments that would have required notified bodies to protect confidential information,¹⁷² to provide detailed reasons for the denial of type certifications, and to put in place an appeals mechanism for such decisions.¹⁷³ It is unclear to what extent the Council's requirement that notified bodies meet the EN45000 standard could partially ameliorate U.S. concerns on these issues.

Some industry interests had also expressed the hope that the EC Commission would develop "guidelines which clearly describe under what conditions the various modules are to be used," citing uncertainty about the basis upon which modules would be selected for future directives.¹⁷⁴ The EC Commission reports that it presently has no intention of issuing formal guidance on the matter, relying instead on staff-level guidance during the directive-drafting process.¹⁷⁵ However, the EC Commission proposed that new language be added to the decision requiring the EC Commission to spell out the factors—such as the nature of the risks involved, appropriateness of the modules to the types of products, etc.—that it considered in drafting a proposed directive. The Council accepted that amendment in its draft common position.

CE Mark

As noted in our previous report, some confusion has surrounded the requirement that products subject to new approach directives bear the CE mark.¹⁷⁶ This confusion is driven by inconsistency in various new approach directives and a lack of clarity as to the physical form (i.e., ink stamp, brand, stick-on) of the CE mark.¹⁷⁷ For example, some directives say that the manufacturer always attaches the CE mark; others suggest that it is the notified body that does so. A regulation drafted by the EC Commission in 1990—but that has yet to be formally introduced¹⁷⁸—aims to eliminate this

confusion, especially for products that may come within the scope of several directives.

The draft regulation would supersede the existing laws, regulations, and administrative provisions currently in effect in the various member states regarding national marks and replace them with an EC-wide mark of conformity. The CE mark will indicate that the product bearing the mark is in conformity with EC laws, regulations, and administrative provisions pertaining to essential health, safety, and environmental requirements, and that the product can be lawfully marketed throughout the Community.

The subject regulation amends the provisions regarding the CE mark contained in the six directives already adopted, and in the three common positions that have been developed,¹⁷⁹ as well as in the Council Resolution of December 21, 1989. The draft regulation (art. 5) specifies that the manufacturer, the manufacturer's agent, or the importer, not the notified body, is responsible for affixing the CE mark.

Article 2 states that the affixed CE mark indicates the conformity of a product with all Community regulation applying to it, and that the person who affixes the CE mark to the product assumes responsibility for its conformity with all Community regulations applying to it. The third article prescribes that affixing of any mark, sign, or symbol that may cause confusion with the CE mark shall be prohibited. The fourth article specifies that the CE mark of conformity shall be followed by the mark or symbol of the notified body, in accordance with the Council Decision of December 21, 1989, and as outlined in modules for the various phases of the conformity-assessment procedures, where a notified body is involved in the production control phase. This article further provides that other indicative signs such as the last two digits of the year in which the mark was affixed, a pictogram (pictograph) concerning a particular use of the product, or a mark of conformity to a particular standard may be affixed near the CE mark provided that there is no possibility of confusion as to the meaning of these symbols or the mark.

The draft regulation (art. 6) leaves open the possibility that the Community may lay down detailed conditions concerning the affixing of the

¹⁷² On p. 4 of its Feb. 27, 1990 position paper on the matter, the EC Committee of the American Chamber of Commerce in Belgium said "It should be emphasized in the text [of the modular decision] that any information given to 'notified bodies' by manufacturers in connection with accreditation, etc., as proprietary information must be kept totally confidential (therefore, must be restricted to that notified body and must not be passed to other parties, including other notified bodies)."

¹⁷³ On p. 5 of its Feb. 27, 1990, position paper on the matter, the EC Committee of the American Chamber of Commerce in Belgium said, "There is also a need for an organization which can offer speedy means of redress and final arbitration in case of disputes. This is critical to ensuring that manufacturers are not confronted with undue delays and uncertainty."

¹⁷⁴ See, for example, American Chamber in Commerce in Belgium position paper, pp. 4-5 for a discussion of this issue.

¹⁷⁵ USITC field interview with staff of the EC Commission, July 20, 1990.

¹⁷⁶ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-31.

¹⁷⁷ U.S. Department of State Telegram, Apr. 13, 1990, Brussels, Message Reference No. 05852.

¹⁷⁸ U.S. Department of State Telegram, Aug. 6, 1990, Brussels Message Reference No. 11844.

¹⁷⁹ The following directives and common positions may be affected: *Directives*: (1) Council Directive of June 25, 1987, on the Harmonization of the Laws of the Member States Relating to Simple Pressure Vessels (87/404/EEC); (2) Council Directive of May 3, 1988 on the Approximation of the Laws of the Member States Concerning the Safety of Toys (88/378/EEC); (3) Council Directive of December 21, 1988 on the Approximation of the Laws, Regulations and Administrative Provisions of the Member States Relating to Construction Products (89/106/EEC); (4) Council Directive of May 3, 1989, on the Approximation of the Laws of the Member States Relating to Electromagnetic Compatibility (89/336/EEC); (5) Council Directive of June 14, 1989 on the Approximation of the Laws of the Member States relating to Machinery (89/292/EEC); and (6) Council Directive of December 21, 1989, on the Approximation of the Laws of the Member States Relating to Personal Protective Equipment (89/686/EEC). *Common position*: (1) Gas and appliances; (2) Nonautomatic weighing instruments; and (3) Electromedical devices.

CE mark appropriate to the product in the category of products and in particular the condition of (1) the size and position of the CE mark, possibly followed by the mark or identification symbol of the notified body; (2) condition relating acceptable proximity to other indicative signs; and (3) conditions concerning visibility, legibility and indelibility. Article 7 states that all member states shall ensure the legal protection of the CE mark, prohibit confusion of other marks or signs with the CE mark, prevent any abuse of the CE mark, and enact legal penalties for any infringement.

The subject regulation, if passed, would likely have a positive affect on trade with the EC by providing a uniform approach to affixing and use of the CE mark. In addition, importers would be authorized to affix the CE mark to imported products. This authorization should have a salutary impact on trade with the EC for products covered by directives that do not require the approval of a notified body. However, in order to evaluate the possible effect the subject regulation may have on nonmember states, one must also take into consideration the proposed European Community testing and certification policy, as outlined in the proposal the EC Commission submitted to the EC Council for the Community's future approach to conformity assessment.¹⁸⁰ The EC testing and certification policy specifies that products covered by directives that require the approval of a notified body or bodies first need the consent of such body or bodies before the CE mark can be affixed. Such notified bodies are designated by the member-state authorities, and, as discussed above, to date the EC has not agreed to accredit non-EC laboratories and certification bodies as notified bodies.

In a field interview with USITC staff, the EC Commission reported that it has yet to formally propose the draft regulation because Member States have expressed a preference for the requirements to be embodied in a directive instead, allowing them time to implement it and to make the necessary changes in domestic legislation. The most serious stumbling block to the adoption of a more coherent approach towards the CE mark, the EC official said, is the Construction Products Directive. Unlike other "new approach" directives, in the case of construction products, the CE mark signifies conformity with harmonized standards (those developed by CEN/CENELEC), not to the directive's essential requirements.¹⁸¹

Implementation

The Toy Safety Directive formally entered into force on January 1, 1990.¹⁸² It is the first "new

¹⁸⁰ For a discussion of this issue, see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-17 to 6-23.

¹⁸¹ USITC field interview with staff of the EC Commission, July 20, 1990.

¹⁸² The directive is analyzed in detail on pp. 6-114 to 6-118 of USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990.

approach" directive to be implemented, and a number of problems have arisen, many of which, some analysts fear, will be repeated as other "new approach" directives enter into force over the coming years.¹⁸³ Member states have been slow to transpose the directive into national legislation. As of June 14, 1990, only six member states—Portugal, Ireland, West Germany, Greece, France, and the United Kingdom—had actually implemented the directive. A list of notified bodies had not been published as of that date, but EC Commission officials reported that a list for the six countries had been sent to the *Official Journal*, and included some 30 bodies. (Under the directive, manufacturers have the option of either declaring conformity of the product or of obtaining a certificate of compliance from a notified body.) Reportedly Italy has not only failed to transpose the directive into national legislation, it is also failing to actually enforce it by ensuring the products sold on the Italian market meet the directive's essential safety requirements.¹⁸⁴ U.S. producers apparently have experienced shipment delays because Italian Customs officials have insisted that products be recertified in Italy.¹⁸⁵

At the same time, U.S. toy manufacturers have complained that France is imposing administrative burdens over and above those provided for in the directive and is refusing to accept test results from bodies located outside French territory, a matter that is apparently being pursued through both formal and informal channels.¹⁸⁶ Private purchasers in the United Kingdom are requiring third-party certification by European-based notified bodies, even though the directive itself gives producers the option of issuing manufacturers' declarations. The British retailers reportedly fear that failure to require third-party approval could open them up to greater product-liability exposure on the grounds that they did not exercise due diligence in ensuring the product's safety. Meanwhile, a great deal of uncertainty has surrounded the issues of how to handle existing stocks of toys in the EC that do not bear the required CE mark and of where to place the CE mark on packaging. The U.S. firms affected are reportedly mainly larger firms that serve the EC market through direct exports.¹⁸⁷

¹⁸³ Comments by U.S. testing laboratory representative at an ANSI-U.S. Chamber of Commerce conference on testing and certification in the EC held in Washington, DC, June 25, 1990.

¹⁸⁴ Comments by officials of the EC Commission, as reported in U.S. Department of State Telegram, July 3, 1990, Brussels, Message Reference No. 10157.

¹⁸⁵ U.S. Department of State Telegram, June 5, 1990, Rome, Message Reference No. 10824.

¹⁸⁶ David Miller, President, the Toy Manufacturers of America, letter to Bennett Harmon, Office of the United States Trade Representative, Office of EC Affairs, May 1, 1990.

¹⁸⁷ USITC staff interview with representative of the Toy Manufacturers' Association, July 11, 1990.

Part 2. Institutional, Legal, and Policy Framework

Introduction

The two previous USITC reports on the 1992 process¹⁸⁸ examined the EC's standardization effort generally and from a sectoral perspective, focusing on the particular industries affected by EC standards measures. This chapter continues the sectoral approach in section 3 below. This section provides an overview of the institutional, legal, and policy framework for the EC's standardization process. Its aim is to place individual standards directives associated with the 1992 program, as well as evolving policies on testing and certification, in the larger perspective of the policy parameters and institutional underpinnings of the EC's overall regulatory agenda.

In the 1985 White Paper, the EC Commission observed that member states generally had the same goals in mind when issuing technical regulations, namely, "the health and safety of citizens and consumer and environmental protection."¹⁸⁹ The EC recognized that member states have the responsibility to meet such goals,¹⁹⁰ but suggested that if technical barriers among member states were to be minimized, harmonization of member-state laws should be pursued at the EC level in those fundamental areas.¹⁹¹ The EC Commission undertook to focus the Community's future efforts to harmonize technical requirements across the member states on measures designed to meet those objectives.¹⁹² The principle of mutual recognition was to make possible the free movement of goods in the EC when such essential interests were not at stake. Even so, member states may under article 36 enact regulations that are stricter than EC rules, as Denmark did in the case of motor-vehicle emissions.

The discussion below tracks four categories of measures that are at the heart of the EC's standards harmonization agenda. The first three relate to the policy goals of (1) environmental protection, (2) consumer protection, and (3) safeguarding public health and safety. It should be noted, however, that

¹⁸⁸ USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989; USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990.

¹⁸⁹ White Paper, p. 20.

¹⁹⁰ Article 36 of the Treaty of Rome recognizes the importance of such goals to member states by permitting them to impose import restrictions to protect public morality, policy, and security; the health and life of humans, animals, and plants; national artistic, historic, and archaeological treasures; and industrial and commercial property.

¹⁹¹ White Paper, p. 20. European Commission, Directorate-General for Research, *Fact Sheets on the European Parliament and the Activities of the European Community*, PE 122.000, En III/D/2.

¹⁹² This concept was further elaborated in the EC Council Resolution on a New Approach to Technical Harmonization and Standards, May 7, 1985, OJ No. C 136, Annex 3.2, reprinted in EC Commission Document "Common Standards for Enterprises," p. 69.

many of the EC's standardization measures have more than one goal. For example, the line between protection of human health and safety and protection of consumers' interests can be thin, and measures such as the directive on toy safety and restrictions on tobacco advertising can be put into both categories. The last part of this section, on product liability, does not relate to a specific goal listed in the White Paper. Rather, the topic is at the crossroads of the listed goals and forms an important aspect of the 1992 standards agenda. It discusses the roles of legal redress mechanisms in ensuring that responsibility for product safety is properly shared among regulators, manufacturers, and consumers.

As the discussion below makes clear, in some areas the technical regulations and standards-related directives being developed as part of the 1992 program have been framed within the context of a well-defined policy and established institutional mechanisms. The EC has developed a number of fundamental principles in consumer protection and public health and safety, for example. In areas such as the environment, however, the shift in regulatory emphasis from member state to the EC level associated with the Internal Market program has highlighted the need for a more coherent EC-level policy and centralized institutions to oversee it.

Environmental Protection

Policy

Although the EC issued an action program on the environment as early as 1973,¹⁹³ it was only with the passage of the Single European Act (SEA) in 1987 that the EC gained explicit authority to enforce member-state implementation of its environmental legislation. The SEA added a new title on the environment to the EEC Treaty.¹⁹⁴ Central to the theme of this new title is the mandate that, "Environmental protection shall be a component of the Community's other policies."¹⁹⁵ The title reinforces three preexisting EC principles for Community action relating to the environment: prevention, rectification at the source, and the "polluter pays" principle.¹⁹⁶

¹⁹³ The EC Community initiated its first environmental action program in 1973, OJ No. C 112, Dec. 20, 1973, p. 1; its second program in 1977, OJ No. C 139 (June 13, 1977), p. 1; its third program in 1983, OJ No. C 46 (Feb. 2, 1977), p. 1; and its fourth program, which is discussed above in the text, in 1987 OJ.

¹⁹⁴ European Economic Community, "Treaty of Rome," pt. 3, Title VII, added by SEA art. 25.

¹⁹⁵ EEC Treaty, art. 130r, par. 2.

¹⁹⁶ *Ibid.* The "polluter pays" principle was first developed in the Organization for Economic Co-operation and Development (OECD) and then moved to the EC, where it was integrated into EC environmental policy. Representatives of OECD, meeting with USITC staff, Paris, June 8, 1990. The principle was defined in an EC Council Recommendation, as follows: natural or legal persons governed by public or private law who are responsible for pollution must pay the costs of

In preparing action relating to the environment, the treaty, as amended, requires the Community to take account of available scientific and technical data, environmental conditions in the various regions of the Community, the potential benefits and costs of action or lack of action, and the balanced economic and social development of the Community as a whole and its individual regions.¹⁹⁷ The environmental title also speaks to the "subsidiarity" principle, by providing that—

*The Community shall take action relating to the environment to the extent to which the objectives [of protecting the environment] can be better attained at the Community level than at the level of the individual Member States.*¹⁹⁸

However, other provisions of the treaty allow member states, with the EC Commission's approval, to apply their own stricter national measures relating to, among other things, protection of the environment.¹⁹⁹ The EC Commission will confirm such measures only after verifying that "they are not a means of arbitrary discrimination or disguised restriction on trade between Member States."²⁰⁰

The European Community's ability to take effective environmental action was further bolstered by the SEA with the adding of article 100a to the EEC Treaty. Under this article, the Council can approve EC Commission proposals by a qualified majority rather than by unanimity.²⁰¹ The existence of the qualified-majority provision has been a powerful tool in reaching consensus on environmental measures.²⁰²

Article 100a is also significant for environmental action in that it provides the European Parliament (EP) with an advisory role and budgetary powers on environmental proposals.²⁰³ This authority has taken on particular importance because the current EP has high environmental awareness.²⁰⁴ As a

¹⁹⁸ — Continued

such measures as are necessary to eliminate that pollution or to reduce it so as to comply with the standards or equivalent measures laid down by the public authorities. Council Recommendation 75/436/Euratom, ECSC, EEC.

¹⁹⁷ Ibid., par. 3.

¹⁹⁹ Ibid., par. 4.

²⁰⁰ EEC Treaty, art. 100a, par. 4, added by SEA art. 18. In a similar vein, the derogation provision of EEC Treaty art. 36 permits member states to prohibit or restrict imports based on, among other things, "protection of health and life of humans, animals or plants," providing the prohibition or restriction does not "constitute a means of arbitrary discrimination or a disguised restriction on trade between Member States." The European Court of Justice has recognized that the environment is sufficiently important to justify derogation under this provision. USITC staff meeting with staff of French interministerial committee on environmental affairs (SGCI), meeting with USITC staff, Paris, June 11, 1990. For example, this provision was the basis of an EC Court of Justice case upholding a Danish bottling law.

²⁰¹ Ibid.

²⁰² Ibid., par. 1.

²⁰³ Staff of the EC Commission, interview by USITC staff, Brussels, Belgium, June 5, 1990.

²⁰⁴ Ibid.

²⁰⁵ Ibid.

consequence of these powers, the EP has had a growing influence in the environmental area.²⁰⁵

Further in 1987, the EC Council of Ministers (Council) adopted the Fourth Environmental Action Programme, for 1987-92.²⁰⁶ This program calls for the concentration of EC Community action in the following areas: (1) pollution protection (air, water, marine, soil, toxic wastes, chemical, and noise); (2) improvement in the management of natural resources (fauna and flora, environmentally sensitive areas, forests, soil, water resources, the Mediterranean region); (3) international activities; and, (4) development of appropriate instruments to promote environmental protection, such as scientific research, implementation of appropriate standards and EC directives, economic instruments such as taxes and state aids, improved access to environmental information, and increased environmental education.²⁰⁷

In October 1988, the EC environmental ministers adopted an initiative requesting the EC Commission to report to the Council on the environmental dimension of the single market. In response, the EC Commission established a task force for the purpose of identifying key issues and likely environmental impacts of the single market. The task force subsequently issued a comprehensive report on these issues,²⁰⁸ which defines existing EC environmental policy and which has served as a reference for EC environmental action.

The task force report emphasizes five principles for the development of new environmental policy mechanisms: the prevention principle; the polluter pays principle; the subsidiarity principle;²⁰⁹ the principle of economic efficiency and cost-effectiveness; and the principle of legal efficiency.²¹⁰ As noted above, these principles incorporate preexisting EC environmental policy and to varying extents are reflected in measures taken by the EC Commission in the environmental field.

Aside from the EC's broad steps in the environmental area in 1987 and 1988, other factors and events have shaped and strengthened EC environmental policy in the last several years. First, catastrophes such as Seveso, Chernobyl, and the Sandoz have resulted in a number of new directives

²⁰⁶ Staff of the European Parliament, interview by USITC staff, Strasbourg, June 6, 1990.

²⁰⁷ OJ No. C 328 (Dec. 7, 1987), p. 1.

²⁰⁸ Ibid., p. 4.

²⁰⁹ Task Force Report on the Environment and the Internal Market.

²¹⁰ The environmental area is by no means the only area in which subsidiarity plays an important role. As noted elsewhere in this report and the two previous reports, the balance between subsidiarity and harmonization is key to many EC measures. See, e.g., ch. 15, "The Social Dimension." See also *European Report*, No. 1584, Institutions and Policy Coordination, (May 5, 1990), p. 1 (noting that the EP is drafting a report on subsidiarity, which principle is "the keystone of the future EEC Treaty revision for political union.")

²¹⁰ See generally, *Task Force Report*.

or amendments to existing directives.²¹¹ Second, the growth of, and increasing voter support for, the Green Party has resulted in increased emphasis on environmental legislation and enforcement at both the EC and the member-state level.²¹² Third, the last several years have been marked by increasing public interest in and international commitment to environmental action.²¹³

Member-State Differences in Environmental Priorities

There is a noticeable North-South split in the EC regarding the setting of environmental priorities.²¹⁴ Spain, Greece, Portugal, and to a lesser extent, Italy, are comparatively in the earlier stages of environmental development.²¹⁵ The Netherlands,

²¹¹ For example, after the Seveso incident, the EC adopted a directive aimed at the prevention of industrial accidents involving dangerous substances. *Council Directive 82/501 OJ* (June 24, 1982). Among other requirements, this directive established a requirement for quantitative risk assessments. Representative of GE Plastics of Spain, interview by USITC staff, Madrid, June 13, 1990. In the aftermath of the Sandoz fire and the resultant pollution of the Rhine River, this directive was amended to require fire-water-receiving basins and to provide for notification and information to the public on potential accidents. *Council Directive 88/610, OJ No. L 336* (Nov. 24, 1988).

²¹² Between 1979 and 1989, the Greens' voice in the European Parliament increased by 15 percent for the United Kingdom and 6 to 7 percent for France, Italy, and the Netherlands. W. G. Seddon-Brown, manager for public affairs for Monsanto Europe and Chairman of the Environment Subcommittee for the American Chamber of Commerce in Belgium, introductory remarks to the "Environmental and Pollution Liability Seminar," Brussels, Nov. 9, 1989.

One official noted that most complaints regarding member-state compliance with environmental directives come from the Green Party. Staff of the French SGCI, interview by USITC staff, Paris, June 14, 1990. The possible influence of the Green Party is demonstrated by France's "surprise" decision to accept the EC car emissions directive shortly after the Green Party made a strong showing in French April 1989 elections. *Ibid.*

²¹³ For example, membership in British conservation bodies and environmental pressure groups rose from 1.8 million in 1980 to 4 million in 1989 and is projected to rise to 6 million by 1992. Seddon-Brown Remarks. See *Europe Now*, U.S. Dept. of Commerce, International Trade Administration, winter 1989-90, p. 1; Representatives of Waste Management Europe, interview by USITC staff, London, June 4, 1990. In Spain (where the Green Party is only a minor force), a nonpolitical organization—the Spanish Association for Defense of the Environment has played an influential and respected role in environmental policy. Representative of GM Spain, interview by USITC staff, Madrid, June 13, 1990.

²¹⁴ Staff of U.S. Mission to the EC, meeting with USITC staff, Brussels, June 5, 1990; USITC staff meeting with EC Commission staff, Brussels, June 5, 1990; Staff of French Ministry of the Environment, meeting with USITC staff, Paris, June 8, 1990; Staff of Spanish Office for Coordination with the European Community, meeting with USITC staff, Madrid, June 12, 1990; *European Report*, (Aug. 30, 1989), Business Brief, p. 6.

²¹⁵ *Ibid.*; "Greening Europe—The Freedom To Be Cleaner Than the Rest," *The Economist*, Oct. 14, 1989, p. 21. Although Ireland is not a "southern" EC country, its environmental state is more closely aligned with that of the southern countries than with other EC countries. *Ibid.* It may even be that, while the newer EC members are improving their environments, "the quality of the environment in Ireland has been deteriorating in recent years." *European Report*, No. 1556, (Jan. 17, 1990), Internal Market, p. 3.

West Germany, and Denmark are at the other end of the spectrum.²¹⁶

The governments of the southern countries are caught somewhat in a quagmire of choosing between compliance with EC directives and addressing other, more immediate national environmental concerns.²¹⁷ For example, Spain has set out a series of environmental priorities that do not necessarily coincide with those of other EC countries because of the condition of the environment in Spain. Whereas air pollution control and stricter auto emissions are top priorities for West Germany, France, and Denmark, there are more important environmental concerns for Spain at this time. The main environmental problems for Spain are water sources, forest fires, preservation of flora and fauna, and the quality of Mediterranean waters.²¹⁸

As stated in the task force report—

*[T]he problems of the periphery differ, in degree, if not in character, from those of the rest of the Community. The cities of the periphery are growing more rapidly than elsewhere in the Community, they are less well served in terms of mass transit and environmental management [is] relatively undeveloped. The rapid pace of urban development also exacerbates the problems of the rural areas, with depopulation and decline in the rural economy. Many of the periphery's land problems have to do with land use—erosion, habitat destruction, visually destructive developments, etc.—which involve large numbers of individual actions which are technically difficult to monitor and control, and politically to restrict.*²¹⁹

Southern countries such as Spain have accepted the EC environmental policy and are trying to conform their laws to the EC policy.²²⁰ But, these countries believe it is important that their concerns be incorporated into EC environmental policy.²²¹ The EC Commission has responded to the concerns of the southern countries by providing for the establishment and funding of regional environmental projects through the ENVIREG program²²² and by focusing attention on the protection of the Mediterranean region through the MEDSPA program.²²³

²¹⁶ *Ibid.*

²¹⁷ Staff of Spanish Office for Coordination with the European Community, meeting with USITC staff, Madrid, June 12, 1990.

²¹⁸ *Ibid.* The Spanish Minister of Public Works is quoted as quipping at an EC Council meeting that, "As a Spaniard, I would like to have acid rain, because we don't have any rain at all."

²¹⁹ *Task Force Report*, p. 4.6.

²²⁰ Staff of Spanish Office for Coordination with the European Community, meeting with USITC staff, Madrid, June 12, 1990.

²²¹ *Ibid.*

²²² EC Commission, *Commission Initiative Contributing to Protection of the Environment and Promoting Socio Economic Development*, XVI/418/89. See EP resolution on the same, doc. A3-46/90, OJ No. C 96, (Apr. 17, 1990), p. 345.

²²³ *Proposal for a Council Regulation on Action by the Community for the Protection of the Environment in the Mediterranean Region*, Com(89) 598 final (Mar. 13, 1990), OJ No. C 80, p. 9 (Mar. 30, 1990).

Institutional Framework

At the EC Commission level, environmental policy is the responsibility of Directorate-General XI (DG XI), which oversees environment, nuclear safety, and civil protection. The DG addresses environmental policy at four levels: legislative, research, implementation, and financial encouragement through grants or loans.²²⁴ Because of the wide-reaching impact of environmental measures, all DG XI proposals are filtered by the other DGs, and must be approved by all DGs before presentation to the EC Commission.²²⁵ Likewise, all proposals written by other DGs must first pass through DG XI to check for environmental impact.²²⁶

At the European Parliament level, environmental policy is the responsibility of the Committee on Environment, Public Health and Consumer Protection. Of the 17 EP committees, this committee is the busiest.²²⁷ Many of the matters handled by this committee are trade related. For example, the auto emissions standard historically has been dealt with as a trade matter, but it is handled by the environmental committee.²²⁸ As noted above, the EP's budget and consultation authority under EEC Treaty article 100a has given it the vehicle for increased influence in the formulation of EC environmental policy.²²⁹

For the last 6 years, the coordination of Communitywide environmental data has fallen under the auspices of an EC Commission work program called the CORINE programme.²³⁰ In 1985, the Council approved this program as an experimental project for gathering, coordinating, and assuring the consistency of Community environmental information.²³¹ The data collected from this program has been used in drafting EC directives and member-state environmental laws.²³²

The Council specified that the CORINE project would run for an initial period of 4 years, ending on

²²⁴ "Directorate-General Environment, Nuclear Safety and Civil Protection," publication of the EC Commission.

²²⁵ DG XI staff, meeting with USITC staff, Brussels, June 7, 1990.

²²⁶ Ibid.

²²⁷ European Parliament staff, meeting with USITC staff, Brussels, June 6, 1990.

²²⁸ Ibid.

²²⁹ Ibid.; EC Commission staff, meeting with USITC staff, Brussels, June 5, 1990.

²³⁰ See *Communication From the Commission to the Council and the European Parliament Concerning the Corine Programme - Results and Future Guidelines at the Halfway Stage in Accordance With Article 3 of the Decision of the Council of 27 June 1985*, Com (88) 420 final (July 22, 1988).

²³¹ Council Decision of June 27, 1985 on the Adoption of the Commission Work Programme Concerning an Experimental Project for Gathering, Coordinating and Ensuring the Consistency of Information on the State of the Environment and Natural Resources in the Community, 85/338, OJ No. L 176 (July 6, 1985), p. 14. Staff of Task Force on the European Environmental Agency (EEA), meeting with USITC staff, Brussels, June 5, 1990.

²³² Ibid.

January 1, 1989.²³³ At the end of the 4-year period, the EC Commission announced and proposed the creation of a European Environmental Agency (EEA), which would continue the work undertaken in the CORINE program.²³⁴ The EC Commission also proposed, and the Council approved, a 2-year extension of CORINE during the transitional period for the operation of the EEA.²³⁵

After much debate, the Council, on May 7, 1990, adopted a regulation establishing the EEA and the European environment information and observation network.²³⁶ A hotly debated question surrounding the formation of the EEA concerned the extent of the agency's authority. The original EC Commission draft contemplated that the EEA would serve as a center for gathering and assessing environmental data.²³⁷ The EC Commission took the position that the EEA would take on responsibilities of scientific and technical control, but only under the political and legal surveillance of the EC Commission.²³⁸ The EP, on the other hand, favored empowering the EEA with policy and enforcement powers, to be carried out by a "green police force."²³⁹ This force would consist of Community inspectors who were entitled to carry out environmental and nuclear safety inspections in member states and to check the work of member-state inspection agencies.²⁴⁰ The final version adopted by the Council represents a compromise under which the EEA initially will be charged only with recording, collating, and assessing environmental data; but within 2 years, the agency's powers will be reviewed with an eye towards extension of its authority.²⁴¹

²³³ 85/338/EEC, OJ No. L 176 (July 6, 1985), p. 14.

²³⁴ Proposal for a Council Regulation for the Establishment of the European Environmental Agency and the European Monitoring and Information Network, Com (89) 303 final, OJ No. C 217 (Aug. 23, 1989), p. 7. See EC Commission publication on CORINE, October 1989, p. 7.

²³⁵ Proposal for a Council Decision Amending Council Decision 85/338/EEC in Order to Provide for the Continuation of the Commission Work Programme Concerning an Experimental Project for Gathering, Coordinating and Ensuring the Consistency of Information on the State of the Environment and Natural Resources in the Community, Com (89), 542, OJ No. C 68 (Oct. 21, 1989), p. 7; Council Decision Amending Decision 85/338/EEC on the Adoption of the Commission Work Programme, 90/150/EEC, OJ No. L 81 (Mar. 3, 1990), p. 38.

²³⁶ Council Regulation No. 1210/90, OJ No. L 120 (May 11, 1990), p. 1.

²³⁷ OJ No. C 217 (Oct. 23, 1989), p. 7.

²³⁸ Europe, No. 5194 (Feb. 15, 1990).

²³⁹ European Report, No. 1564 (Feb. 16, 1990), Internal Market, p. 8.

²⁴⁰ Ibid.; Europe, No. 5186, (Feb. 3, 1990); OJ No. C 68 (Mar. 19, 1990), p. 50 (text of European Parliament's proposed amendments to EC Commission's proposal).

²⁴¹ Council Regulation 1210/90, arts. 2 and 20. See European Report, No. 1572 (Mar. 16, 1990), Internal Market, p. 6. The European Parliament had asked for 90 amendments to the EC Commission's proposed regulation. OJ No. C 68 (Mar. 19, 1990), p. 50. The Council adopted some, but not all, of these amendments. Member of EC Commission staff, meeting with USITC staff, June 5, 1990. The European Parliament was angered at the EC Commission's failure to consider all of the amendments and has threatened both to sue the Council and to block money for the EEA. Ibid.

The EEA will be an independent body consisting of 12 members from each member state, 2 members from the EC, and 2 members from the EP.²⁴² All board decisions must be unanimous. The budget and number of agency personnel in the EEA will be low. For the first year, the EEA budget is only 2 million ECU. Initially, the EEA's main purpose will be to collect information, which will then be used as a tool in developing environmental policies.²⁴³ If the EC Commission follows a similar practice to that used with respect to the CORINE project, it likely will look to the EEA for advice in writing proposals.²⁴⁴

The controversial question regarding the location of the EEA has yet to be resolved. All member states except Luxembourg proposed sites for the agency, but the choice most likely will be between Copenhagen and Madrid.²⁴⁵

Environmental Measures

EC Legislation

Currently, the vast majority of EC environmental instruments are in the form of directives that must be implemented by the member states.²⁴⁶ In view of notorious problems with implementation of the environmental directives (discussed below), the European Parliament and some experts in the field favor a move towards the use of self-enforcing regulations rather than directives.²⁴⁷

In addition to the regulation establishing the EEA, the EC recently has adopted several other environmental measures that are likely to affect all industry sectors. In June 1990, the Council of Ministers adopted a directive on the freedom of information on the environment.²⁴⁸ Under the directive, member states must ensure that public authorities, upon the request of any person, make available "information relating to the environment."²⁴⁹ The requestor is not required to

²⁴² Staff of the Task Force on the EEA, meeting with USITC staff, Brussels, June 5, 1990.

²⁴³ Most of the environmental work will be performed under large contracts within six environmental "thematic centers" representing broad environmental categories, e.g., water, air. The EEA will ask member states which of the institutions within their states could be a center of excellence in one "theme." The EEA will have a contract with the state agency in that area. Once this system is in place, all materials relevant to the particular theme will be sent to the appropriate thematic center. For example, all water data will be sent to the water-quality thematic center rather than to the EEA. *Ibid.*

²⁴⁴ *Ibid.*

²⁴⁵ European Parliament, meeting with USITC staff, June 6, 1990.

²⁴⁶ Staff of European Parliament, meeting with USITC staff, Brussels, June 6, 1990.

²⁴⁷ *Ibid.*; Representatives of Waste Management Europe, meeting with USITC staff, London, June 4, 1990.

²⁴⁸ Council Directive 90/313, OJ No. L 158 (June 23, 1990), p. 56.

²⁴⁹ *Ibid.* "Information relating to the environment" is defined as follows:

any available information in written, visual, aural or data-base form in the state of the water, air, soil, fauna, land and natural sites, and on activities (including those which give rise to

prove an interest as a precondition to receiving the information.²⁵⁰ Like the U.S. Freedom of Information Act (FOIA), the EC directive allows for exceptions to the disclosure requirement.²⁵¹ For U.S. and other businesses, this directive raises concerns about exactly what type of information falls under the exception for commercial or industrial confidential information.²⁵² For example, industry representatives are concerned that this directive could be used to inform one company about particular products under development by another company.²⁵³ In addition, the U.S. Committee of Amcham is concerned about the absence of a provision for notification to companies when information has been requested relating to their specific operations.²⁵⁴

Another area in which EC legislation is likely to have cross-sector impact involves management of hazardous waste. There are existing or proposed EC measures addressing waste disposal and recycling,²⁵⁵ transborder shipment of hazardous waste,²⁵⁶ radioactive waste shipment,²⁵⁷

²⁴⁸ — Continued

nuisances such as noise) or measures adversely affecting, or likely so to affect these, and on activities or measures designed to protect these, including administrative measures and environmental management programmes. Ibid., art. 2(a).

²⁵⁰ *Ibid.*, art. 3. Some member states, including Belgium, West Germany, Spain, and the United Kingdom, would have preferred that the requestor be required to prove a direct interest or show a need for the information. *European Report*, No. 1572 (Mar. 16, 1990), *Internal Market*, p. 5; 1992 — *The External Impact of European Unification*, Buraff Publications, vol. 2, No. 2 (Apr. 20, 1990), p. 2. The U.S. Freedom of Information Act (FOIA) has no such requirement, either explicitly or as construed by the U.S. courts. See 5 U.S.C. sec. 552.

²⁵¹ See 5 U.S.C. sec. 552(b). Under the EC directive, member-state legislation may provide for denial of a request for information that affects the confidentiality of government proceedings; international relations; national defense; public security; matters under inquiry or investigation; commercial confidentiality, including intellectual property; the confidentiality of personal data; voluntarily supplied third-party material; and material that, if disclosed, is likely to damage the environment. *Council Directive 90/313*, art. 3.

²⁵² Representative of Amcham Environment Sub-Committee, meeting with USITC staff, Brussels, June 5, 1990; EC Committee of Amcham in Brussels, *Business Guide to EC Initiatives*, spring 1990, p. 36. (*Business Guide*).

²⁵³ Representative of Amcham Environment Sub-Committee, meeting with USITC staff, Brussels, June 5, 1990.

²⁵⁴ *Business Guide*, p. 36.

²⁵⁵ *Council Directive 73/442*.

²⁵⁶ *Council Directive 84/631*, OJ No. 181/86 (June 12, 1986).

The numerous issues surrounding the shipment of hazardous waste from the country in which it is generated to another country for final disposal have international implications well beyond the scope of this report. For example, a number of these questions are addressed in the Basle Convention on the control of transfrontier movements of hazardous waste, which the EC and certain member states signed in March 1989. DG XI staff, meeting with USITC staff, Brussels, June 7, 1990; OECD representatives, meeting with USITC staff, Paris, June 8, 1990; *European Report*, No. 1577 (Apr. 3, 1990), *External Relations*, p. 8. For a detailed discussion of the EC's existing directive on transfrontier shipment of hazardous waste, see M.E. Kelly, "International Regulation of Transfrontier Hazardous Waste Shipments: A New EEC Environmental Directive," *Texas International Law Journal*, vol. 21, No. 1, (winter 1985), p. 85.

²⁵⁷ *Programme of the Commission for 1990*, p. 22.

waste-water treatment,²⁵⁸ air pollution caused by waste incineration,²⁵⁹ and civil liability for damage caused by waste.²⁶⁰ Consistent with the prevention principle articulated in the SEA, a common thread in these measures reflects the EC's aim to limit the production of waste.²⁶¹

The goal of reducing waste production is the basis for the EC Commission's proposal for the directive on civil liability for damage caused by waste.²⁶² That directive creates an exception to the polluter-pays principle by holding the producer of the waste strictly liable for damage even after the waste is out of the producer's hands. However, the producer can transfer liability to a licensed waste disposal enterprise, by transferring the title property, and risk.²⁶³ The proposed directive is based on the view that holding the producer liable will give companies the incentive to restrict the production of waste.²⁶⁴ The draft directive excludes punitive damages but includes the cost of restoring the environment and of preventative measures.²⁶⁵

The proposed civil liability directive is also somewhat controversial in that it allows public interest groups to sue for "injury to the environment."²⁶⁶ However, the proposal does not require that member states allow such suits; rather, it preserves this right for member states.²⁶⁷ In certain member states (the Netherlands and Luxembourg, and to a lesser extent, France and Italy), environmental groups already have the right to sue for damage to the environment. The proposed EC directive notes that this right should be respected but does not require that this right be allowed across the EC. It is left to the individual

member states to decide whether to allow such suits.²⁶⁸

The draft civil liability directive does not address the means for establishing a mandatory system of insurance to protect against environmental liability.²⁶⁹ The EC Commission and EP have, however, received input from insurance companies on this subject.²⁷⁰ From the standpoint of U.S. business interests, some uniformity for required insurance is desirable.²⁷¹ As long as the EC or individual member states allow for arbitrary insurance requirement, there is a potential for discrimination, they believe.²⁷²

Other environmental areas in which there are significant pending or recently adopted EC measures include water pollution, air pollution, biotechnology, and labeling.

Fiscal Incentives

A key aspect of environmental policy under the EC's current, Italian presidency involves the use of economic instruments as incentives or disincentives to orient environmental behavior.²⁷³ Fiscal instruments to achieve this end can take several forms, e.g. environmental taxes (ecotaxes), state aids (which must be approved by the EC Commission),²⁷⁴ or pollution charges. To the extent any such incentives already exist, they have been adopted by local or member-state governments, rather than by the Community as a whole.²⁷⁵

For example, Italy recently introduced ecotaxes on plastic bags and on pesticides and fertilizers; Denmark taxes chlorofluorocarbons (CFCs), certain plastic products, and packaging and containers; and Belgium has introduced taxes on waste, water, and sewage, the revenues of which will go into a newly established environmental fund.²⁷⁶ Several member states, including West Germany, Denmark, Belgium, the Netherlands, and Greece, offer subsidies for "clean" cars, i.e., cars that use lead-free

²⁶⁸ Ibid. One industry representative observed that by allowing anybody to bring suit for injury to the environment, this proposal has the potential negative impact of moving away from national management of environmental policy towards court management of environmental policy. Representative of waste management energy, London, June 4, 1990. The court-management approach that has evolved in the United States could be particularly problematic for companies operating in the EC given that the various EC countries each have different legal systems. Ibid.

²⁶⁹ AMCHAM, *Business Guide*, p. 30.

²⁷⁰ EC Commission staff, meeting with USITC staff, Brussels, June 5, 1990.

²⁷¹ Representatives of OECD, meeting with USITC staff, Paris, June 8, 1990.

²⁷² Ibid.

²⁷³ EC staff, meeting with USITC staff, Brussels, June 5, 1990.

²⁷⁴ Under EEC Treaty art. 92, state aids are allowed only insofar as they are "compatible with the foreign market."

²⁷⁵ Ibid.; *Task Force Report*, pp. 2.21 to 2.26; J. Wayles, "Italy Wants Joint EC Economic Action on Environment Protection," *Financial Times*, Aug. 1, 1990, p. 2.

²⁷⁶ *Task Force Report*, 2.26; "EC Looks at New Taxes To Curb Environmental Harm," 1992 - *The External Impact of European Unification*, vol. 2, No. 6 (June 15, 1990), p. 4.

²⁷⁷ Ibid.; EC Commissioner's staff, meeting with USITC staff, Brussels, June 5, 1990.

²⁵⁸ OJ No. C 1/90 (1989).

²⁵⁹ Council Directive 89/369, OJ No. L 163/89 (June 8, 1989); Council Directive 89/429, OJ No. L 203/89 (June 21, 1989).

²⁶⁰ Com (89) 282 final (Sept. 15, 1989).

²⁶¹ European Parliament staff, meeting with USITC staff, Brussels, June 6, 1990; DG-XI staff, meeting with USITC staff, Brussels, June 7, 1990. See, e.g., *Amended Proposal for a Council Directive on Hazardous Waste*, Com (89) 560 final, OJ No. C 636 (Dec. 12, 1989), p. 6; *Proposal for a Council Directive on Civil Liability for Damage Caused by Waste*, Com (89) 282 final (Sept. 15, 1989).

²⁶² Com (89) 282 final (Sept. 15, 1989); OJ No. C 251 (Oct. 4, 1989).

²⁶³ Ibid.; OECD representatives, meeting with USITC staff, Paris, June 8, 1990.

²⁶⁴ European Parliament staff, meeting with USITC staff, Brussels, June 6, 1990; DG-XI staff, meeting with USITC staff, Brussels, June 7, 1990; SGCI staff, meeting with USITC staff, Paris, June 11, 1990.

²⁶⁵ DG-XI staff, meeting with USITC staff, Brussels, June 7, 1990.

²⁶⁶ Com (89) 282, art. 4(4). Representative of waste management energy, meeting with USITC staff, London, June 4, 1990. While the European Parliament favors inclusion of this provision, some member-state parliaments have expressed concern about allowing any member of the public to sue for environmental injury. European Parliament staff, meeting with USITC staff, Brussels, June 6, 1990. As such, it is unlikely that the Council will adopt the proposed directive with this provision intact. Ibid.

²⁶⁷ DG-XI staff, meeting with USITC staff, Brussels, June 7, 1990.

gas and have catalytic converters.²⁷⁷ France makes use of environmental subsidies by providing up to 50 percent of nonprofit investment costs for equipment used for prevention, reduction, or measuring of atmospheric pollution.²⁷⁸

EC Environment Commissioner Carlo Ripa di Meana recently announced plans to introduce various ecotaxes at the Community level.²⁷⁹ The package of measures would include taxes on emissions of carbon dioxide and CFCs, permits for toxic waste producers, and refundable deposits on items such as bottles and packaging.²⁸⁰ As an alternative to an emissions tax, the EC is considering imposing a fossil-fuel tax at the point of importation or production but will not impose such a tax unless the United States and Japan agree to do the same.²⁸¹

The EC Commission is also discussing the use of pollution licenses.²⁸² Under this proposal, every business would be granted a transferable license to discharge a certain amount of pollution each year. This proposal, however, is unpopular with the Greens because they believe it encourages pollution. The advocates of licensing argue that this system forces companies to account for environmental charges up front on their balance sheets.²⁸³

Member-State Implementation

In the environmental area, there currently are over 300 pending infraction proceedings by the EC Commission against member states.²⁸⁴ However, this figure includes matters at any stage, from those for which letters of notice have been issued to those that have been referred to the Court of Justice.²⁸⁵ Further, the figure combines cases involving member states' failure to adopt required national legislation, member-state adoption of national legislation that is only in partial compliance with the relevant EC directive, and improper application by the member state of its required national legislation.²⁸⁶ Of 362 cases on which the EC Commission had taken action as of December 1989, 60 involved failure to adopt, or communicate adoption of, legislation; 90 alleged partial compliance; and 213 involved improper application.²⁸⁷

The number of cases initiated increased markedly after 1985, largely because of an

²⁷⁹ European Report, No. 1571 (Mar. 14, 1990), Business Brief, p. 6.

²⁷⁸ "EC Looks at New Taxes To Curb Environmental Harm," 1992—*The External Impact of European Unification*, vol. 2, No. 6 (June 15, 1990), p. 4.

²⁸⁰ *Ibid.*

²⁸¹ *Ibid.*; EC Commission staff, meeting with USITC staff, Brussels, June 5, 1990.

²⁸² *Ibid.*

²⁸³ *Ibid.*

²⁸⁴ MEP staff, meeting with USITC staff, Brussels, June 6, 1990; *Europe*, No. 5192 (Feb. 12/13, 1990), p. 11.

²⁸⁵ *Ibid.*

²⁸⁶ *Europe*, No. 5195, (Feb. 12/13, 1990), p. 11.

²⁸⁷ *Ibid.*

increasing number of complaints received by the Commission.²⁸⁸ In this regard, the number of cases initiated against any particular member state is somewhat affected by the number of complaints filed against that state, which in turn is affected by factors such as the influence of the Greens or other environment groups in that country.

The member states that have been cited the least often are Luxembourg and Denmark, which have high environmental awareness and which generally adopt and enforce required national legislation as prescribed by the relevant EC directives.²⁸⁹ Spain has been cited the most often.²⁹⁰ But, as noted in the discussion of the north-south differences, it has started from a position well behind those of most member states and has made great progress since it joined the EC.²⁹¹ Spain has not been given many of the same time allowances granted to Portugal.²⁹² In many of the other member states, implementation of environmental directives is hindered by the same types of internal and administrative problems that generally create implementation problems.²⁹³

Many of the implementation actions involve directives that require member states to introduce cleanup projects.²⁹⁴ This is particularly true for the directives on bathing water and the disposal of toxic waste.²⁹⁵ In addition, the EC Commission recently has instituted a number of actions against member states, including the United Kingdom, West Germany, France, and Belgium, for failure to implement the drinking water directive.²⁹⁶

In some instances, the member states have not agreed among themselves as to the proper interpretation of a directive. For example, each of the 12 member states came up with a different interpretation of the Seveso directive.²⁹⁷ Similarly, the member states have not been consistent in their interpretations and application of Community air pollution directives. West Germany has adopted especially stringent air emissions standards, TA Luft, which may eventually set the norm for the rest of the Community.²⁹⁸ The EC Commission has

²⁸⁸ *European Report*, No. 1556, (Jan. 17, 1990), Internal Market p. 2; 1992—*The External Impact of European Unification*.

²⁸⁹ *European Report*, No. 1556 (Jan. 17, 1990), Internal Market, p. 2.

²⁹⁰ *Ibid.*

²⁹¹ *Ibid.*; Staff of U.S. Embassy in Madrid, meeting with USITC staff, July 12, 1990.

²⁹² *Ibid.*

²⁹³ See ch. 1 of USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989; USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, and this report.

²⁹⁴ *European Report*, No. 1556 (Jan. 17, 1990), Internal Market, p. 2.

²⁹⁵ *Ibid.*

²⁹⁶ *Ibid.*; DG XI staff, meeting with USITC staff, Brussels, June 7, 1990; *European Report*, No. 1541 (Nov. 16, 1989), Internal Market, p. 2; Lafayette Publications, *Europe—1992: The Report on the Single European Market*, December 1989, p. 457; *Europe*, No. 5169, Jan. 11, 1990, p. 8.

²⁹⁷ *European Report*, No. 1556 (Jan. 17, 1990), Internal Market, p. 2.

²⁹⁸ Representatives of GE Plastics de Espana, meeting with USITC staff, Madrid, June 13, 1990. U.S. air emissions standards contain requirements similar to those of TA Luft.

instituted an action against France for failure to enact a law implementing the EC air pollution directive, but France continues to believe that its existing law meets the EC requirements.²⁹⁹

Both Spain and the United Kingdom have had problems complying with the EC directive on sulfate and hydrates in power plants. Because of the type of coal used, these countries are having difficulty meeting the levels set by the directive. In order to comply with the directive, Spain will have to stop using coal imported from the United States.³⁰⁰

The greatest number of the reported environmental-infracture procedures involve directives aimed at protection of natural resources, particularly against Spain, France, and Greece.³⁰¹ An action that is receiving a great deal of attention in France involves a series of EC directives aimed at the protection of birds.³⁰² One of the directives requires the designation of special zones for the protection of birds. The EC Commission insisted that France designate 70 specific zones. However, in some of the zones that the Commission wanted to designate, hunting still takes place. France interpreted the directive differently from the EC Commission and successfully argued to the Court of Justice that the directive is not as specific as the EC Commission claimed.³⁰³

There currently are pending in the member states various proposed environmental laws aimed mostly at emission reductions and establishment of liability.³⁰⁴ This year, France published its Plan Vert, which provides for quantitative water quality and air emissions objectives, new financial measures for environmental protection, reorganization of the Ministry of the Environment, and establishment of more efficient enforcement mechanisms. In Italy, there is draft legislation pending on emission reduction. Under consideration in the Netherlands is a national environmental policy plan, which provides for long-term (20 to 50 years) environmental protection. As of 1990, Spain will require generators and disposers of toxic and dangerous substances to obtain insurance against environmental damage. Spain is also considering a law imposing retroactive liability for contamination, which, if passed, would affect successor companies. In the United Kingdom, the proposed Green bill would require integrated control of emissions to air, land, and water.³⁰⁵

²⁹⁹ Staff of French Ministry of the Environment, meeting with USITC staff, Paris, June 8, 1990.

³⁰⁰ Staff of U.S. Embassy Madrid and staff of Spanish Office for Coordination with the European Community, meetings with USITC staff, Madrid, June 12, 1990.

³⁰¹ *Europe*, No. 5192 (Feb. 12/13, 1990), p. 12.

³⁰² *European Report*, No. 1556 (Jan. 17, 1990), Internal Market, p. 3; Staff of French Ministry of the Environment, meeting with USITC staff, Paris, June 8, 1990.

³⁰³ *Ibid.*

³⁰⁴ Notes prepared by Alberto Murillo, GE Plastico de Espana.

³⁰⁵ *Ibid.*

Implications for U.S. Firms

Compliance with EC environmental laws will increase operating costs for all businesses operating in the EC, including U.S. firms with operations in the EC.³⁰⁶ Industry representatives and Government officials uniformly agree that EC environmental directives will affect business planning and operations. In this regard, an industry representative experienced in environmental matters believes that the directive on civil liability for damage caused by waste will likely force large operations to have onsite facilities for waste disposal and landfill.³⁰⁷ According to this expert, the EC introduction of a list of wastes that may not be landfilled will force onsite incineration or recycling.³⁰⁸ Similarly, the EC Commission staff responsible for drafting EC water directives is aware that the costs of complying with such directives may influence a company's decision to continue operations, open a new plant, or close a plant.³⁰⁹

In addition to the costliness of compliance, some industry representatives believe that inconsistencies within the EC standards and among the various member-state laws will make investment decisions uncertain.³¹⁰ Likewise, investment decisions are made difficult in light of the uncertainties as to which directives will become law and when they must be implemented. These decisions are particularly difficult with respect to a company's efforts to arm itself against potential environmental liabilities.³¹¹

In some member states, such as Spain, U.S.-based firms are leaders in environmental compliance. For example, the Spanish Government recently gave GM Spain an award for its environmental program.³¹²

Another project by a subsidiary of a U.S. company provides a model for compliance with EC environmental compliance. GE Plastics recently negotiated an agreement with the Government of Spain to develop a facility in Cartagena-Murcia in southeast Spain.³¹³ Because the facility will be built from scratch, it will have state-of-the-art environmental controls. Fifteen percent of GE

³⁰⁶ U.S. Chamber of Commerce, *EC Technology Policy* (1989), p. 71.

³⁰⁷ Representative of GE Plastics of Spain, meeting with USITC staff, Madrid, June 13, 1990.

³⁰⁸ *Ibid.*

³⁰⁹ DG XI staff, meeting with USITC staff, Brussels, June 7, 1990.

³¹⁰ Representatives of Waste Management Europe, meeting with USITC staff, London, June 4, 1990.

³¹¹ Representative of GE Plastics of Spain, meeting with USITC staff, Madrid, June 13, 1990.

³¹² Representative of GM Spain, meeting with USITC staff, Madrid, June 13, 1990.

³¹³ Representatives of GE Plastics of Spain, meeting with USITC staff, Madrid, June 13, 1990. During the negotiations, two sites were considered — this one and another in northern Spain. GE also gave consideration to sites in other EC countries, e.g., Scotland. Based on the incentives package offered by Spain, GE choose the Murcia site. Under the agreement with Spain, GE was given 750 hectares of land.

Plastic's investment will be used for environmental-control measures. However, these measures will go beyond what is currently required by EC or Spanish law, because GE Plastics, like many other U.S.-owned firms, complies worldwide with U.S. environmental standards.³¹⁴

Included in the package negotiated between GE Plastics and the Spanish Government were water rights. In southeast Spain, where the plant will be located, water is a precious commodity. GE Plastics is taking water from a farming community to develop the plant. In turn, the company is developing a waste-water treatment process to allow recycling of the water to the community. To develop this process will involve major expenditures on processes such as tertiary treatment, carbon treatment, and reverse osmosis.³¹⁵

In addition to the waste-water treatment plant, GE Plastics will build its own onsite hazardous waste incinerator, which will handle 100 percent of the plant's waste disposal. Of the solid waste, 75 to 80 percent will be thermally destroyed; the remaining 15 percent will turn to ashes, which, because they could be toxic, must not get into the water. Therefore, GE Plastics will have its own landfill, where the ashes will be stabilized with cement. There will be no underground piping for the sewers, in order to avoid leaks.³¹⁶

Industry representatives believe that the increase in EC environmental legislation has created and will continue to create opportunities for environmental consultants, attorneys, and engineers, as well as environmental-control companies.³¹⁷ Some U.S.-owned environmental firms operating in the EC view the tightening of technical regulations in the EC as beneficial, because these firms are already in compliance with U.S. environmental laws.³¹⁸

Some member states, such as West Germany and the Netherlands, already have many environmental laws in place. Opportunities for environmental firms already are good in these countries, because the clients seek and understand environmental expertise.³¹⁹ In addition, these firms expect more opportunities to open in the other member states more directives are implemented.³²⁰

However, one industry representative opined that it will become increasingly difficult for small environmental businesses to compete successfully, especially if they have not already formed alliances with indigenous firms.³²¹ According to this

³¹⁴ Ibid.
³¹⁵ Ibid.
³¹⁶ Ibid.
³¹⁷ Ibid.; Representatives of Waste Management Europe, meeting with USITC staff, London, June 4, 1990.
³¹⁸ Ibid.
³¹⁹ Ibid.
³²⁰ Ibid.
³²¹ Ibid.

representative, such alliances are critical for U.S. firms, in order to understand cultural nuances and relationships and to adapt to changing local circumstances.³²²

Small and medium-size firms, however, may find "coattail" opportunities with projects such as the development of GE Plastics' Murcia project.³²³ For the Murcia project, GE Plastics has used a joint venture consisting of three consulting firms, including one U.S. firm. In addition to the consulting firms, GE Plastics will employ up to 20 U.S. engineers (the same engineers who built GE Plastics' facilities in the United States.)

Finally, the movement in the EC towards stricter environmental standards may be beneficial for American firms involved in the design and sale of pollution-control systems.³²⁴ Since these firms have long been manufacturing products that must meet already-strict U.S. standards, the firms are likely to find an expanding market in the EC for exports of their products.³²⁵

Consumer Protection

Policy

Consumer protection is an important topic that involves many areas of EC policy besides standardization *per se*, including policies relating to agriculture, transport, tourism, competition, insurance, and banking.³²⁶ In the standards area, labeling requirements, advertising restrictions, and standards for service have been employed in an effort to ensure that consumers' "right to know" is protected and to prevent fraudulent or misleading claims by suppliers. All of the EC's consumer protection measures are discussed here in the standards chapter, although many of them clearly have relevance to other portions of the report.³²⁷

The original Treaty of Rome did not explicitly establish consumer protection policy as an EC goal. However, the interests of consumers have been protected by such longstanding EC programs as EC competition law, which forbids unfair practices that can drive up consumer prices.

At a meeting in Paris in October 1972, the EC heads of state and government identified "improvement in the quality of life" as an important EC goal and set about creating a consumer protection policy. The Council adopted a first consumer program in April 1975, proclaiming five basic rights:

³²² Ibid.
³²³ Staff of U.S. Embassy Madrid, meeting with USITC staff, June 12, 1990; Representative of GE Plastics of Spain, meeting with USITC staff, Madrid, June 13, 1990.
³²⁴ U.S. Chamber of Commerce, *EC Technology Policy*, 1989, p. 71.
³²⁵ Ibid.
³²⁶ Benedicte Federspiel, Vice President, European Bureau of Consumers' Unions (BEUC), *Europe*, No. 5198, (Feb. 21, 1990), (New Series), p. 14. The BEUC is one of the strongest lobbies in Brussels. *Europe* 92, (newsletter), vol. 1, issue 4.
³²⁷ For further discussion of such topics as competition and financial sector, see other chapters in this report, notably chs. 5 and 9.

1. The right to safeguards for health and safety;
2. The right to protection of consumers' economic interests;
3. The right to redress of damages;
4. The right to information and education; and
5. The right to representation.

A second program was adopted in May 1981, which confirmed the original program's aims but stressed the importance of value for money, of services, and of dialog between consumers' representatives and public and private sector decisionmakers.³²⁸

In spite of the various declarations and programs, progress in consumer protection was slow, in part because EC businesspeople considered such measures too expensive except in time of plenty. In 1986, the EC Commission issued a communication approved by the Council reaffirming the importance of consumer protection. In October 1986, the Council recognized the need to involve consumers more in EC decisionmaking, including putting more consumer representatives on the Economic and Social Committee as well as on European and national standardsmaking bodies.³²⁹ In December 1986 and November 1989, the Council stressed that consumer policy must be integrated into other common policies.³³⁰ Article 100A(3) of the Treaty of Rome, added by the Single European Act, states that the EC will in its consumer protection measures take as a base a high level of protection, in order to ensure consumer confidence in the functioning of the internal market.³³¹

Institutions

Following the 1972 summit, the EC Commission formed a service for consumer protection that was later incorporated into a directorate-general.³³² The

EC Commission then set up a Consumers' Consultative Committee in which the EC's various consumer associations could cooperate among themselves and with the EC institutions.³³³ The committee's 33 members were to consist of 9 experts as well as 6 representatives each from the big consumer organizations: BEUC (European Bureau of Consumers' Unions), COFACE (Committee of Family Organizations in the European Communities), EUROCOOP (European Community of Consumer Cooperatives, and ETUC (the European Trade Union Confederation). At times, the committee has disagreed strongly with the EC Commission, such as in its opposition to transnational television advertising of over-the-counter drugs. The committee argued that television is not an adequate medium to advertise complex pharmaceutical products. The EC Commission has supported such advertising as increasing consumer awareness. The committee has issued more than 130 opinions to the EC Commission on such subjects as hormones, mortgages, and package tours.³³⁴ Moreover, since 1983 the EC Council of Ministers has held regular meetings of national ministers responsible for consumer affairs.

On December 17, 1989, the EC Commission issued a decision setting up a Consumers' Consultative Council in the place of the existing Consumers' Consultative Committee.³³⁵ The decision declared that "the constant improvement of the living and working conditions as well as the harmonious development of the economies constitute objectives" of the EC and that the development and enlargement of the EC³³⁶ necessitated a redefinition of the old committee. The new council is to advise the EC Commission and comprise representatives of European consumer organizations as well as national organizations, institutions and individuals "specially qualified in consumer affairs."³³⁷ The EC

³²⁸ EC Commission, European file, "The European Community and Consumers," June-July 1987, pp. 3-4.

³²⁹ *Ibid.*, pp. 10-11. The BEUC has been pressing for increased consumer representation in the standardsmaking process because of the perceived strength of industry representation, which is important because the EC's new approach to technical harmonization puts increasing emphasis on private standardsmaking bodies in the development of EC technical rules. *Europe*, No. 5198 (Feb. 21, 1990), (New Series), p. 14. French, German, and British delegates to the OECD have also expressed dissatisfaction with the level of consumer input into EC standardsmaking. U.S. Department of State Telegram, Apr. 27, 1989, "OECD: OECD Committee on Consumer Policy Meeting, April 17-21, 1989," Paris.

³³⁰ EC Council Resolution of December 15, 1986, *OJ* No. C 3, Jan. 7, 1987, p. 1; Council Resolution of November 9, 1989, *OJ* No. C 294, Nov. 22, 1989, p. 1.

³³¹ EC Council, 1361st Council Meeting, on consumer affairs, Nov. 9, 1989, Press Release 9586/89 (Presse 195), p. 7.

³³² DG XI is the Directorate-General for Environment, Consumer Protection, and Nuclear Safety, and is headed by Laurens Brinkhorst. Within DG XI is a Consumer Policy Service. Karel Van Miert is the Commissioner primarily responsible for consumer affairs. *Europe*, No. 5198 (Feb. 21, 1990), (New Series), p. 14.

³³³ Decision 73/306/EEC, *OJ* No. L 283, Oct. 10, 1973, p. 18, as amended by Decision 80/1087/EEC, *OJ* No. L 320, Nov. 27, 1980, p. 33. EC Commission, *European File "The European Community and Consumers,"* June-July 1987, p. 4; *Europe*, No. 5205 (Mar. 2, 1990), (New Series), p. 14.

³³⁴ European Parliament, Directorate-General for Research, *Fact Sheets on the European Parliament and the Activities of the European Community*, PE 122.000, En III/0/4.

³³⁵ EC Commission Decision 90/55/EEC of Dec. 17, 1989, *OJ* No. L 38/40, Feb. 10, 1990.

³³⁶ In particular, the EC Commission considered that the old committee did not adequately meet the needs of the new Mediterranean EC members, i.e., Greece, Spain, and Portugal. *European Report*, No. 1551 (Dec. 22, 1989), Internal Market, p. 3.

³³⁷ *Ibid.* The council has 39 unpaid members serving 3-year terms. Each European body sends four full and four alternate representatives. The national organizations and institutions of a general nature of each member state are represented by 17 members, 1 member for smaller member states and 2 members for larger ones. Experts account for the remaining six seats. Consumer organizations must meet certain criteria regarding representativeness, independence from business circles, and the relevance of their work in terms of public interest and/or the number of members. *Ibid.*, art. 3, p. 41, and annex I, p. 43.

Commission, although it is not required to, may consult the consultative council on consumer policy matters. EC Commission staff convene the council meetings, which occur at least twice a year, and participate in its deliberations.³³⁸

At the first meeting of the Consumers' Consultative Council on April 23-24, 1990, EC Commissioner Van Miert presented a new 3-year action plan for consumer protection, to include improvements in procedures, information, safety, and consumers' transactions. In particular, the plan would encourage the formation of consumer organizations in member states where such groups do not exist, step up consumer education in schools, protect the right of consumers to buy in member states other than their own, and regulate contracts to eliminate unfair clauses.³³⁹ He stated that member-state implementation of consumer directives was not as diligent as it could be and noted that Italy and Belgium were particularly remiss, unlike the United Kingdom.³⁴⁰

Consumer Protection Measures

The term "consumer protection" encompasses several areas of concern, including the protection of health and safety, the protection of economic interests, and education. The protection of consumer health and safety is an important part of consumer protection, but that aspect merges into the EC's general effort to promote health and safety and is therefore discussed more fully in the section of this chapter on health and safety regulations. Another aspect of consumer protection, and one distinct from EC efforts in other fields, is the protection of consumers' economic interests against dishonest or improper dealing. Disparity among member-state laws on protection of economic interests can in the EC's view lead to barriers to trade. The EC seeks to prevent consumers from being penalized by not being able to shop among member states for the best deals. Thus the EC's purview includes the conditions under which consumers obtain credit, services such as holiday tours, and products free of defects.³⁴¹ Practices to be targeted include defective products and guarantees, improper advertising, unfair credit terms, aggressive sales methods, and inadequate after-sales service and repairs.³⁴²

³³⁷ — Continued

The Brussels-based European body COFACE criticized the arrangement, particularly the practice of basing the number of national representatives on country size and having the council meet two rather than four times a year. *European Report*, No. 1548 (Dec. 13, 1989), *Internal Market*, p. 4.

³³⁸ *Ibid.*, arts. 8-9, p. 41.

³³⁹ *European Report*, No. 1576 (Mar. 31, 1990), *Internal Market*, p. 1.

³⁴⁰ *European Report*, No. 1582 (Apr. 28, 1990), *Internal Market*, p. 9.

³⁴¹ EC Commission, *European File*, "The European Community and Consumers," June-July 1987, p. 7.

³⁴² European Parliament, Directorate-General for Research, *Fact Sheets on the European Parliament and the Activities of the European Community*, En III/0/4.

The EC also includes education and information as part of consumer protection. The Council of Education Ministers undertook in 1986 to include consumer problems as part of the curriculum of EC schools.³⁴³ The EC considers that consumers should be given the information needed to make educated purchasing decisions. Indicative of this, the EC is passing measures regulating the labeling of foodstuffs³⁴⁴ and certain dangerous products to warn of possible hazard it has also proposed measures that require the marking of energy consumption data on consumer electrical equipment and the inclusion of unit pricing in product labeling. Another effort is EHLASS (European Home and Leisure Accident Surveillance System), which gathers and disseminates information about accidents involving consumer products.³⁴⁵ The EC Commission intends to issue information about price differences among the member states³⁴⁶ and about the rights of consumers when purchasing a product in another member state.³⁴⁷

In the future, the EC also plans to regulate the functioning of after-sales services, to ensure that guarantees are honored in the consumer's country of residence, wherever the product may have been bought. The quality and efficiency of public services and their concern for consumers' interests is under review. The EC also seeks to establish faster and cheaper procedures for consumers to obtain advice and redress in minor litigation, particularly through extrajudicial dispute settlement; the EC Commission has already begun supporting pilot projects in this area.³⁴⁸ The EC will seek a more equitable structuring of air fares. Another EC Commission aim is to penalize airlines for overbooking.³⁴⁹

³⁴³ See also recommendation for increased consumer education in European Parliament Opinion, OJ No. C 120, May 20, 1986.

³⁴⁴ See discussion of recent labeling proposals in the section on processed food below.

³⁴⁵ NO TAGEC Council, Press Release 9586/89, p. 12.

³⁴⁶ The BEUC recently provided an example of why such price comparison information can be useful. A BEUC study found that price differences between member states for identical car models have increased, suggesting that certain consumers can gain from buying in other member states. However, the BEUC also cited obstacles to such comparison shopping, such as dealers' refusals to sell to foreigners, difficulties with guarantees, and clumsy customs formalities. *Europe*, No. 5165 (Jan. 5, 1990), (New Series), p. 14.

³⁴⁷ EC Commission, *European File* "The European Community and Consumers," June-July 1987, p. 10.

³⁴⁸ *Ibid.*, p. 9. EC Council, Press Release 9586/89, p. 12.

³⁴⁹ *Europe* 92, vol. I, issue 4. The proposal would impose fines of 25 percent of the fare for delays up to 4 hours, and 50 to 100 percent for longer periods, as well as set up a special task force to carry out the new rules. EC airlines' fares are also under review, for possible predatory pricing. The EC Commission is seeking additional authority to combat predatory practices involving the misuse of travel agent incentives and frequent flyer programs. *European Report*, No. 1582 (Apr. 28, 1990), *Business Brief*, p. 3; *Financial Times*, May 3, 1990, p. 1.

Setting aside health and safety measures that merge into the EC's general health and safety program, the EC's consumer protection policy has directly resulted in the proposal of only a small number of 1992 directives. Those directives mainly aim at protecting economic interests: the misleading advertising directive;³⁵⁰ the package holiday directive;³⁵¹ the consumer credit directive and the directive on calculation of the annual percentage rate of charge for credit;³⁵² the directive on contracts negotiated away from business premises (i.e., door-to-door sales);³⁵³ and the directive on dangerous imitation products.³⁵⁴ The directive on indication of prices of foodstuffs³⁵⁵ and on indication of prices of nonfood products³⁵⁶ are also relevant to consumer protection.

Although only a few directives are based primarily on the need for consumer protection, there are a number of other 1992 measures that involve consumer protection even though they mainly address other concerns, such as safety and health. The directive on toy safety is an example of this kind of measure.³⁵⁷ The directives on classification, packaging and labeling of dangerous preparations,³⁵⁸ and on the labeling of tobacco³⁵⁹ also typify the sort of measure aimed at the protection of consumers' health and safety via the provision of adequate information at the consumer

level. Similarly, three measures that are interrelated are the directive on general product safety,³⁶⁰ the decision on a rapid information-exchange system on dangers arising from use of consumer products,³⁶¹ and the directive on liability for defective products.³⁶² Although the product liability directive deals with both consumer protection and safety regulation, it is more fully discussed in a separate section on product liability below.

EC measures in areas other than safety and health can also have consumer protection aspects. In the insurance field, for example, both the directive on life insurance and the second directive on nonlife insurance express the need to balance the benefits of according more freedom to insurance providers with the need to protect consumers against unfair practices.³⁶³

The EC's directive on broadcasting activities³⁶⁴ arguably can be included under the rubric of consumer protection, because it seeks to protect consumers from improper advertising, but it also contains other provisions, some of which are more in the public eye.³⁶⁵

Public Health and Safety Regulation

Description of EC Health and Safety Policy

The EC's public health and safety policy is one that is still in the early stages of development and, thus, is still evolving. This area is a broad one, encompassing matters ranging from cancer concerns to plant health. Its breadth spans other issues that are the subject of the 1985 White Paper, such as labor, consumer protection, and the environment. This section addresses primarily issues that do not fall within these other areas because they are covered by other sections of this report.

The EC aims to eliminate to the fullest extent possible technical barriers preventing the free

³⁵⁰ Council Directive 84/450, OJ No. L 250, p. 84. Passed before white paper, but important consumer measure, and listed as 1992 measure in *Count-Down 1992*.

³⁵¹ Council Directive 90/314. The directive covers private and business travel, provides for adequate disclosure of terms and prices in brochures, as well as for compensation when holidays go wrong, and regulates the liability of tour operators. USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 6 118; *European Report* (Feb. 23, 1990), No. 1566, internal Market, p. 9. The BEUC has opined that the present version of the measure is inadequate to protect the interests of consumers. Because art. 100A of the Treaty of Rome requires that measures aim at a high level of protection, the BEUC warns that the EC Council might be sued if the current draft is adopted. *Europe*, No. 5198 (Feb. 21, 1990), (New Series), p. 14.

³⁵² Council Directive 87/102, OJ No. L 42/87; Council Directive 90/88, at p. 14, OJ No. L 61/90. The directives harmonize member-state rules on credit information, advertising, the content of credit agreements, and the relationship between creditor and debtor. EC Commissioner Van Miert opined that these measures will permit consumers to compare credit offers and to know the terms under which they sign. *European Report*, No. 1566, (Feb. 24, 1990), Economic and Monetary Affairs, p. 1.

Because there are indications that member states are not following EC Commission Recommendation 88/590 concerning the relationship between the issuer of a payment card and the cardholder, the EC Commission is also considering the issuance of a directive in place of the nonbinding recommendation. *Common Market Reporter* (CCH), May 24, 1990, p. 3.

³⁵³ Council Directive 85/577 OJ No. L 372/85. The directive seeks to protect the consumer in transactions with door-to-door salesmen, in particular by giving the consumer the right, disclosed by the salesman in writing, to cancel the contract within a period of at least 7 days.

³⁵⁴ Council Directive 87/357, OJ No. L 192/87.

³⁵⁵ Council Directive 88/315, OJ No. L 142/88.

³⁵⁶ Council Directive 88/314, OJ No. L 142/88.

³⁵⁷ Council Directive 88/378.

³⁵⁸ Council Directive 88/379, OJ No. L 187/88.

³⁵⁹ Council Directive 89/622, OJ No. L 359/89.

³⁶⁰ OJ No. C 193/89. In April 1990, EC Commissioner Van Miert opined that the Council's work on the directive had not advanced far enough and that the directive should be extended to include banking and insurance-related services. *European Report*, (Apr. 28, 1990), No. 1582, Internal Market, p. 9.

³⁶¹ Council Decision 89/45, OJ No. L 17/89.

³⁶² Council Directive 85/374 of July 25, 1985, OJ No. L 210/85.

³⁶³ Council Directive 88/357/EEC, and proposal Com(90) 46 final, OJ No. C 72 (Mar. 22, 1990), as described in EC databank Info 92, May 29, 1990.

³⁶⁴ Council Directive 89/552, OJ No. L 298/89. See discussion in USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, p. 6-22; USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 6-112.

³⁶⁵ Its most well known aspect is the attempt, in the name of protecting European culture, to legislate minimum EC content levels for EC broadcasts. That provision might appear designed to protect EC film producers rather than consumers. U.S. producers were particularly alarmed by the directive's initial form, which proposed binding quotas on the amount of permitted non EC programming. "But, U.S. industry continues to express concern that the EC broadcasting rules are discriminatory. See, e.g., testimony before U.S. International Trade Commission, June 20, 1990.

movement of goods among its member states, while recognizing national differences in producing the goods that may affect their safe use in other member states. However, what is considered to be a health or safety problem in one country is not necessarily considered to be a health and safety problem in another. This is particularly true in the animal and plant health area. To some extent, then, a dual system of trade may be sanctioned, whereby certain goods from certain countries may be scrutinized more closely than the same goods from other countries, on the grounds that such measures are justified because of the need to protect the public health and safety.

Fundamentally, the degree to which health and safety are to be protected is set forth in article 100A of the Treaty of Rome, which was adopted as part of the Single European Act. It requires the EC Commission "to take as a base a high level of protection" when proffering proposals in these areas, among others. In addition, a number of proposals may be based on article 43, which pertains to agriculture.³⁶⁶

The most important issues in the public health and safety arena pertain to foodstuffs and pharmaceuticals.³⁶⁷ The EC's free trade in foodstuffs program aims to set general food safety and hygiene standards and establish a more informative system of labeling. The Framework directives cover food labeling,³⁶⁸ food additives, foods for particular nutritional uses, materials and articles in contact with foods, and the official control of foodstuffs.

Several EC policies relate to anticancer efforts. One is the "Europe Against Cancer" program, which is now in its second phase.³⁶⁹ Another facet of the anticancer movement is the campaign against tobacco advertising.³⁷⁰ The third involves limitations on radon in new and existing buildings.³⁷¹

³⁶⁶ Art. 43 provides for, in part, making regulations, issuing directives, and making decisions with respect to a Common Agricultural Policy.

³⁶⁷ Europe has had a number of problems regarding the safety of foodstuffs over the years. These problems include instances of salmonella poisoning of eggs, listeria in cheese, poisoning of wine, and, most recently, bovine spongiform encephalopathy, known as BSE or "mad cow disease," in beef.

³⁶⁸ See below for a discussion of the nutritional-labeling directive.

³⁶⁹ The first program was adopted in 1988 and also set forth a program for 1989. See *OJ* No. C 50 (Feb. 26, 1987) and *OJ* No. L 160 (June 28, 1988). See *OJ* No. C 164 (June 1989) for details of the second program. It will extend from 1990 to 1994 and comprises three parts. The first emphasizes preventive measures, the second part of the plan involves health education and information, and the third concerns the support of national or regional programs to promote training for health care personnel. "Measures to Combat Smoking, Cancer and AIDS," *European Report*, No. 1587 (May 16, 1990), sec. 4, p. 8.

³⁷⁰ See below for a discussion of the ban on tobacco advertising.

³⁷¹ A recommendation was adopted by the EC Commission on Feb. 21, 1990. It is believed that the recommendation, which is nonbinding, is likely to be ignored by member states.

Close behind concerns with foodstuffs and human health are concerns with animal and plant health, although the former is accorded more importance than the latter because the health of animals more directly influences that of the consumer. The EC may have set its policy regarding the use of hormones given to animals on March 15, 1990, when the European Parliament amended the EC Commission's proposals to suspend the approval process for bovine somatotropin (BST) until the end of 1990.³⁷²

Another policy that arises out of the debate is the method of evaluating these substances. It has been accepted that the safety, quality and efficacy of a product are valid concerns.³⁷³ A fourth criterion (also termed the "fourth hurdle") is socioeconomic impact and concerns an evaluation of whether a new product or process is needed and whether it will decrease employment. The EC Commission is expected to issue a report on the matter the fall of 1990.³⁷⁴

³⁷¹ - Continued

However, to combat radon some member states have already introduced legislative measures that contain much stricter requirements than those imposed in the recommendation. "Commission Adopts Recommendation on Radon in Buildings," *European Report*, No. 1566 (Feb. 24, 1990), sec. 4, p. 9; "Commission to Discuss Radon Recommendation on February 21," *European Report*, No. 1564 (Feb. 17, 1990), sec. 4, p. 6.

³⁷² At least one businessman in Europe believes that the BST trial period will be extended or that there will be some other means of prolonging the time before a decision to approve or disapprove the hormone is made. Representative of U.S. company located in Belgium, interview by USITC staff, Brussels, June 7, 1990. Another believes that the BST issue will be carried into 1991, without registration of the hormone by the end of this year. The report evaluating BST, due by Oct. 1, 1990, is being closely guarded, so the anticipated outcome is unknown. See below for an updated discussion of the moratorium on BST.

³⁷³ See, e.g., "EEC Vets Federation Rejects Fourth Criterion for Growth Promoter Approval," *European Report*, No. 1578 (Apr. 7, 1990), sec. 3, p. 7; Michel Philippe, "The Fourth Hurdle: A Bridge Too Far?," *Health Horizons*, No. 10, (May 1990), p. 24.

³⁷⁴ The European Parliament recently called for the use of this criterion when considering the marketing of new, growth-enhancing substances, such as BST. There is much concern among industry representatives that use of the fourth criterion will extend beyond growth promoting hormones. Representative of U.S. company located in the United Kingdom, interview by USITC staff, Basingstoke, June 4, 1990. There may already be an attempt under way to expand the criterion to the authorization to market additives such as the antibiotic Avoparcin in animal feed because it promotes animal weight gain and boosts milk yields. The EC Commission has authorized national use of this drug until Nov. 30, 1990, pending an EC wide marketing authorization, and it may be covered in the EC Commission's report. "New Marketing Authorisation for Avoparcin in Animal Feed," *European Report*, No. 1580 (Apr. 21, 1990), sec. 4, p. 3; "Council Experts Continue Work on Medicated Feed Directive; New Compound Feed Marketing Standards Adopted," *European Report*, No. 1564 (Feb. 17, 1990), sec. 4, p. 4.

At least one industry representative believes that evaluating the socioeconomic impact of products after they have been authorized for sale may be useful. This would permit measurement of the impact of the products on income, employment, and the like. Philippe, "The Fourth Hurdle," p. 24; Industry representative located in Belgium, interview with USITC staff, June 7, 1990.

Institutional Framework

Several institutions to regulate public health and safety have been proposed, but none has yet been established. One of the principal tools of regulation in this area is the anticipated European Medicines Agency. It is expected to be modeled to some degree after the U.S. Food and Drug Administration.³⁷⁵ It is expected that the agency will utilize both centralized and decentralized procedures for approving new pharmaceuticals. Some details concerning the agency, however, are still unclear.³⁷⁶ The proposal was to be presented in July of 1990, and the European Commission's ideas are expected to be published formally in 1991 and take effect in 1993.³⁷⁷

The EC Commission is also proposing a new agency, separate from the medicines agency, to centralize approval for new products based on novel chemicals. In the event of disputes, the medicines agency would arbitrate.³⁷⁸ The medicines agency would augment the work of the committee in Brussels that now makes recommendations as to the approval of new drugs in the form of advisory opinions, but the opinions would then become binding.³⁷⁹ There is a separate call by the European Parliament's Committee on the Environment, Public Health and Consumer Protection for establishing a centralized system to oversee the production and marketing of new veterinary medicines as soon as possible.³⁸⁰

In the area of processed foods the foodstuffs division of the EC Commission is establishing a documentary system to receive petitions for consideration and scientific and technical information pertaining to food additives, materials in contact with foods, foods for particular nutritional uses, flavorings, solvents, and other

³⁷⁶ It appears at the present that its scope would be similar, but it is likely that its powers will differ. The sentiment in Europe appears to be that no one desires an agency that would burden applicants with too many requirements that may retard or impede the free flow of trade, although there is interest in enhancing protection to consumers. One industry representative stated that he would have no objection to the agency if it is kept to a reasonable size, if state-named experts are used, and if it issues binding decisions within a reasonable time. Representative of U.S. company located in Belgium, interview with USITC staff, Brussels, June 7, 1990.

³⁷⁸ One problem already foreseen will be the power of the agency to verify information given to it by the member states. European Parliament staff member, interview by USITC staff, Brussels, June 6, 1990.

³⁷⁷ Ibid.; Peter Marsh, "EC Drugs Agency Plan Attacked As Potential Disaster," *Financial Times*, June 21, 1990. However, at least one industry representative thinks it may be as long as 10 years before the agency is functional. Representative of U.S. company located in Belgium, interview by USITC staff, Brussels, June 7, 1990. It is interesting to note that some other industry representatives believe that the agency would receive more respect from consumers than national bodies currently enjoy. Representatives of U.S. companies located in the United Kingdom, interview by USITC staff, Basingstoke, June 4, 1990.

³⁷⁹ Marsh, "EC Drugs Agency Plan Attacked."
³⁷⁸ Representative of U.S. company located in Belgium, interview by USITC staff, Brussels, June 7, 1990; Marsh, "EC Drugs Agency Plan Attacked."

³⁸⁰ "Council Awaits European Parliament's First Reading," *European Report*, No. 1567 (Feb. 28, 1990), sec. 4, p. 10.

matters. The petitions would be examined to determine whether they conform with EC rules.³⁸¹

Three years ago the EC Commission proffered proposals to deal with the many differing national standards and trade restrictions relative to plant health, and included was an EC plant health inspectorate. The single market will require that controls be adopted at the Community level, and the idea is to have a "plant passport," which entails evidence of compliance with EC rules and which would replace plant health certificates to aid in free movement across the borders within the EC.³⁸²

In the public procurement sphere, the Irish EC Council presidency³⁸³ sought to establish an independent inspection force to ensure that basic standards are implemented in nuclear installations throughout the EC.³⁸⁴ The Parliament adopted a resolution on safety procedures at nuclear power plants on March 15, 1990.³⁸⁵ Such plants will likely be covered by the EC's directive on procurement in the "excluded sectors."

EC Measures and Court Rulings

As explained in the first USITC followup report on the EC 92 program, some U.S. producers and U.S. regulatory agencies are very interested in the EC's agricultural policies. Of prime interest is the ongoing debate involving hormone such as BST, which is used to stimulate milk production.³⁸⁶

The EC has already banned the sale of meats from hormone-treated animals, an action challenged by the United States as not based on scientific grounds. The European Animal Health Federation (FEDESA) initiated a case in the United Kingdom, which is now before the Court of Justice, challenging the hormones directive. The Court's final ruling is expected before it recesses for the summer on July 15.³⁸⁷

³⁸¹ "Call for Proposals for Documentation System," *European Report*, No. 1563 (Feb. 14, 1990), sec. 4, p. 6; *Operation of a Documentary System: Invitation to Tender, Of No. C 28* (Feb. 7, 1990).

³⁸² "New Measures Proposed to Prepare for Post-1992 Single Market," *European Report*, No. 1563 (Feb. 14, 1990), sec. 4, p. 1. There are also plans for an official control system at the marketing stage and for registration of plant-protection products. Ibid.; "Debate on EEC-Wide Plant Health Product Register Widens," *European Report*, No. 1577 (Apr. 4, 1990), sec. 4, p. 11. See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-67 to 6-68, for more information on registration of plant-protection products.

³⁸³ The presidency of the Council of Ministers lasts for 6 months and is rotated among the member states. Ireland held the post from January to June 1990.

³⁸⁴ "Green' Presidency Well Received at European Parliament," *European Report*, No. 1566 (Feb. 24, 1990), sec. 4, p. 4.

³⁸⁵ "European Parliament Adopts a Resolution Calling for a Review of Procedures at Nuclear Plants," *European Report*, No. 1572 (Mar. 17, 1990), sec. 4, p. 10.

³⁸⁶ See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-48 to 6-51, for background information on BST and other hormones.

³⁸⁷ The Court annulled the directive for procedural reasons and it was again adopted, in identical form. It was challenged yet again and subsequently upheld by one of the Court's advocates-general in March 1990. The advocate-general stated, among other reasons, that the Council could impose a

Hormones fall generally under the rubric of biotechnology, and the EC has recently adopted a directive that deals with another facet of this science—genetic engineering, specifically genetically modified organisms (GMOs), which are organisms in which genetic material has been altered in a manner that does not occur naturally by mating or natural recombination. One directive pertains to the contained use of GMOs,²⁸⁸ i.e., their use in laboratory experiments. Besides seeking to protect human health, the directive aims to provide common rules throughout the EC for the use and release of GMOs and to protect the environment.²⁸⁹

In addition to these measures, another regarding the protection of workers from exposure to biological agents is being discussed. A common position has been reached, and the measure may be completed by the end of 1990.²⁹⁰

With respect to veterinary controls on intra-EC trade of live animals, 2 years ago the EC Commission submitted a draft directive.²⁹¹ It specifies for the point of origin a wide range of controls that must be respected before importation is allowed as well as random checks at the point of destination. The EC Parliament's Agriculture Committee has proposed an amendment to allow on-the-spot inspections for diseases without prior notification only if there are reasonable grounds to believe the member state's actions are inadequate. The committee has also proposed that a contingency plan be drafted at the EC level to develop criteria that would measure the adequacy of steps taken by member states in the event of an outbreak of a serious animal disease. The Council of Ministers' veterinary experts recently issued a draft decision on the EC's

contribution to the much greater veterinary expenditure that the post-1992 regime will engender, due to stricter controls on the point of origin (farms and abattoirs).³⁹² The decision provides for the designation of EC liaison and reference laboratories, performance of technical and scientific tasks, and establishment of an animal health data base, all at the expense of the Community. Several member states also wish to link this measure to the new directive phasing out vaccination against foot and mouth disease and the draft directive abolishing border checks on live animals after 1992.³⁹³ The directive on foot and mouth disease would abandon vaccination and require compulsory slaughter and destruction after January 1991.³⁹⁴ With respect to veterinary medicines, the EC Commission recently amended the package of these proposals.³⁹⁵

Currently under discussion is a controversial proposal, the general product safety directive.³⁹⁶ Some member states wish to narrow the scope, exempting certain products such as foodstuffs or those used exclusively for professional purposes. The Parliament has voted for upgrading the draft directive to a regulation and for the measures to apply from January 1, 1991.³⁹⁷

In the chemical area, there is a proposed directive currently before the Parliament respecting a Communitywide register of approved pesticide and plant-protection products.³⁹⁸

²⁸⁷ —Continued

total ban on hormones if this were the only means to eliminate all risks to public health, even if hypothetical. "Internal Conflicts Heat Up While the Legality of Community Ban Is Put to the Test," *European Report*, No. 1596 (June 20, 1990), sec. 4, pp. 9-10; "EEC Court Advocate General Upholds Validity of EEC Hormone Ban," *European Report*, No. 1570 (Mar. 10, 1990), sec. 4, p. 14.

²⁸⁸ Council Directive of 23 April 1990 on the Contained Use of Genetically Modified Micro Organisms, 90/219, OJ No. L 117 (May 8, 1990). Another GMO directive relates to their deliberate release into the environment. Council Directive of 23 April 1990 on the Deliberate Release Into the Environment of Genetically Modified Organisms, 90/220, OJ No. L 117 (May 8, 1990).

²⁸⁹ It covers activities using live, genetically modified micro-organisms, such as viruses, bacteria, fungi, and cell cultures. Before the directives were adopted, some member states had extremely severe regulation of GMO activities and others had almost none. The member states were unanimous in deciding that there should be regulation in this area, however. Those countries with no laws were not developing GMOs and did not want to be a dumping ground for the others. Industry in those countries that were developing GMOs did not want competitors in other countries operating under rules different from those under which they had to operate. EC Commission staff member, interview with USITC staff, Brussels, June 6, 1990.

²⁹⁰ *Ibid.*

²⁹¹ "More Hitches for Plan to Abolish Border Checks," *European Report*, No. 1595 (June 16, 1990), sec. 4, p. 1; "Euro-MPs to Debate Border Checks on Live Animals For-Post [sic] 1992 Era," *European Report*, No. 1587 (May 16, 1990), sec. 4, p. 5.

³⁹² "Edging Towards a Compromise on EEC Contribution to Expenditure Under Post 1992 Strategy," *European Report*, No. 1588 (May 19, 1990), sec. 4, p. 4.

³⁹³ *Ibid.*, pp. 4, 5.

³⁹⁴ "Impact of German Unification on CAP," *European Report*, No. 1589 (May 24, 1990), sec. 4, p. 14.

³⁹⁵ The European Commission took into account Parliament's opinion of Mar. 15, 1990, but only as regards cosmetic changes and not dealing with growth-promoting hormones or the European Medicines Agency, which were issues raised by the Parliament. It appears that the EC Commission wishes to include the hormones in its report due by October 1990. "EEC Commission Amends Proposals for Harmonising Legislation," *European Report*, No. 1585 (May 9, 1990), sec. 4, pp. 7-8. The Parliament had asked for a definition of veterinary medicines to distinguish between growth-promoters and drugs used to treat animal diseases and other problems (e.g., infertility). *Ibid.*

³⁹⁶ See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-121 to 6-124, for the specifics of this proposed directive.

³⁹⁷ "Euro MPs Call for Regulation to Replace Draft Directive," *European Report*, No. 1573 (Mar. 21, 1990), sec. 4, p. 5; "Member States Debate General Product Safety Proposal," *European Report*, No. 1565 (Feb. 21, 1990), sec. 4, p. 5. For more information on the general product safety directive, see discussion below on product liability.

³⁹⁸ There is concern as to whether the proposal adequately protects consumers, users, or the environment. "European Parliament Sends Report on EEC Register Back to Committee," *European Report*, No. 1595 (June 16, 1990), sec. 4, p. 8. See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-67 to 6-68, for more information on the proposed directive.

Implementation in Member States

Although the EC appears, generally, to be willing to act to set policies in the area of public health and safety, especially in the event of a crisis, the member states do not hesitate to set their own policies when health matters are involved. For instance, a number of member states chose not to follow the EC's policy pertaining to BSE, an action that sparked a major dispute among the member states.³⁹⁹ In another instance, implementation of the toy directive⁴⁰⁰ has been quite slow, and one member state is reportedly requiring more formalities than ever before allowing importation of these products.⁴⁰¹

The handling of this situation may establish a precedent for the way in the which the EC Commission and the member states approach other, similar matters. Some EC countries may continue to disregard the fact that other member states have found a particular product to meet prescribed health and safety requirements. Officials are, in fact, concerned that such crises may become more common as the EC removes border controls under the 1992 program, for member states may use these opportunities to exploit health and safety concerns in order to protect their home markets.⁴⁰²

Product and Other Liability

Policy

One of the more significant aspects of the 1992 integration program has been the EC's revision of

³⁹⁹ While West Germany, France, and Italy imposed an outright ban on the import of British beef, Belgium simply advised its citizens not to eat British beef until the results of an inquiry as to the safety of the beef were known. The EC Commission warned that, unless the bans were lifted by a specified time, legal action would be instituted. No legal action could proceed against Belgium because it had not imposed a formal ban. The United Kingdom was reportedly considering retaliation measures, should the EC's actions have proven to be inadequate. Tom Walker, "Trade Repercussions of the 'Mad Cow' Row," *Wall Street Journal Europe*, June 11, 1990, p. 10. Richard Palmer, "Government Hints at Retaliation Over Europe's Beef Bans," *Sunday Times of London*, June 3, 1990, p. 2; "EC Sets 'Beef War' Deadline," *Times of London*, June 2, 1990, pp. 1, 16.

The situation was defused by an emergency meeting of the agriculture ministers in Brussels when they agreed to impose a certification system on exported British beef and also asked the EC Commission to organize an EC wide research program on BSE. Martin du Bois, "EC Ministers Set Rules to Contain Mad Cow Disease," *Wall Street Journal Europe*, June 8-9, 1990, p. 2; "EC Strikes Beef Deal, Export Bans Are Lifted," *International Herald Tribune*, June 8, 1990, p. 11.

⁴⁰⁰ See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-115 to 6-118, for more information on this measure.

⁴⁰¹ Only six member states have implemented the directive. It is alleged that France is stopping every shipment of toys to ensure compliance with the directive, although "sporadic checking" of shipments is specified. "Toy Directive Problems Under Commission Scrutiny," 1992 - *The External Impact of European Unification*, vol. 2, No. 8 (July 13, 1990), pp. 3-4.

⁴⁰² Walker, "Trade Repercussions;" du Bois, "EC Ministers Set Rules."

its laws on the liability and responsibility of producers and others for defects and damages. In 1985, the EC issued the first measure in this effort: Directive 85/374 on liability for defective products.⁴⁰³ In the recitals prefacing that directive, the EC found that differences among member-state liability laws distort trade and hamper the free movement of goods and the formation of a common market for consumers.⁴⁰⁴ In 1988, the EC issued a related decision on a rapid information-exchange system on dangers arising from the use of consumer products.⁴⁰⁵ In 1989, the EC Commission proposed a directive, complementary to the liability directive, on general product safety.⁴⁰⁶ The EC Commission has also proposed a directive establishing rules on liability of polluters for waste, and plans a directive on liability for defective services.

This range of measures demonstrates that the EC's policy of strengthening liability rules contains aspects of consumer protection, in that consumers can recover losses incurred because of defects in products; health and safety regulation, because the threat of liability is meant to increase the safety of products; and environmental regulation, because being held accountable may deter firms from polluting the environment.

Some industry sources express concern that the growing influence of "Green" (environmental) political groups and an expanding consumer movement are pushing liability measures through the EC legislative process without proper concern for the views of agricultural, manufacturing, insurance, and other industries. Although EC measures have not been of great concern so far, industry sources believe that the rise of consumerism within the EC may lead to pressure for more drastic measures in the future.

Product Liability

The product liability directive⁴⁰⁷ is the most visible aspect of the EC's liability-reform policy. The directive aims at harmonizing EC member-state laws, many of which had failed to provide consumers with effective legal recourse against producers of defective products. Many member states had denied redress to an aggrieved consumer unless the customer could succeed in the often difficult task of proving that the producer had been negligent. In contrast, the EC directive instituted a form of strict liability, under which a producer or

⁴⁰³ Council Directive 85/374, OJ No. L 210/85. This measure was discussed in the initial report. USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, pp. 6-37 to 6-38.

The measure and the related proposed directive on general product safety were also discussed in the first followup report. USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-120 to 6-124.

⁴⁰⁴ Utz Toepke, address to American Bar Association (ABA) EC conference, "Europe 1992," June 8, 1990.

⁴⁰⁵ Council Decision 89/45 of Dec. 21, 1988, OJ No. L 17/89.

⁴⁰⁶ OJ No. C 193/89.

⁴⁰⁷ Council Directive 85/374. See discussion in USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, p. 6-37; USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 6-120.

other person responsible for a defect in a product can be held liable if the consumer proves merely that the product was defective and that the defect had caused damage. The producer remains liable for 10 years after its product is put into circulation, although the consumer must sue within 3 years of the date on which he or she became aware or should have known of the defect and the identity of the producer.⁴⁰⁸ The consumer can also bring suit against the importer of a defective product, and, if the producer cannot be identified, against the supplier of the product.⁴⁰⁹

As the EC increases the scope of its liability laws, the U.S. Congress, with the President's support, is moving toward reform of U.S. product-liability laws to limit liability, in view of the heavy burden such laws have placed on U.S. business, notably resulting in insurance costs that average 20 times those in Europe.⁴¹⁰ In contrast to the increased uniformity that the EC is establishing with its directive, U.S. product-liability laws are still fragmented among the States. The United States is attempting to reform its product-liability laws to make them clearer and more predictable, in order to improve the competitiveness of U.S. firms. Although the EC is instituting strict liability, the EC liability standard arguably will remain more limited than the U.S. standard even if Congress passes the proposed reform measures it is currently considering.⁴¹¹

Implementation Problems

The product liability directive had an implementation deadline of July 30, 1988. On December 22, 1988, the EC Commission announced that it would open infringement proceedings against nine of the EC's member states because they had failed to implement the directive, as well as against the United Kingdom and Italy because the legislation they passed did not conform to the directive. At that time, only Greece⁴¹² was considered to have properly transposed the directive into national law.⁴¹³

⁴⁰⁸ Council Directive 85/374, art. 10. Although consumer protection is the most frequently cited goal of the directive, the time-limit provision actually benefits producers more, because many countries' preexisting laws contained significantly longer time limits, such as 30 years. Utz Toepke address.

⁴⁰⁹ The consumer's chance of success is increased under the Brussels Convention, which provides EC plaintiffs with a choice of jurisdictions in which to sue. Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters, signed at Brussels Sept. 27, 1968.

⁴¹⁰ Washington Post, May 23, 1990, p. C 1; EC-US Business Report, May 1, 1990, p. 21.

⁴¹¹ Wendell Wilkie II, General Counsel, U.S. Department of Commerce, address to ABA-EC conference, "Europe 1992," June 7, 1990.

⁴¹² Law effective July 30, 1988, but applying to products put into circulation after publication in the Greek Official Gazette of Apr. 22, 1988. USITC staff interview with officials of the Greek Ministry of Foreign Affairs, Athens, Jan. 16, 1990.

⁴¹³ EC Commission, Press Release, IP (88) 877, Dec. 22, 1988; confirmed in USITC staff interview with EC Commission officials, Brussels, Jan. 8, 1990.

Since then, most member states have attempted to comply with the implementation requirement. The number of infringement actions was reduced by two as of March 1990 following the issuance by Luxembourg and Denmark of implementing legislation.⁴¹⁴ West Germany passed implementing legislation that took effect on January 1, 1990.⁴¹⁵ Portugal has also transposed the directive into national law. France, Belgium, and the Netherlands have drafted implementing legislation that they have not yet passed, whereas Spain is undecided over what form the transposition should take.⁴¹⁶

In spite of these efforts, the EC Commission has not suspended its enforcement procedures. The EC Commission has begun an action before the Court of Justice to seek revision of the United Kingdom's Consumer Protection Act,⁴¹⁷ which the EC Commission considers to not comply with the directive.⁴¹⁸ At issue is the United Kingdom's interpretation of what is permitted under the "development risks defense," which provides a defense to a producer if the defect could not have been discovered considering the state of technical knowledge at the time the product was put into circulation.⁴¹⁹ According to the EC, the United Kingdom's version of the defense is too generous to producers.⁴²⁰ The EC Commission has also sued Italy, both because it has allegedly watered down the development-risk defense and because Italy's implementing measure was not in an acceptable form.⁴²¹ The West German law may also result in Court of Justice litigation because it accords special treatment to producers of pharmaceuticals.⁴²²

Even after full implementation, differences among member states will remain. These differences involve the types of damages covered, the jurisdiction of various national courts, and court procedures. For example, the United Kingdom and Ireland permit "preaction discovery," a milder counterpart to U.S. pretrial discovery, by parties in lawsuits, whereas many other EC countries do not.⁴²³ Moreover, by the terms of the directive itself,

⁴¹⁴ The EC Committee of AMCHAM, *Business Guide to EC Initiatives*, Spring 1990, p. 7.

⁴¹⁵ Product Liability Act (Produkthaftungsgesetz); U.S. Department of State Telegram, "New Product Liability Law in Germany," Mar. 6, 1990, Bonn, Message Reference No. 07250.

⁴¹⁶ The Dutch bill is scheduled to pass by fall 1990, the Belgian bill by the end of the year. 1992—*The External Impact of European Unification* (Buraff Publications), June 1, 1990, pp. 5-6.

⁴¹⁷ Consumer Protection Act 1987, pt. 1, effective Mar. 1, 1988.

⁴¹⁸ EC US Business Report, vol. 2, No. 4, Apr. 1, 1990, pp. 7-8.

⁴¹⁹ The directive describes the defense as—

The producer shall not be liable as a result of this Directive if he proves... that the state of scientific and technical knowledge at the time when he put the product into circulation was not such as to enable the existence of the defect to be discovered. Art. 7, par. (e), Council Directive 85/374.

⁴²⁰ Report Drawn Up on Behalf of the European Parliament Committee on Legal Affairs and Citizens' Rights, Apr. 28, 1989, p. 9; EC-US Business Report, vol. 2, No. 4, Apr. 1, 1990, pp. 7-8.

⁴²¹ Presidential Decree No. 224 of May 24, 1988, effective July 30, 1988; Report of the Committee on Legal Affairs and Citizens' Rights, p. 9.

⁴²² 1992—*The External Impact of European Unification* (Buraff Publications), June 1, 1990, pp. 5-6.

⁴²³ Utz Toepke address.

member states may pass implementing legislation that is more stringent than the directive, in that the legislation may cover more products and exclude some defenses provided in the directive.⁴²⁴ Each member state may develop its own definition of what constitutes an "unacceptable risk," raising the possibility that producers will face a different liability standard in each state.

Other Measures

As a complement to the product liability directive, the EC Commission in 1989 proposed a directive on general product safety. The proposal provides for member states to take necessary measures to ensure that products marketed and used in the EC do not pose "an unacceptable risk for the safety and health of persons."⁴²⁵ Member states would require suppliers (importers and distributors as well as manufacturers) to use appropriate warning labels and monitor the safety of their products. Member states would establish procedures for the exchange of information on product risks.⁴²⁶ To aid the EC Commission in the product safety area, the proposal would establish a new Committee for Product Safety Emergencies, an advisory body composed of member-state representatives and chaired by an EC Commission representative.

The measure has generated controversy. Although the proposal began as a directive, the European Parliament has proposed that the measure be issued as a regulation. Moreover, although there were indications that the measure might be narrowed to cover only consumer products,⁴²⁷ Parliament has proposed no such narrowing of scope.⁴²⁸ West Germany and the United Kingdom have called for an exemption for foodstuffs and agricultural produce; France and Portugal oppose such an exemption. Belgium proposed to extend the measure to all products except those used exclusively for professional purposes; West Germany and the Netherlands opposed that move.⁴²⁹

The EC Commission has stated that it also plans to issue a proposed directive on civil liability for

⁴²⁴ West Germany, Greece, Portugal, and Spain have imposed a cap on the amount of damages a plaintiff can receive; the other member states have not. West Germany, Italy, Portugal, Denmark, the Netherlands, Ireland, and the United Kingdom permit producers to use the development-risk defense; France, Belgium, Luxembourg, and Greece do not. Utz Toepke address and conference materials, Tab H, p. 5.

⁴²⁵ EC Commission, Com (89) 162, June 7, 1990, art. 2, OJ No. C 193 (July 31, 1989), p. 1.

⁴²⁶ This information exchange would supplement the provisions of the EC Council's 1988 decision on a rapid information-exchange system on dangers arising from use of consumer products. Council Decision 89/45 of Dec. 21, 1988, OJ No. L 17/89.

⁴²⁷ USITC staff interview with officials of EC Commission Directorate General III, Brussels, Jan. 8, 1990.

⁴²⁸ OJ No. C 96 (Apr. 17, 1990), p. 284.

⁴²⁹ European Report, No. 1565, Internal Market, p. 5.

defective services.⁴³⁰ The draft proposal would apply only to services that may injure health and the physical integrity of persons and their property. A defect in a service would lead to liability depending on the degree of safety that can reasonably be expected, and force majeure (e.g., acts of God) or compliance with mandatory rules would obviate liability.⁴³¹ The Economic and Social Committee has recommended that the measure on general product safety be supplemented by a similar measure ensuring the safety of services.⁴³²

On October 4, 1989, the EC Commission proposed a directive on civil liability for damages caused by waste.⁴³³ The proposal resembles the product liability directive, particularly in the lack of a need to prove negligence, but adds a provision for obtaining redress for damage to the environment on top of damage to persons and property. The proposal also permits aggrieved persons to sue for injunctive relief to prevent further damage.⁴³⁴

Part 3. Industry Analysis

Agriculture

Overview

Previous USITC reports have noted that the primary focus of EC integration measures in the agriculture sector is to promote the free movement of products within the EC and to replace border control inspections between member states with inspections at the site of production.⁴³⁵ Approximately two-thirds of the 60 agriculture-related proposals contained in the EC Commission's White Paper for 1992 have already been adopted.⁴³⁶ Unlike the case of industrial products, the EC develops animal and plant health standards internally, consulting member-state authorities. These standards are legally binding and are enforced by member-state health authorities. The EC Court of Justice has explicitly excluded sanitary and phytosanitary questions from the principle of mutual recognition because the risks involved are too large. Currently, member states are allowed to maintain existing domestic legislation and prohibit

⁴³⁰ Fourth Progress Report of the Commission to the Council and the European Parliament Concerning the Implementation of the Commission's White Paper on the Completion of the Internal Market, Com (89) 311 final (June 20, 1989).

⁴³¹ AMCHAM, *Business Guide to EC Initiatives*, p. 28.

⁴³² EC Economic and Social Committee Opinion on the Proposal for a Council Directive Concerning General Product Safety, OJ No. C 75, (Mar. 26, 1990), p. 1.

⁴³³ EC Commission proposal of Sept. 1, 1989, OJ No. C 251, p. 3; Martijn van Empel, address to ABA-EC conference, "Europe 1992," June 8, 1990. "Waste" is broadly defined to encompass all types that are generated as a result of economic activity, with the exceptions of nuclear waste and pollution caused by oil. AMCHAM, *Business Guide to EC Initiatives*, p. 34.

⁴³⁴ *Ibid.*

⁴³⁵ See USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, p. 6-16.

⁴³⁶ U.S. Department of State Telegram, June 1990, Brussels, Message Reference No. 08309.

imports based on three criteria: public safety, public health, and plant health.⁴³⁷

EC goals concerning the 1992 plant quarantine regime are to replace crossborder plant-health checks with inspection at the site of production. Plant passports would replace plant-health certificates and would designate areas in which the product could be transported. Regions where these products would be restricted would be based upon phytosanitary contaminations rather than national borders. Under this program, third-country imports would still be required to have phytosanitary certificates but upon entrance into the EC would be given their plant passport and be treated in the same manner as EC products. Such action would prevent products originating in an infected region from entering uninfected areas. The EC plans to place the burden of inspecting imports on member states and to create an inspectorate to monitor these inspections.⁴³⁸

This report updates the status of several previously analyzed directives and analyzes several new developments. The EC's directives on hormones and "third country meat," BST, and pesticide residues for fruits and vegetables were all discussed in previous USITC reports.⁴³⁹ In the first six months of 1990, the EC took further steps on these matters. The United States and the EC have been involved in a dispute for several years concerning the use of certain artificial growth stimulants (hormones). The United States contends that EC regulations banning growth stimulants are scientifically unjustifiable and further contends that the use by the EC of the so-called fourth criterion (socioeconomic factors) in prohibiting use of substances is unfair. During the period under review, the EC modified its regulations relating to the substances. Also, the United States contends that the EC has for several years unduly restricted the number of U.S. meat facilities authorized to ship meat to the EC; recent EC regulations concerning such restrictions are described below. The EC also is terminating a suspension of a regulation on imports of bovine semen, potentially to the detriment of U.S. exports. Concerning pesticides for raw agriculture commodities, the EC expects to have to establish tolerances for up to 1,000 chemicals, of which they have completed 150. The EC Commission, supported by a strong consumer preference for labeling, has proposed labeling of postharvest chemicals for fruits and vegetables. The Parliament is now withholding its response to this directive in an effort to force stricter labeling requirements.⁴⁴⁰ As pertains to plant health, the EC's policy is to harmonize the registration of plant-protection

⁴³⁷ U.S. Department of State Telegram, June 1990, Brussels, Message Reference No. 08406.

⁴³⁸ U.S. Department of State Telegram, June 1990, Brussels, Message Reference No. 08406.

⁴³⁹ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-47 to 6-52.

⁴⁴⁰ U.S. Department of State Telegram, June 1990, Brussels, Message Reference No. 08406.

products on the basis of mutual recognition. Each member state is to allow import and sale of a pesticide registered in another when agricultural, plant health, or environmental conditions relevant to the use of the product are comparable.⁴⁴¹ Included in the following is a brief discussion of U.S.-EC developments in biotechnology.

Council Regulation 90/C 84/05 (ref. Com (89) 645) concerning fish inspection has been proposed by the European Community and bears watching. This regulation would lay down the health conditions for the production and placing on the market of fishery products.

Deep-Frozen Bovine Semen

Background

The EC imposes health and sanitary restrictions on intra-Community trade in, and imports of, bovine semen. The EC had suspended certain health regulations applicable to trade in bovine semen. The suspension had provided for trade in bovine semen collected from bulls that had a positive test for enzootic bovine leukosis (a viral, sometimes congenital disease, unique to cattle that is transmitted sexually through semen or blood) providing such semen had been subjected, with negative results, to a test for the presence of white blood cells.

Anticipated Changes

The subject directive (among other) terminates, effective June 30, 1990, the aforementioned suspension of certain health regulations applicable to trade in bovine semen. The directive also imposes an additional unrelated restriction on trade in bovine semen. The suspension of the regulation had provided an opportunity for the importation into the EC of some U.S. bovine semen that would otherwise be prohibited. Also, the additional unrelated restriction requires that semen be "collected in a center where all bulls give a negative result to a serum neutralization test or an ELISA test for infectious bovine rhinotracheitis or infectious pustular vulvovaginitis." Thus, the directive prohibits trade or imports of semen of all bulls in a group if any bulls in that group test positive to the tests as described above. Both the termination of the suspension of the regulation and the additional restriction are sources of complaints by U.S. interests.

Possible Effects

U.S. exports to the EC

Enforcement of the directive will likely result in a reduction in U.S. exports of bovine semen to the EC, although it is not possible to estimate how much

⁴⁴¹ "Debate on EEC-Wide Plant Health Product Register Widens," *European Report*, No. 1577 (Apr. 4, 1990), sec. 4, p. 11.

such exports will be reduced. An official of the National Association of Animal Breeders (NAAB) estimates that as many as 20 percent of U.S. cattle would test positive for enzootic bovine leukosis and thus their semen would apparently not be eligible for importation into the EC. The official also indicated that it would be prohibitively expensive for companies to administer the requirements applicable to the serum neutralization test or ELISA test for infectious bovine rhinotracheitis or infectious pustular vulvovaginitis. The requirement would apparently necessitate the maintenance of separate facilities limited to bulls testing negative for the diseases.

During 1989 the EC accounted for \$27.6 million, or 52 percent, of the total of \$53.0 million of U.S. exports of bovine semen, up from \$16.7 million, or 47 percent of the total of \$35.7 million of U.S. exports in 1987. U.S. exports of bovine semen to all markets accounted for an estimated 25 percent of the total quantity of U.S. sales in 1989, and U.S. exports to the EC amounted to an estimated 5 percent of total EC sales.

Diversion of trade to the U.S. market

It appears unlikely that enforcement of the directive will result in diversion of trade to the U.S. market. Most U.S. and EC imports of bovine semen are thought to be those of specific animals or bloodlines required by the animal breeder. Because there is little substitutability between strains it is unlikely that a third-country supplier would be adversely affected by the EC action, or that such products would represent a direct competitive threat in the U.S. market.

U.S. investment and operating conditions in the EC

U.S. investment in the EC bovine semen industry is thought to be negligible. Most U.S. trade consists of direct exports to EC interests.

U.S. Industry Response

An official of the NAAB contends that the enforcement of the directive will likely result in a reduction in U.S. exports of bovine semen to the EC for reasons described above. He further contends that animal health in the EC could be protected by means other than that required by the directive. He indicated that although an animal may test positive to exposure to the organism causing enzootic bovine leukosis, very few animals develop the disease, and impending development of the disease would be signaled by the presence of white blood cells. He indicated there is no scientifically defensible animal health reason for termination of the suspension described above. He also indicated there is no scientifically defensible animal health requirement to prohibit trade in semen from bulls with a negative result to a serum neutralization test

or an ELISA test for infectious bovine rhinotracheitis or infectious pustular vulvovaginitis merely because they were part of a group in which at least one bull tested positive.

Meat: Hormones, Inspection

Background

The EC restricts the use of certain artificial animal-growth stimulants (hormones) in the raising of food animals and restricts imports of meat from countries, such as the United States, where the use of such stimulants is authorized. For imports from the United States, the restrictions (which constitute a general prohibition with limited exceptions) have been in effect since January 1, 1989. Exceptions to the general prohibition include certain meat certified as coming from animals not supplied with the stimulants, veal (because veal animals would not normally receive the stimulants), and certain meat and animal organs for nonhuman use (pet food). The EC general prohibition has been a source of U.S.-EC conflict for several years and is the subject of an ongoing section 301 case. The United States contends that the EC policy is scientifically indefensible inasmuch as the stimulants have been found to be safe when properly used. EC officials generally contend that the issue is not scientific but rather one of consumer acceptance, citing instances of injury to human health, and subsequent adverse publicity, resulting from misuse of stimulants.

Anticipated Changes

The subject decision provides another exception to the restrictions on imports into the EC by allowing imports of meat of U.S. origin if the meat is certified as being obtained from cows that have only been used for dairy production, presumably because cows kept for dairy production are not normally administered the subject stimulants.

Possible Effects

U.S. exports to the EC

The decision will likely result in an increase in U.S. exports of beef to the EC. Although the amount of such an increase cannot be estimated exactly, it will likely be at most a few million pounds. The United States is a net importer of manufacturing-type beef (the type derived from dairy cows) and in the EC must compete with manufacturing-type meat produced domestically and imported from Australia, New Zealand, Eastern Europe, and certain African countries. Even with an increase, the United States is likely to account for only a small share of the EC market (less than 2 percent) and the exports are likely to account for less than 2 percent of U.S. production of that and similar types of meat.

Separate statistics are not available for U.S. exports of beef derived from dairy cows, but such

exports are thought to be minimal. U.S. exports of all beef and veal to the EC decreased from 18.0 million pounds, valued at \$32.6 million, in 1987 to 5.0 million pounds, valued at \$8.0 million, in 1989. The EC accounted for about 4 percent of the total value of U.S. exports of beef and veal in 1987, but only about 0.5 percent in 1989. The decline apparently reflects the previously described EC restriction.

Diversion of trade to the U.S. market

It appears unlikely that enforcement of the decision will result in a significant diversion of trade to the U.S. market inasmuch as it is expected to have a minimal generally positive impact on trade.

U.S. investment and operating conditions in the EC

U.S. investment in the EC beef industry is thought to be negligible. Most U.S. trade consists of direct exports to EC interests.

U.S. Industry Response

While domestic interests generally do not object to the decision, they contend that it should not be necessary, inasmuch as the original restrictions are unjustifiable.

Third Country Meat Directive

There were few developments concerning the so-called Third Country Meat Directive(s) during the first half of 1990. On May 8, 1990, the EC published a list of sites (60 slaughterhouses, 41 cutting premises, and 74 cold storage facilities) eligible to ship meat and products to the EC. The total number of approved sites is 151 because some sites are approved in more than one category. The composition of the list was only slightly different from a similar list released January 29, 1990. However, the January list included several sites that had only temporary eligibility to ship meat and products to the EC pending EC-required modifications; nearly all of the plants completed the modifications, and the May list included them without qualification. Domestic interests and the U.S. Government contend that the May list is still too restrictive.

During the first half of 1990 the EC instituted a mandatory residue test program. The tests include those for certain heavy metals (lead and cadmium), and certain substances (clenbuterol, Beta-blockers, tranquilizers, thyrostatics, and 4 hormones that are growth stimulants) used by some producers engaged in animal agriculture. The residue test program establishes an absolute prohibition for some of the substances and tolerable levels for others.

The American Meat Institute (AMI), a trade association representing meat packers and meat processors, and one of the original participants in a section 301 complaint concerning the EC

meat-import policy, objected to the residue test requirement in a letter to the U.S. Secretary of Agriculture. The AMI described the program as a "new level of harassment" and indicated that the requirements will be expensive to enforce.

Animal Growth Stimulants

There were apparently few developments concerning animal growth stimulants (hormones) during the first half of 1990 except for a residue test program associated with the list of facilities authorized by the EC to ship meat there (see Third Country Meat Directive) and the previously discussed Decision (90 120) Amending Decision 89/15 on the importation of live animals and fresh meat from certain third countries.

The residue test program requires that facilities enforce EC-approved testing procedures for the presence of several substances, including certain growth stimulants (hormones) before meat from the facilities is eligible for shipment to the EC. The decision (90 120) provides another exception to the animal growth-stimulant-related restrictions on meat imports into the EC by allowing imports of meat of U.S. origin if the meat is certified as being obtained from cows that have only been used for dairy purposes, presumably because cows kept for dairy production do not receive the subject stimulants.

Biotechnology

Biotechnology is a loosely defined concept encompassing various processes employed by different business sectors. The processes include recombinant DNA technology; monoclonal antibody technology; bioprocess technology; and cell culturing, as well as embryo manipulation and transfer.⁴⁴² Biotechnology may be divided into several sectors: therapeutics (human or animal); diagnostics (human or animal); agricultural (genetics or microbial protectants); and, others (including chemicals, waste management, enhanced land use, and industry suppliers).⁴⁴³

Although biotechnology is not new (fermentation and genetic selection have been used for thousands of years), developments in the study of biology during the 1950s led to initial commercialization of innovative biological techniques in the 1970s and 1980s. These innovative biotechnological commercial activities are still generally considered to be in development, with much of the efforts devoted to research and development. Industry suppliers are generally considered to be the most mature sector, followed by therapeutics and diagnostics. Agriculture is still primarily research and development oriented; indeed, research and development expenditures

⁴⁴² U.S. Department of Commerce, *U.S. Industrial Outlook 1990*, p. 20-1.

⁴⁴³ Ernst & Young High Technology Group, *Biotach 90: Into the Next Decade*, (New York: Mary Ann Liebert, Inc., 1989), p. 23.

were reported to have been equal to about 146 percent of sales.⁴⁴⁴

Although detailed statistics are not available, sales of human therapeutics are estimated to have amounted to about \$650 million in 1989; human diagnostics, \$360 million; and agriculture, \$50 million.⁴⁴⁵ There are about 1,100 biotechnology companies in the United States, employing estimated 60,000 people.⁴⁴⁶ although most biotechnology companies are small, employing 50 or fewer persons, subsidiaries of large companies account for a significant share of total industry employment and sales.

According to an official of the Industrial Biotechnology Association (IBA), an industry trade association composed almost exclusively of U.S.-based companies, the United States has accounted for about 90 percent of world sales attributed to biotechnology processes. Less than 2 percent of biotechnology companies list foreign-company competition as a key business issue.⁴⁴⁷

Nearly all biotechnology companies have foreign sales, which are expected to increase from 16 percent of total sales in 1989 to 36 percent in 10 years. whereas agriculture, of total sales are expected to increase from less than 10 percent to 25 percent within the next 10 years.⁴⁴⁸ Over half of the agricultural biotechnology companies are thought to have sales in Western Europe.⁴⁴⁹

Nearly two-thirds of all U.S. biotechnology companies and 68 percent of agricultural biotechnology companies viewed the EC 92 program as positive for the future, citing united regulatory and patent law and easier cross-border passage.⁴⁵⁰ Trade sources report that over half of U.S. biotechnology companies have strategic alliances with European companies.⁴⁵¹ Approximately 73 percent of these companies cited marketing capability as a factor in considering alliances in Western Europe; 43 percent named availability of capital; 16 percent listed research capability; and 29 percent mentioned regulatory experience.⁴⁵² Some EC-based companies are reported to have entered into strategic alliances and invested in U.S.-based biotechnology companies, in part because of a more restrictive regulatory environment in the EC.⁴⁵³ However, European

Some U.S. companies have manufacturing facilities outside the United States, including facilities in the EC. One company has a facility to patent systems are frequently preferred over the U.S. system by U.S. biotechnology companies. produce BST in Ireland; however the facility is subject to the EC restrictions on sales of BST.

Granada BioSciences, Inc., a Texas-based biotechnology and genetic engineering company, was among the earliest participants in embryo-transfer technology in the 1970s and extended its research and development activities to include cloning in the 1980s. The company recently opened a laboratory in the United Kingdom to produce cloned dairy cow embryos. The laboratory is to produce 80,000 pregnancies from the embryos. The laboratory is part of a 5-year exclusive agreement with the Milk Marketing Board of the United Kingdom to improve the United Kingdom's dairy herd. The 5-year agreement is expected to generate revenues of \$135 million.⁴⁵⁴

The U.S. Office of Technology Assessment (OTA) identified five countries as major potential competitors of the United States with respect to the commercialization of biotechnology: Japan, West Germany, the United Kingdom, Switzerland, and France.⁴⁵⁵ Japan is expected to be a major competitor in specialty chemicals, produced by biotechnology processes, and possibly pharmaceuticals. Japanese pharmaceutical companies have not traditionally been major exporters, but Government promotion, rising investments in research and development, and increased domestic competition portend a larger role for Japanese pharmaceutical companies in the world market. West Germany was identified as having an extensive research base and a large private sector with an international marketing apparatus. However, West Germany was also found to have funding and administrative problems in its universities and an inflexible Government policy for implementing biotechnology policy. The United Kingdom's advantages include a strong basic and applied research base, the Government's strong interest in direct measures to stimulate the commercial development of biotechnology, the excellent university system, and a relatively positive regulatory environment. On the other hand, the United Kingdom's private sector was thought to be less aggressive than that of the United States. Switzerland was identified as having a good university system and several renowned research

⁴⁴⁴ Industrial Biotechnology Association, Congressional Seminar on the Biotechnology Industry, "Selected Readings," p. 17.

⁴⁴⁵ *Ibid.*, p. 13-5.

⁴⁴⁶ Ernst & Young High Technology Group, *Biotach 90*, p. 20.

⁴⁴⁷ *Ibid.*, p. 37.

⁴⁴⁸ *Ibid.*, p. 31.

⁴⁴⁹ *Ibid.*, p. 87.

⁴⁵⁰ *Ibid.*, p. 31.

⁴⁵¹ *Ibid.*, p. 65.

⁴⁵² *Ibid.*, p. 66.

⁴⁵³ Ms. Lisa Raines, Director of Government Relations, Industrial Biotechnology Association, meeting with USITC staff, Apr. 27, 1990.

⁴⁵⁴ "The National Provisioner," Apr. 23, 1990, vol. 202, No. 15, p. 22; The Milk Marketing Board of the United Kingdom is chartered by Parliament to manage the marketing of the country's milk and milk products. Government-owned, the board is reported to be the fourth-largest food company in Europe and the 50th largest business in the United Kingdom. The board is also the largest volume supplier of bull semen, insemination services, and embryo-transfer services in the United Kingdom.

⁴⁵⁵ *Commercial Biotechnology: An International Analysis* (Washington, DC: U.S. Congress Office of Technology Assessment, January 1984), OTA-BA-218, pp. 505-530.

institutions, a strong financial sector, and a technology-based, export-oriented economy. However, for a number of reasons including aversion to financial risk and adverse publicity related to health concerns, the Swiss private sector has only recently begun to concentrate in the biotechnology sector. France was found to have a well-coordinated Government policy and an adequate funding program but a shortage of personnel and an initially hesitant private sector.

Subsequent to the OTA assessment, the EC regulatory environment apparently became more restrictive. Industry sources have suggested that in recent years regulations associated with environmental concerns made the EC biotechnology sector less competitive than it otherwise would be and that continued enforcement of or additions to the regulations would continue to adversely affect the EC's competitive position.⁴⁵⁶ Trade sources report that European biotechnology companies, at least in part because of the restrictive regulatory environment, are considered to be at least 3 years behind the United States and Japan.⁴⁵⁷

Processed Foods and Kindred Products

Overview

Previous USITC reports have explained that the EC processed foods and kindred products industry is similar in structure to the U.S. industry. The majority of the production and trade within the EC market is done by large firms that are integrated horizontally, vertically, or both ways. The largest firms are located in the northern member states; the more southern member states' industrial structures are characterized by smaller enterprises. According to the U.S. Department of Commerce, 8 out of the 10 leading processed-food firms in the EC are U.S.-based multinational firms. Many of the larger companies have foreign subsidiaries. The U.S. Department of Commerce has noted that these multinational firms will most likely be able to influence Community decisions, but that smaller firms, which accounted for \$600 million in direct U.S. exports in 1988, do not appear to have such a voice in the EC's process for developing directives and other requirements on processed foods.

The EC's approach to food-additive legislation is both broader in scope and more restrictive than that in the United States. The EC has defined a food additive as anything not normally eaten by itself, thus substances such as baking soda and salt are theoretically within the scope of EC regulation. Moreover, only substances which are specifically approved are permitted to be used. This so-called "positive list" approach on foodstuffs contrasts with the EC's approach to chemical regulation, where "negative lists" of products specifically banned or

restricted are developed; substances not on such lists are permitted to be used. The U.S. FDA also uses positive lists for food additives, however, a large number of substances are considered to be "Generally Recognized as Safe" and thus do not need FDA pre-market authorization. Some in U.S. industry have expressed concern that the process of gaining approval for new food additives will most likely be lengthy, especially for producers outside the EC.

The EC Commission is largely responsible for evaluating food-safety issues. The Scientific Committee for Food (SCF) and the Food Advisory Committee (FAC) assist the EC Commission in developing new food standards. Proposals for a more formal system, such as a cooperative system between national institutes, are reportedly under consideration. In addition, the creation of a European food agency, which would act as an inspection and control service, has been discussed.

Earlier USITC reports analyzed seven directives pertaining to processed foods and kindred products. This report updates the status of those directives and analyzes new EC proposals in organic foods, nutritional labeling, tobacco labeling, advertising, and taxation.⁴⁵⁸

Several proposals acted upon by the EC during the first 6 months of 1990 were noteworthy. The EC Commission continued its efforts to develop a "positive list" of materials permitted to come in contact with foodstuffs. Among the products, in addition to foodstuffs, that could be affected by this directive are pulp and paper, chemicals, plastics, glass, ceramics, metals and alloys, certain wooden products, and a host of miscellaneous products associated with food and beverage packaging and serving applications.

The EC also proposed a comprehensive and fairly stringent set of rules that must be followed before a foodstuff can be called "organic." The proposed directive appears to be no more stringent than regulations currently under consideration by the U.S. Congress. Because of this, the EC directive appears unlikely to harm U.S. exports of organic foods.

The EC also moved closer to final adoption of regulations for nutritional labeling. Both proposals are likely to result in mandatory labeling of most foods. In 1989, total U.S. exports of raw agricultural and processed-food products were \$27.4 billion, of which the EC accounted for approximately 14 percent, or \$3.7 billion. Processed-food

⁴⁵⁶ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-53 to 6-65. In the March 1990 USITC followup report, the following specific directives were analyzed: official control of foodstuffs (Directives 89/397 and Com(89) 225 final 76), food additives (Directive 89/107), quick-frozen foods (Directive 89/108), infant formulas and followup milks (Proposal (86)564 final), maximum tar yield of cigarettes (Com (89) 398 final), spirit drinks (Council Regulation 89/1576), and materials and articles in contact with foodstuffs (Directive 89/109).

⁴⁵⁸ Lisa Raines meeting.

⁴⁵⁷ *Business Week*, June 18, 1990, pp. 177-178.

products – the category that will be most affected by these proposals – typically accounts for about 25 percent of U.S. food exports. U.S. firms and trade associations have indicated that the integration of EC labeling regulations is likely to facilitate U.S. exports to the EC. Other activity in this area has included discussions over a harmonized food-quality program. Such a program would involve both harmonizing names of geographical locations and the use of a quality mark to designate a product of a higher standard than required by the general market. Such a program would be voluntary and available to third-country imports.⁴⁵⁹

Several directives affecting the sale of manufactured tobacco products were acted upon, notably the directive rules concerning labeling regarding public health risks. If passage of the directive promotes consumer use of U.S.-blend cigarettes, which are generally lower in tar content U.S. brands of cigarettes manufactured in Europe could gain market share. Another directive, requires member states to comply with EC rules relating to tobacco-product advertising. The outlines of EC rules are not yet clear, however, which makes it difficult to predict the impact on U.S. firms. Harmonization of tobacco excise taxes is not expected to occur in the near term,⁴⁶⁰ and new opposition will likely delay agreement. In May 1990, the EC Council adopted final rules limiting tar yield of cigarettes to 15 milligrams by December 31, 1992, and to 12 milligrams by December 31, 1997.

Organic Production of Agricultural Products

Background

In the first months of 1990, a draft proposal for a council directive on organic foods was made available to USITC staff. The purpose of the directive is to set the minimum standards by which organic foods can be produced and marketed in the European Community. As in the United States, the dramatic rise in popularity of organic foods in the EC has generated the need to ensure that such foods are, in fact, organically grown. Any producer or exporter to the EC wishing to market products as “organic” will have to comply with the standards set forth in this directive. The U.S. Congress is working on a similar proposal for the U.S. organic foods industry.

Anticipated Changes

The adoption of this proposal will result in the establishment of Communitywide standards for the production and marketing of foodstuffs labeled as “organic” in the EC. The staff of the EC Commission Council were to formally submit a proposal

⁴⁵⁹ U.S. Department of State Telegram, June 1990, Brussels, Message Reference No. 08406.

⁴⁶⁰ Don Nelson, Philip Morris Inc., telephone conversation with USITC staff, May 31, 1990.

for council consideration by the end of July 1990. In general, synthetic chemicals may not be used in the production of an item unless they are absolutely essential and no other more suitable substitute exists. The Council is considering an exemption for certain traditional chemicals such as sulfur and copper; however, the EC Commission opposes this exemption.⁴⁶¹ The directive also provides for inspection of both facilities and products in the EC organic foods industry. Article 11 of the proposed directive specifies the ways in which third-country producers can obtain clearance to market their foodstuffs in the EC. The EC Commission intends to draw up a list of certified third-country producers, the imports of which must be accompanied by a certificate of inspection. Annex I of the directive states that foodstuffs marketed as “organic” in the EC cannot have been subject to synthetic chemicals for at least 1 year prior to sale.

Possible Effects

U.S. exports to the EC

The EC is a large and growing market for U.S. organic foods. All such products will be affected by the regulations. However, this directive is not likely to harm U.S. exporters of organic foods to the EC. The U.S. Congress is likely to pass a bill on organic food regulations that will be far more stringent than the current EC proposal. For example, the Senate proposal, S. 2108, requires that at least 3 years elapse between the last chemical application and the time of retail sale. Because U.S. standards, if passed, are likely to meet or exceed those of the EC, the prospects for gaining EC approval of U.S. standards under article 11 of the proposed directive appear favorable. Under that scenario, the requirement to obtain EC certification and inspection should not pose a serious obstacle to U.S. suppliers and may in fact represent an improvement over current procedures. However, the impact of the regulations will ultimately depend on how significant the time, paperwork, and financial burdens of obtaining such inspection and certification are on U.S. suppliers.

According to industry and Government experts, U.S. exports of organic foods have been increasing dramatically in recent years. The EC, Japan, and Canada are the principal markets for U.S. exports. Although some of the larger organic food producers export their products to the EC directly, many of the smaller and medium-sized firms use brokers to market their products overseas. Most organic food producers – whether processors or farmers – are small compared with the major U.S. food companies.

Data on U.S. exports of organic foods are not available, because U.S. Customs does not monitor trade flows of organic foods to and from the United States. According to official statistics of the U.S. Department of Commerce, total U.S. exports of raw agricultural products and processed food products

⁴⁶¹ U.S. Department of State Telegram, June 1990, Brussels, Message Reference No. 08406.

were \$27.4 billion in 1989, of which the EC accounted for approximately 14 percent of that amount, or \$3.7 billion. Organically grown food products more than likely account for less than 5 percent of that amount, but their share is growing. Total sales for the industry reportedly were \$1.5 billion in 1989, the bulk of which was sold within the United States.⁴⁶²

Diversion of trade to the U.S. market

This proposal should not result in the diversion of organic food products from other third-country producers to the U.S. market. As mentioned above, the EC proposal calls for less stringent regulations than those proposed in the U.S. Congress. Therefore, it is unlikely that any third-country producer would view the United States as a more liberal alternative for their products.

U.S. investment and operating conditions in the EC

There is no known U.S. investment in organic farming or food production in the EC, although such investment may exist. As a rule, U.S. firms usually do not own the European farms from which they purchase their raw products for processing. In the processed-foods industry, it is possible that some of the larger U.S. firms may have invested in organic-food processors in the EC. Even if part of this investment is in organic-food production, it is unlikely that this proposal will either encourage or discourage such investment in the future, unless the certification requirements for third-country suppliers prove more burdensome than those for EC-based producers.

U.S. Industry Response

Industry sources contacted have indicated some awareness of the EC proposal, but they are more interested in the bills pending in the U.S. Congress. Several firms indicated that European consumers have a high opinion of organic-food products from the United States. In addition, sources informed ITC staff members that an organization known as IFOAM (International Federation of Organic Agricultural Movements) is working on developing an international accreditation system for organic farming. Organic farmers and processors in the United States, the European Community, and other countries have participated in IFOAM conferences and are showing a willingness to adhere to its certification standards. More than one source believes that mutual cooperation between the United States and the EC could be more readily achieved through IFOAM than at the governmental level.

Several sources added that the integration of the EC market into one unified market will facilitate the trade of organic foodstuffs in the EC. Since a large

percentage of U.S. exports of organic foods is perishable, the elimination of internal border inspections could greatly reduce the risk of product spoilage.

Labeling, Advertising, and Presentation of Foodstuffs

Background

The EC has advanced two major proposals dealing with the labeling of foodstuffs. One directive consolidates current EC requirements into a single comprehensive directive. It requires manufacturers to follow common rules for food labeling and advertising. The second directive harmonizes member states' regulations on nutrition labeling. Both proposals are likely to result in mandatory labeling of most foods, except in the cases of fresh produce, mineral waters, and certain other items consisting of a single ingredient.

Anticipated Changes

Proposal Sec (89) 2151 calls for the consolidation of Council Directive 79/112 and all subsequent amendments into one single directive. By combining these directives into one package, the Council hopes to eliminate confusion and to facilitate the process of harmonizing the labeling and advertising laws of the different member states. The proposal introduces no new legislation, nor does it suggest the banning of any ingredients or treatments to foodstuffs. The proposal is concerned only with products sold directly to EC households or mass caterers. The directive would, however, require that manufacturers provide certain types of information on food packages and use a common format for presenting such information. It also sets rules regarding advertising.

In February 1990, the EC internal market ministers reached a "common position" on the nutrition labeling of foodstuffs marketed in the EC. The proposal reflects the growing public awareness of the link between nutrition and health and the consumers' resulting desire to have more information on the nutritional content of the food they purchase. The proposal would require nutrition labeling only when food manufacturers make health claims on the package.

Sec (89) 2151, which is the more comprehensive of the two proposals, will require the following: (1) the listing of ingredients on all packages (with some exceptions); (2) the "date of minimum durability" (or expiration date); (3) the place of origin in cases where the lack of such information might mislead the consumer; and (4) indications that a foodstuff has been subject to ionizing radiation (not applicable to ingredients in compound foodstuffs). The nutritional-labeling proposal would require food manufacturers to provide information on energy value, protein, carbohydrates, and fat when any kind of nutrition claim is made. Information on sugars, saturates, fiber, and sodium would also be required if the nutrition claim involved one of those

⁴⁶² Based on conversation with the Catalyst group, Brattleboro, VT.

constituents. Third-country producers would also be expected to comply with these regulations; however, neither proposal gives much information on how imports will be inspected for compliance.

Possible Effects

U.S. exports to the EC

Since labeling requirements are common in the processed-food industry, both proposals, if adopted, are not likely to hurt U.S. food exports. Many producers have stated that the harmonization of EC labeling laws into one single code is actually a net positive benefit for U.S. exporters. Processed-food products—the category that will be most affected by these proposals—(typically) accounted for less than 25 percent of the \$3.7 billion in 1989 U.S. food exports to the EC.

Diversion of trade to the U.S. market

The labeling proposals are not likely to result in diversion of trade from the EC to the U.S. market since the directive is not expected to harm foreign suppliers. Other significant third-country producers include Canada, Mexico, Southeast Asia, and other Western European countries (Austria, Sweden, Switzerland, etc.). Most of these countries perceive the United States as having very specific, well-defined labeling laws. Even in the event of a worsening EC regulatory environment, it is unlikely that such suppliers would view the United States as a liberal alternative for their exports.

U.S. investment and operating conditions in the EC

These proposals should have little or no effect on U.S. investment portfolios in the European Community. Several industry sources stated the benefit from producing only one label for each product will far outweigh the negative aspects of these proposals. Nevertheless, U.S.-owned subsidiaries in the EC will probably show more flexibility in complying with the new labeling laws than will U.S.-based firms.

U.S. direct investment in food manufacturing in the EC is quite large and accounts for over half of U.S. overseas investment in this area. In 1988, U.S. investment in EC food manufacturing reached \$7.4 billion,⁴⁶³ nearly double the 1981 level of \$3.7 billion.⁴⁶⁴ The leading U.S. investors include Pepsico, Mars Food Manufacturers, Kellogg, and Heinz.⁴⁶⁵ U.S. companies either partially or wholly own 12 of the 20 largest EC food-manufacturing firms.⁴⁶⁶

⁴⁶³ U.S. Department of Commerce, *Survey of Current Business*, vol. 69, No. 8, August 1989, p. 69.

⁴⁶⁴ U.S. Department of Commerce, *EC 1992: A Commerce Department Analysis of European Community Directives*, vol. 2, SIMIS No. L-131, p. 22.

⁴⁶⁵ "Blueprint for a New Europe," *Financial Times*, Mar. 5, 1990.

⁴⁶⁶ "Europe 1992: Implications for Food and Agriculture," *National Food Review*, U.S. Department of Agriculture, October-December 1989, p. 18.

U.S. Industry Response

U.S. firms and trade associations have indicated that the integration of EC labeling regulations is likely to facilitate U.S. exports to the EC. In addition, the costs of producing only one label for each product will be much less than the costs of producing several different labels. Because of the specificity of U.S. laws, U.S. firms already have to comply with some of the requirements of the proposed EC law, such as the listing of ingredients. In the U.S. market, food manufacturers are required to list ingredients and support nutritional claims on most food packages; however, they are not required to mention irradiation treatments or to provide an expiration date on most canned or frozen foods (although the latter has developed in practice). However, one source expressed concern over the "date of minimum durability" requirement, which is still optional in the United States. The source indicated that the selection of an expiration date is purely arbitrary and may result in misleading information about product quality.

Labeling of Tobacco Products

Background

In February of 1988, the EC Commission presented to the Council its original proposal on the labeling of tobacco products. An amended proposal⁴⁶⁷ was submitted on March 11, 1989, after the EC Commission took into account the opinions of the Economic and Social Committee⁴⁶⁸ and the European Parliament.⁴⁶⁹ The directive, passed November 13, 1989, requires that the marketing and free movement of tobacco products be made subject to uniform rules concerning labeling that take due account of public health protection.⁴⁷⁰

Anticipated Changes

Member states will be required to comply with uniform EC rules regarding health warning labels on tobacco products marketed in the EC. Most EC member countries already have laws requiring health warnings on tobacco products; only Luxembourg, Greece, and Italy do not have such requirements.⁴⁷¹ Under the EC directive, all tobacco product packages must carry a general warning and cigarette packages must carry one of several additional, specific warnings. Labels for cigarette packages also must include information on tar and nicotine yields measured on the basis of the ISO 4387 and ISO 3400 methods. Member states are to adopt the laws, regulations, and administrative

⁴⁶⁷ Com (87) 719 final/modified.

⁴⁶⁸ OJ No. C 48 (Feb. 20, 1988), p. 8, and OJ No. C 237 (Sept. 12, 1988), p. 43.

⁴⁶⁹ OJ No. C 12 (Jan. 16, 1989), p. 106, and OJ No. C 291 (Nov. 20, 1989).

⁴⁷⁰ The Economic and Social Committee held in 1986 that the printing of health warnings on packages of all tobacco products is a vital factor in the protection of public health (OJ No. C 184 (July 27, 1986), p. 19).

⁴⁷¹ "Health: European Parliament Opts for Strict Rules on Tobacco Labelling," *European Report* (Oct. 14, 1989), p. 3.

provisions necessary to comply with the directive before July 1, 1990. Such laws and regulations are to be brought into force before December 31, 1991. A period of 1 year for cigarettes and 2 years for other tobacco products is allowed for the sale of existing products that do not comply with the new requirements.

Possible Effects

U.S. exports to the EC

The directive is unlikely to significantly affect direct U.S. exports to the EC. It is difficult to predict how much the labeling will discourage consumer use of tobacco products, particularly U.S. products. U.S. tobacco product exports to the EC in 1989 totaled \$1.7 billion. Over half of U.S. tobacco exports to the EC were cigarettes (valued at \$963 million). However, trade sources indicate that most of the cigarettes did not enter the EC market, because of the 90-percent EC common customs tariff on cigarettes, but instead were transshipped to other markets.⁴⁷² Tobacco leaf follows cigarettes in value of tobacco product exports to the EC, with a value of \$518 million in 1989.

Labels that contain health warnings and inform consumers about tar and nicotine content of particular cigarette brands may enhance consumer preferences for low tar cigarettes. Most "American blend" cigarettes have lower tar content than the dark tobacco varieties that have been popular in Europe. To the extent that consumers switch from high-tar cigarettes, U.S. brands of cigarettes and U.S. exports of light tobacco leaf used in American blend products could gain market share. Alternatively, some high-quality U.S. tobacco leaf is of relatively higher tar and nicotine, so some softening of demand for higher quality U.S. leaf is possible.⁴⁷³

Diversion of trade to the U.S. market

Trade sources indicate it is unlikely that any major third-country supplier will divert tobacco products originally intended for the EC market to the U.S. market because of this directive.

U.S. investment and operating conditions in the EC

U.S. tobacco firms are known to have substantial investments in the EC, although precise data are unavailable. Manufacturing subsidiaries of U.S.

⁴⁷² EC tariffs for other tobacco products: leaf = 14-23 percent; cigar = 43 percent; smoking tobacco = 117 percent; reconstituted = 26 percent; chewing = 65 percent; other manufactured = 26 percent. Don Nelson, Philip Morris Inc.

⁴⁷³ Dan Stevens, U.S. Department of Agriculture, Foreign Agricultural Service, telephone conversation with USITC staff, June 1, 1990.

companies and U.S. brands manufactured under license arrangements with EC tobacco producers supply over 30 percent of the EC market, and the share is growing. If passage of the directive promotes consumer use of American blend cigarettes, U.S. brands of cigarettes manufactured in Europe could gain market share.

U.S. Industry Response

Officials of Philip Morris Inc. and R.J. Reynolds Tobacco Co. have indicated to USITC staff that because labeling requirements already exist for most tobacco products in the majority of EC countries, industry could agree to harmonization of the rules. The industry objects to certain other provisions of the directive, particularly requirements that apply only to manufactured cigarettes and not to other tobacco products. The firms also countered that some of the warning texts required are not consistent with scientific knowledge about the effects of smoking.

Advertising of Tobacco Products

Background

On April 7, 1989, the EC Commission transmitted to the EC Council its initial proposal for a directive on advertisements of tobacco products in newspapers, magazines, and similar publications and in posters and bills. The proposal would not ban advertising, according to an opinion in favor of the directive adopted by the Economic and Social Committee.⁴⁷⁴ The directive would (1) require all cigarette advertisements to carry specific health warnings and advertisements of other tobacco products to carry a general warning; (2) limit advertisements to the depiction of the tobacco product packet itself, possibly with added information on the features of the product; (3) prohibit advertising in the press or by means of posters and bills that refer to a trademark, emblem, or symbol used mainly in connection with tobacco products; and (4) ban tobacco product advertisements from publications intended for people under 18 years old.

The European Parliament approved the EC Commission proposal after making several substantive amendments on March 14, 1990.⁴⁷⁵ The amended version of the proposed directive would ban all forms of tobacco advertising in the press, by means of posters and bills, in film or any other advertising medium. The amendments also would prohibit all indirect forms of tobacco promotion, such as use of trademarks and emblems on clothing, cigarette lighters, and the like, or sponsorship of activities and sporting events.

⁴⁷⁴ OJ No. C 62/23 (Mar. 12, 1990).

⁴⁷⁵ OJ No. C 96/93 (Apr. 17, 1990).

Anticipated Changes

Some existing laws in EC member states restrict tobacco advertising. Tobacco advertising is prohibited under national laws in Italy and Portugal and is restricted in Greece, Belgium, the United Kingdom, the Netherlands, and Spain.⁴⁷⁶ The French Parliament currently is considering whether to ban tobacco advertisements. If the directive becomes effective, member states will be required to comply with EC rules relating to tobacco product advertising. However, because the extent of the restrictions contained in the final directive is not yet known, anticipated changes in such member-state laws are uncertain.

Possible Effects

U.S. exports to the EC

As noted previously, direct U.S. imports of cigarettes to the EC are limited. The extent to which restrictions on tobacco advertising will affect direct U.S. exports to the EC is unclear. Cigarettes are the primary type of tobacco product advertised, and they are likely to be affected most should the directive be implemented. Some industry sources maintain that tobacco advertisements do not affect consumption overall but only encourage smokers to switch among various brands of tobacco products. To the extent this is true, the proposed directives may have little effect on consumption of some U.S. products, particularly unmanufactured tobacco and cigarette brands that are well known to EC consumers. However, introducing U.S. cigarette brands to new markets in the EC or introducing new product lines will likely be more difficult if stringent advertising restrictions are implemented.

Diversion of trade to the U.S. market

Trade sources indicate it is unlikely that any major third-country supplier will divert tobacco products originally intended for the EC market to the U.S. market because of this directive.

U.S. investment and operating conditions in the EC

Information is not available to determine how U.S. brands of cigarettes manufactured in Europe would be affected by the proposed advertising restrictions.

Tobacco Excise Taxes

Harmonization of tobacco excise taxes is not expected to occur in the near term,⁴⁷⁷ and new opposition will likely delay agreement on any proposal to harmonize excise taxes. Southern European tobacco firms have opposed EC

⁴⁷⁶ "What Price Tobacco Ads? A Countdown in France," *New York Times*, Apr. 9, 1990, p. D-8.

⁴⁷⁷ Telephone conversation with Don Nelson, Philip Morris Inc., May 31, 1990.

Commission proposals to harmonize excise taxes on tobacco and cigarettes, saying that harmonization would unfairly affect their region.⁴⁷⁸ To attain the minimum tax proposed by the EC Commission, some member countries would need to raise their taxes and other countries would need to reduce taxes.⁴⁷⁹ For cigarettes, the minimum tax rate proposed in December 1989 would be 15 ECU per 1,000 cigarettes, effective January 1, 1993.⁴⁸⁰

Tobacco firms in Italy, Portugal, Spain, Greece, and France contend that the proposal burdens the southern countries with more than their fair share of fiscal reform. Under the 1989 EC Commission proposal, Spain and Greece would have had to raise their taxes to attain the minimum tax rate.

In May 1990, the southern tobacco firms presented a counterproposal to the EC Commission, which would provide for a specific tax of no more than 3 ECU per 1,000 cigarettes. Under the counterproposal, only Greece would need to increase taxes to reach the minimum rate. On the other hand, harmonization of excise taxes is expected to reduce taxes on tobacco products in the United Kingdom.⁴⁸¹

The U.S. industry prefers a specific tax rather than an ad valorem rate or a combination of ad valorem and specific taxes.⁴⁸²

Maximum Tar Yield of Cigarettes

In May 1990, the EC Council adopted final rules limiting tar yield of cigarettes to 15 milligrams by December 31, 1992, and to 12 milligrams by December 31, 1997.⁴⁸³ Greece received derogations so that tar yield of cigarettes sold in Greece would be limited to 20 milligrams by December 31, 1992, and to 12 milligrams by December 31, 2006. The final compromise followed extensive discussion among member states over several earlier proposals.⁴⁸⁴

The proposed directive covers manufactured cigarettes and indirectly could affect the demand for dark tobacco varieties, which generally contain more tar than light tobacco. Alternatively, tar yield can be reduced by changing filters rather than modifying tobacco blends. To the extent that EC

⁴⁷⁸ *European Report*, No. 1582 (Apr. 28, 1990), p. 2.

⁴⁷⁹ Tax rates now in place vary widely. For example, the highest tax on cigarettes is in Denmark, at 85 percent of retail value, approximately 10 times the tax rate applied in Greece. USDA, FAS, *Tobacco Annual Report*, Brussels, Belgium, Apr. 30, 1990, p. 3.

⁴⁸⁰ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 10-6.

⁴⁸¹ U.S. Department of Agriculture, Foreign Agricultural Service, "Modest Increase Only in UK Tobacco Taxation," report from American Embassy, London, UK-8034 21-V, March 1988.

⁴⁸² Don Nelson, Philip Morris, telephone conversation with USITC staff, May 31, 1990.

⁴⁸³ Don Nelson, Philip Morris Inc., telephone conversation with USITC staff, June 5, 1990. Slightly different dates are given in USDA, FAS, *Annual Tobacco Report*, U.S. Embassy, Lisbon, Apr. 30, 1990, p. 21.

⁴⁸⁴ "Health: Ministers Set to Adopt Tobacco Labelling Rules at November 13 Council," *European Report*, No. 1538 (Nov. 8, 1989), p. 6; "Minimum Tar Content - Cigarettes," *Eurobrief*, vol. 2, No. 6, Nov. 24, 1989, p. 70.

cigarette manufacturers alter the blends of tobacco used, U.S. light tobacco exports could get a boost, relative to dark leaf produced in Europe.⁴⁸⁵ The EC now is a major importer of light types of tobacco.⁴⁸⁶ Consumer preferences in Europe are already turning to American blend cigarettes, which contain a larger amount of light tobacco.⁴⁸⁷

U.S. brands of American blend cigarettes are produced in the EC by manufacturing subsidiaries of U.S. companies and by European firms under license arrangements. Only a small amount number of cigarettes are imported directly from the United States to the EC.

U.S. Government sources anticipate that rules on maximum tar content may be enacted for shag tobacco, which is used in "roll-your-own" cigarettes. U.S. dark fire-cured tobacco is a high-tar variety used in shag because of its rich quality, and could be affected by any new rules.⁴⁸⁸

Materials and Articles in Contact with Foodstuffs

As noted in the previous USITC report, the EC has proposed regulations that would limit the types of materials permitted to come in contact with foodstuffs. Only materials specifically approved by the EC could be used.⁴⁸⁹ The regulations are likely to have a major impact on the processed-food industry and on producers of packaging materials such as paper and ceramic ware. Directive 89/109, adopted on December 21, 1988, is part of the EC's comprehensive effort to ensure that its population is adequately safeguarded from substances that could endanger human health. This Framework directive will result in more explicit (vertical) directives, which will outline more specifics concerning materials and articles in contact with foodstuffs. The EC Scientific Committee for Food will formulate a list of substances that are "acceptable" for use in materials and articles in contact with foodstuffs. Regulated by this directive will primarily be materials and substances used in food and beverage packaging applications, food and beverage serving applications, or both types of applications. A number of industries could be affected by this directive, including pulp and paper, chemicals, plastics, glass, ceramics, metals and alloys, certain wooden products, and a host of other miscellaneous industries associated with food and beverage packaging and serving applications.

⁴⁸⁵ USDA, FAS, *Annual Tobacco Report*, May 1, 1990, pp. 8, 11, 26.

⁴⁸⁶ USDA, FAS, *Annual Tobacco Report*, Brussels, Belgium, Apr. 30, 1990, p. 10.

⁴⁸⁷ U.S. Department of Agriculture, Foreign Agricultural Service, annual tobacco reports from various countries, April-May 1990.

⁴⁸⁸ USDA, FAS, *Annual Tobacco Report*, The Hague, May 1, 1990, p. 8.

⁴⁸⁹ Art. 3.3(a) of the directive provides that future directives may include "a list of the substances the use of which is authorized to the exclusion of all others. (positive list)."

For products associated with this directive, West Germany generally leads Europe in production efficiency, as well as having the highest existing standards for materials and articles in contact with foodstuffs. Newly adopted EC-wide standards would more likely come up to the level of West Germany's existing standards rather than descend down to the level of other EC members. There is concern in industry circles that this directive has the potential to be trade discriminatory for certain U.S. exporters. If paper and paperboard food-packaging products that meet FDA requirements are not acceptable in the EC, then a trade barrier for U.S. exports could be created. Also, U.S. exports of commercial ceramic tableware to the EC could be restricted if the EC should adopt excessively strict lead-release standards. U.S. exporters of plastics, resins, and other synthetic or natural polymers or monomers are not likely to be adversely affected.

The U.S. International Trade Commission staff estimates that U.S. exports to the EC of the actual paper and paperboard food-packaging materials in question were valued between \$50 million and \$60 million during 1989. These U.S. exports are estimated to have increased at an average annual rate of slightly under 20 percent over the past 5 years. The Netherlands is estimated to have accounted for about three-quarters of U.S. exports of paper and paperboard food-packaging materials to the EC during this period. Nonetheless, many of the domestic pulp and paper companies exporting paper and paperboard food-packaging grades are also exporting other grades of pulp and paper to the European market.

Certain international pulp and paper suppliers, namely non-EC Nordic countries, may have the potential to increase their exports to the EC. U.S. pulp and paper exporters contend that these Nordic countries are members of the 15-nation European Paper Institute (EPI) and are consequently "in" the EC's decision loop when specifics concerning this directive are addressed, whereas they (the U.S. companies) are left "out" of this loop. Consequently, the Nordic countries are in a position to posture themselves for a market-share increase at the expense of U.S. exporters. Also, the European pulp and paper industries have generally been more specialized than their U.S. counterparts. Some industry sources believe that the likelihood of more restrictive vertical directives emanating from this directive will further encourage European "specialization" and further "disadvantage" the more integrated U.S. companies.

Also, certain suppliers of commercial ceramic tableware (e.g., firms in China, Mexico, and Italy) may well have difficulty meeting new, more stringent EC lead-release standards and may subsequently attempt to divert certain tableware exports to the United States.

Chemicals and Related Products

Overview

Previous USITC reports discussed the general thrust of EC work in the chemicals and related products area, provided some background on the process being employed to accomplish this work, and analyzed in detail directives on registration of plant-protection products and on the establishment of a European Environmental Agency and a European Environmental Monitoring and Information Network.⁴⁹⁰ These directives basically harmonize regulation and registration of fungicides, herbicides, plant-growth regulators, and other pesticide products throughout the European Community since currently there are no Communitywide procedures for pesticide registration and each member state determines the products used, concentration levels, and on which crops pesticides may be applied. The EC Environmental Agency was originally an experimental program to gather, coordinate, and ensure the consistency of information on the state of the environment and natural resources within the Community. Originally adopted for 4 years beginning on January 1, 1985, it was extended to 6 years and was modified to establish a European Environmental Agency (EEA) and a European Environmental Monitoring and Information Network. This report updates the status of the European Environmental Agency and network directives and presents an analysis of directives proposed during the first 6 months of 1990.

The U.S. chemical industry's principal concern is that if unable to participate in the process, EC attempts to streamline and harmonize national standards in this area will be discriminatory against non-European producers. Some also fear that the EC's plans to create a central environmental agency could have a detrimental impact on U.S. access to the European market. In addition, there is some concern that on EC's efforts to inform customers about pesticides and food additives may very well heighten fears and lower the chemical industry's sales.

For the chemicals and related products sector, a total of 11 directives were analyzed in this phase of the investigation. These directives deal with classification, packaging, labeling, marketing, and use of dangerous substances, as well as cosmetic products and methods of analysis. Other directives cover laboratory practice, human poisoning, and the European Environmental Agency and the European Environmental Information and Observation Network. Four directives were considered to be potentially of interest to U.S. industry. These directives include the regulation concerning the European Environmental Agency and the European

Environmental Network already discussed in the Legal, Institutional, and Policy Framework section of this chapter, and in this section, three directives on the classification, packaging, labeling, marketing, and use of certain dangerous substances and preparations.

Restrictions on the Marketing and Use of Certain Dangerous Substances and Preparations

Background

The EC proposed two directives pertaining to the marketing and use of dangerous chemical substances and preparations in the first 6 months of 1990—one restricting the use of cadmium in certain goods and another expected to speed the process of updating current EC directives to technical progress.

Anticipated Changes

Proposed Directive (89) 606⁴⁹¹ illustrates the desire of the EC Commission to adapt already-passed Framework directives on dangerous substances and preparations to technical progress. It would introduce a procedure that authorizes the EC Commission to make such decisions provided they conform to the opinion of a committee of technical experts. Specifically, the proposed directive on technical progress, in restricting the marketing and use of certain dangerous substances, would allow the EC Commission to adapt to technical progress the annexes to the Council directive on the approximation of the laws, regulations, and administrative provisions of the member states relating to restrictions on the marketing and use of certain dangerous substances and preparations.⁴⁹² The proposed directive would allow such adaptation when it conforms to the opinion of the Committee on the Adaptation to Technical Progress of the Directives on the Removal of Technical Barriers to Trade in the Sector of Dangerous Substances and Preparations. The original directive bans uses of the dangerous substances, polychlorinated biphenyl and polychlorinated terphenyl, other than the six uses listed in its annex, and bans the use of vinyl chloride monomer as an aerosol propellant. The EC Council has amended the original directive eight times.

Proposed Directive (89) 548⁴⁹³ on marketing and use of dangerous chemical substances and preparations results from the EC Council resolution of January 25, 1988,⁴⁹⁴ on measures to combat environmental pollution by cadmium. The EC program seeks (1) alternatives to the use of cadmium in pigments, stabilizers, and plating and (2) controls on cadmium content of phosphate fertilizers,

⁴⁹¹ OJ No. C 30 (Feb. 8, 1990), pp. 89-90.

⁴⁹² EC Council, OJ No. L 262 (Sept. 27, 1976), p. 201.

⁴⁹³ OJ No. C (Jan. 13, 1990), pp. 8-11.

⁴⁹⁴ EC Council, OJ No. C 30 (Feb. 4, 1988), p. 1.

⁴⁹⁰ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-65 to 6-70.

tobacco, food plants, and air and water pollution. Approximately 85 percent of the cadmium contained in pigments is used in plastics where the plastic encapsulates the pigment and provides protection unless the plastic product is incinerated.⁴⁹⁵

The proposed directive bans the use of cadmium and its compounds, in excess of 0.01 percent by weight, in polyvinyl chloride, polyurethane, low-density polyethylene, cellulose acetate, cellulose acetate butyrate, and epoxy resins. The ban would take effect in stages over 3 to 5 years, depending on product group. Currently, the EC itself does not restrict cadmium marketing and use, but certain member states do.⁴⁹⁶ Eventually, the disparate national laws restricting cadmium marketing and use would be superseded by this proposed directive.

Under the directive restricting the use of cadmium in certain compounds, producers of paints containing zinc would have 5 years to reduce cadmium content to 0.1 percent by weight. The ban would not apply to products colored for safety reasons. The producers of melamine-formaldehyde resins, urea-formaldehyde resins, unsaturated polyesters, polyethylene terephthalate, polybutylene terephthalate, transparent polystyrene, acrylonitrile methacrylate, cross-linked polyethylene, high-impact polystyrene, and polypropylene would also have 5 years to restrict use of cadmium compounds to 0.01 percent by weight.

Products that use a cadmium-containing stabilizer for safety reasons would be exempt from compliance with reduction of cadmium levels below 0.01 percent by weight for up to 3 years for certain products.⁴⁹⁷

The producers of equipment and machinery for the production of paper and paperboard, textiles and clothing, industrial handling, road and agricultural vehicles, rolling stock, and vessels have 5 years from the date of adoption of this proposal to eliminate cadmium-plated components, excepting certain safety-related applications. However, cadmium-plated components may not be used in products related to food production, agriculture, cooling and freezing, printing and book-binding, household goods, furniture, sanitary ware, or central heating or air conditioning. Electrical contacts may contain cadmium if necessary for their reliability.

This proposal would go into effect no later than June 30, 1991. The member states must inform the

⁴⁹⁵ R.F. Lynch, *Plastics Engineering*, April 1985, p. 55.

⁴⁹⁶ Eighth clause to the Preamble to Com (89) 548, Nov. 22, 1989, p. 1.

⁴⁹⁷ Including packaging materials, office or school supplies, fittings for furniture or coachwork, apparel, floor or wall coverings, treated textile fabrics, imitation leather, phonograph records, tubes and pipes, swing doors, vehicles, steel sheet coatings, and electrical insulation.

EC Commission of the text of these laws no later than December 31, 1990. Further, the EC Commission shall draw up a report on substitutes for cadmium so the EC Council can reassess the situation within 7 years of the adoption of this proposal.

Possible Effects

U.S. exports to the EC

U.S. industry serves the EC primarily through direct exports of chemicals covered in the proposed. It is not immediately clear how these proposals will affect such U.S. exports in the long run. In 1989, U.S. exports to the EC of the cadmium-containing compounds, including inorganic pigments, unwrought cadmium, and cadmium sulfide were approximately 173,000 kilograms, valued at about \$357 million.⁴⁹⁸ Cadmium is also incorporated into other products for which export statistics are not available.

U.S. industry is not likely to be affected significantly by the proposed directive on technical progress because it would apply to products already subject to restrictions in the EC and the United States. U.S. exports of chemicals in schedule B provisions subject to this directive amounted to 46.2 million kilograms, valued at \$73.3 million, in 1989.⁴⁹⁹

Diversion of trade to the U.S. market

The directive on cadmium directly affects the relative competitiveness of EC-based companies and third-country suppliers, but ongoing efforts to make a smooth transition to alternative products should reduce any possible diversion to the U.S. market. Adoption of the directive on technical progress is unlikely to affect relative competitiveness. For this directive, the leading EC competitors are Royal Dutch Shell Corp., Imperial Chemical Industries Ltd., and the French company, Total. The leading non-EC competitors are companies based in Hungary, the Soviet Union, and Algeria.

U.S. investment and operating conditions in the EC

Implementation of the directive restricting cadmium will most likely have little effect on existing U.S. investment in the EC. U.S. multinationals are accustomed to altering products to satisfy the laws and preferences of host countries.

U.S. investors are unlikely to change their investment plans or EC-based production strategies as a result of the proposed directive on technical progress because the second amendment of the Council directive relating to restrictions on the

⁴⁹⁸ Compiled from official statistics of the U.S. Department of Commerce.

⁴⁹⁹ Compiled from official statistics of the U.S. Department of Commerce.

marketing and use of certain dangerous substances and preparations was effective January 12, 1983.⁵⁰⁰ Authorizing the EC Commission to further adapt this directive, 76/769, to technical progress in the sector of dangerous substances and preparations should not cause U.S. investors to change EC-based production strategies.

U.S. Industry Response

A Cadmium Council, Inc., spokesperson stated that the approach to protection from cadmium in the EC is fairer, broader, and more helpful in transition away from nonessential uses than the approach used in the United States. Unlike the EC proposal discussed above, U.S. restrictions on cadmium and its compounds are media specific. The U.S. Occupational Safety and Health Administration (OSHA) has established permissible exposure limits (PEL) for U.S. workers concerning certain products containing cadmium⁵⁰¹ and the U.S. Environmental Protection Agency has set standards for certain other cadmium-containing substances.⁵⁰² OSHA proposes to lower the PELs for cadmium dust and cadmium fume to the lowest level in the World.⁵⁰³ The European countries currently have divergent exposure-limit values for cadmium. None of the EC countries currently regulates cadmium contained in products offered for sale, possibly due to Sweden's reduction in regulations after a ban on contained cadmium was unenforceable. According to this spokesperson, the EC is expected to allow 4 to 20 times the proposed U.S. PELs based on Sweden's experience. Adoption of the OSHA proposed PELs would be a severe action that he believes would be overturned or there would no longer be a viable U.S. cadmium industry.⁵⁰⁴ Submissions from certain individual member companies support the Cadmium Council position.

There are no expressed U.S. industry concerns with the proposed directive on technical progress in the marketing and use of certain dangerous substances, which was adopted in Council Directive 89/678.⁵⁰⁵

Classification, Packaging, and Labeling of Dangerous Substances

Background

Proposed Directive (89)575⁵⁰⁶ (hereinafter the Seventh Amendment) would amend Directive 67/548 on the approximation of the laws relating to the classification, packaging, and labeling of dangerous substances. The Seventh Amendment

⁵⁰⁰ Council Directive 82/806, OJ No. L 339 (Dec. 1, 1982), p. 55.

⁵⁰¹ 29 CFR 1910.1000, table Z-1-A.

⁵⁰² 40 CFR, subchapter IN.

⁵⁰³ 55 FR 4052 4147 (Feb. 6, 1990).

⁵⁰⁴ Cadmium Council, Inc., Letter dated July 5, 1990.

⁵⁰⁵ EC Council, OJ No. L 398 (Dec. 30, 1989), p. 24.

⁵⁰⁶ OJ No. C 33 (Feb. 13, 1990), pp. 3-26.

would harmonize the member-state laws on the exchange of information on notified substances and on the assessment of the potential risk to man or the environment of the notified substances.

Anticipated Changes

The Seventh Amendment expands the scope of existing EC regulations by establishing a new classification of dangerous substances called "sensitizing" substances, those that may produce an adverse reaction of the immune system. Laboratory tests would be required on these sensitizing substances before they may be legally marketed in the EC or approved for use by EC member-state environmental authorities. Such tests would have to be in compliance with existing directives on laboratory practice and protection of animals used for experimental purposes.⁵⁰⁷

The Seventh Amendment would require non-EC manufacturers to appoint a sole EC representative. EC notification procedures require only the identity, production, and uses of substances previously submitted for approval for use in plant protection or animal feedstuffs. Substances may not be marketed earlier than 60 days after the date of notification or acknowledgement by member-state environmental authorities of conformity with the directive.

Notification requirements are reduced for products with sales of less than 1 metric ton per year per manufacturer. For smaller quantities intended for use in research, written records would be required of the identity of the substance, labeling data, quantities, and customers. Products for process-oriented research and development would need to be qualified for an exemption from notification of 1 year, which may be extended for a further year in exceptional circumstances. For sales of 100 to 500 metric tons per year per manufacturer (level 1), mutagenesis studies, and basic toxicokinetic information are required. For sales of 1,000 to 5,000 metric tons per year per manufacturer (level 2), toxicity studies will be required.

In addition to the required testing, substance labels would be required to show an EEC identification number and other information. Labels of substances classified as dangerous would include the words "approved EC label in accordance with Directive 67/548/EEC." Minimum label dimensions would increase according to package size. At or before the first delivery of a dangerous substance, the sender would communicate to the recipient the information necessary for protection of man and the environment. The EC Commission also proposes a symbol meaning "dangerous for the environment" and proposes lowering threshold definitions of "very toxic" and "toxic."

In passing the Seventh Amendment, the EC Council would authorize the EC Commission to

⁵⁰⁷ EC Council, OJ No. L 15 (Jan. 17, 1987), p. 29; EC Council, OJ No. L 358 (Dec. 18, 1986), p. 1.

amend the general classification and labeling, technical dossier information, and test information requirements to conform with opinions of the Committee on the Adaptation to Technical Progress of the Directives on the Removal of Technical Barriers to Trade in the Sector of Dangerous Substances and Preparations. Every 3 years, member states would forward a report on the implementation of this directive in their respective countries to the EC Commission. The EC Commission would then issue a composite report.

Possible Effects

Under the Seventh Amendment, information compiled for the EPA would be resubmitted to the EC. U.S. industry serves the EC both through direct investments in the EC and direct exports from the United States. The most significant effects would be on manufacturers of dangerous substances with U.S. production less than 1,000 pounds and EC sales greater than 100 kilograms because the EPA would grant an exemption and the member state of importation could require substantial information for conforming to the reduced notification requirements. Substances that had not been placed on the EC market prior to September 18, 1981, but were included in the U.S. Toxic Substances Control Act Chemical Substance Inventory would be subject to significant testing prior to being placed on the EC market in quantities of at least 100 kilograms per year per manufacturer.

U.S. exports to the EC

The Seventh Amendment has the potential to be trade inhibiting due to the costs involved with compliance testing and information requirements. U.S. exports of potentially affected products, such as reaction initiators, reaction accelerators, catalytic preparations, and composite diagnostic or laboratory reagents, amounted to 15,273 metric tons, valued at almost \$270 million, in 1989.⁵⁰⁸ This is approximately one-third of total U.S. exports of these products. Approximately 5,000 metric tons of these products, valued at \$81.8 million in 1989, were placed on the EC market after the December 31, 1981, proposal cutoff date.⁵⁰⁹

Diversion of trade to the U.S. Market

The Seventh Amendment is not likely to affect relative competitiveness or result in diversion to the U.S. market, because the EPA established similar requirements under the Toxic Substances Control Act but with a higher action level before notification review than is proposed for the EC.

⁵⁰⁸ Compiled from official statistics of the U.S. Department of Commerce.

⁵⁰⁹ Compiled from official statistics of the U.S. Department of Commerce.

U.S. Investment and operating conditions in the EC

U.S. investors may change their investment plans or EC-based production strategies as a result of this directive because the cost of performing toxicological studies has to be considered in investment plans, although many products are exempted if placed on the EC market prior to 1981.

U.S. Industry Response

The Chemical Manufacturers Association is concerned about uniformity in regulating dangerous substances. The amount of time and effort that must be expended to comply with regulations is significant; therefore, member companies are pressing government to increase uniformity in the application of specific regulations.

Pharmaceuticals

Background

The general direction of EC work in the pharmaceuticals area, some background on the process being employed to accomplish it, and an analysis of the effect of certain conditions in the pharmaceutical industry were discussed in the last USITC report.⁵¹⁰ The report covered in detail the Transparency Directive and its effect on continuing national pricing/reimbursement systems, the proposed directives on the creation of the single-market authorization procedure and patent-term restoration, and the recent implementation of new guidelines on the granting of duty suspensions on certain EC imports.⁵¹¹ This report updates the status of the above issues.

As noted in the previous report, the overall reaction of the U.S. pharmaceutical industry appears to be positive towards many of the changes associated with the 1992 program.⁵¹² The U.S. industry, through an industry association, has been actively involved in the directive-drafting process at many levels. The industry says its opinion has been sought during the process, particularly with regard to the creation of the single-market authorization procedure, and that the EC Commission has already addressed a number of its concerns.⁵¹³ Much of this participation in and access to the process is the result of the relatively high level of investment by the U.S. industry in the

⁵¹⁰ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-70 to 6-84.

⁵¹¹ At the time the previous report was written, directives were expected to be proposed on both the creation of a single market authorization procedure and patent-term restoration. A regulation rather than a directive, however, has since been proposed that will address the patent-term restoration issue; the authorization procedure is expected to be addressed through a regulation and three directives. A regulation has force of law within all member states.

⁵¹² USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-7 to 6-9.

⁵¹³ According to Mr. Harvey E. Bale, Jr., Ph.D., Senior Vice President, International Pharmaceutical Manufacturers Association, written submission to the USITC, dated July 6, 1990 (Bale submission).

EC. Many European subsidiaries of U.S. pharmaceutical companies are reportedly viewed as European companies. U.S. firms currently account for about 27 percent of the EC pharmaceuticals market.

Four issues that were identified in the last USITC report as being of particular concern to the industry, however, are⁵¹⁴ (1) the creation of a single-market authorization procedure; (2) the continued existence of national pricing/reimbursement systems; (3) patent-term restoration; and (4) the recent EC-wide implementation of duty-suspension guidelines that are perceived by industry as being more restrictive.

Update

Since issuance of the last report, a number of fundamentals have been hammered out in regard to these issues, even though, in the first three cases, no directives had yet been formally proposed by press time. For the most part, the approach to these issues has remained the same. Some aspects have, however, been amended and these changes are discussed below. Several other developments in 1990 were noteworthy. The EC Commission has recently adopted three directives concerning the use of medicines. The first of these directives concerns the safety of the drug-distribution circuit and aims to secure the safest possible conditions for these products in their journey from factory gate to patient. The second directive pertains to the access of medicines and harmonizes conditions of supply so that there will be a greater degree of consistency between those drugs that will be sold over the counter and those that will only be available with a medical prescription. The third of these directives, involving information given on the package insert, is to ensure the proper use of the drug.⁵¹⁵

Single-Market Authorization Procedure

Industry sources expect that the directive on the creation of the single-market authorization procedure would be formally proposed in the final quarter of 1990. The draft proposal analyzed herein consists of one regulation and three directives. This structure allows for the immediate adoption of new Community procedures for the authorization and supervision of medicinal products for human and veterinary use and the creation of the European Agency for the Evaluation of Medicinal Products to review the safety of medicines. This central agency, soon to be established, will be responsible for handling requests made by drug companies to sell new products in member states. The creation of this agency will most likely reduce long registration periods and save industry the effort of applying

⁵¹⁴ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-70 to 6-84.

⁵¹⁵ "The EC Pharmaceutical Market - Obstacles to a Single Market for the Free Movement of Medicines," *EC-U.S. Business Reports*, vol. 2, No. 4, Apr. 1, 1990, pp. 15-16.

through each member-state government to get necessary approval.⁵¹⁶ The structure also provides for the replacement of the current multistate approval system with the decentralized system for both human and veterinary products and for the repeal of a past directive that called for the approximation of national measures relating to the placing on the market of high-technology medicinal products, particularly those derived from biotechnology (known as the "concertation" procedure). For the most part, the contents of the current draft are said to be similar to that discussed in the last report. However, one significant change that is of concern to the industry is a provision that would allow for the elimination of the national approval systems for access by companies on a Europe-wide basis by 1996. The U.S. industry currently uses these systems fairly extensively.

The industry suggests that while the new system is being implemented, a transition period should be in effect to allow the industry to retain access to the existing national approval route. The new system is expected to take some time to implement and, because of the scope of the changes instituted by the new authorization procedures, could experience temporary bottlenecks. Access to the national routes until 1996 would allow for an "escape valve" for the industry.⁵¹⁷ At that time, the systems and their use could be reviewed and modified appropriately.

Advertising

The industry has also been watching developments in a directive regarding the advertising of pharmaceutical products in the EC. The directive was formally proposed on June 6, 1990. In the United States, advertising of prescription products is allowed, but regulated by the FDA so that consumer interests are protected. The EC Commission is currently looking at providing separate rules for advertising to the general public and to health professionals. According to information provided recently by the EC Commission, advertisements to the public would be limited to "self-medication" products, subject to certain conditions. Advertising to health professionals would be subject to a more complex set of rules that would concern, among other things, medical sales representatives, financial inducements, and the distribution of free samples. According to the EC information, the monitoring of such advertising, whether to the public or to health care professionals, is expected to be provided for.

Medical Equipment

Background

The previous report discussed the basic thrust of EC efforts to harmonize regulations and

⁵¹⁶ "Agency for Safety of Medicines," *Europe 92*, vol. 1, issue 7.

⁵¹⁷ Bale submission.

conformity-assessment procedures for medical equipment, and analyzed directives on active implantable electromedical devices, active nonimplantable electromedical devices, nonpowered sterile devices (including nonactive implants), and in vitro diagnostics (tests made outside the body).⁵¹⁸ This report updates the status of those directives. Regulatory harmonization in this area, unlike that in the sectors discussed in the immediately preceding sections, is being conducted under the "new approach." Thus, voluntary standards developed by CEN/CENELEC and the EC's policy towards testing and certification will be a major factor in assessing the impact of these measures on U.S. suppliers. U.S. makers of medical equipment generally expect to gain as a result of European harmonization, but EC acceptance of U.S. test data still remains a key industry objective.

Update

The directive on active implantable electromedical devices (pacemakers and similar devices)⁵¹⁹ was approved by the EC Parliament on May 16, 1990. The only significant change in the directive before it was approved was a clarification to make it more explicit that the directive would have jurisdiction over the problem of electromagnetic compatibility (EMC) in medical equipment. This clarification effectively exempts medical equipment from possible overlapping coverage under a proposed EC directive (89/336) on EMC that covers other products such as computers, radios, televisions, lights, and other electronic and electrical equipment that emits (or is affected by) electromagnetic interference. The clarification was made in response to concerns by U.S. medical manufacturers that imprecise language in the original draft could result in increased regulatory compliance costs, including possible design-change requirements for U.S. producers.⁵²⁰ Several other less significant technical modifications and changes in language were made to the original draft on active implantable electromedical devices before it was passed by the European Parliament and approved by the EC Council.

In July 1990, there were reports that the EC Commission had decided to combine the proposed directives on active nonimplantable and nonactive sterile devices into a single directive and had ordered the officials responsible for drafting the medical device directives to issue a working draft by early August.⁵²¹ Industry officials do not believe a

⁵¹⁸ See USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, pp. 6-7 and 6-17; and USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-71, 6-72, and 6-81 through 6-84.

⁵¹⁹ Com (88) 717 final, OJ No. C 14 (Jan. 18, 1989), p. 4.

⁵²⁰ Officials of the Health Industry Manufacturers Association, telephone conversations with USITC staff, May 21, 1990, and National Electrical Manufacturers Association, telephone conversations with USITC staff, May 21 and June 24, 1990.

⁵²¹ USITC telephone conversations with officials of the National Electrical Manufacturers Association and the U.S. Food and Drug Administration (Office of Standards and Regulations) on July 24, 1990.

final directive for such devices will be published in the *Official Journal* before the beginning or middle of 1991. Little work is expected on the proposed directive on in vitro medical devices until completion of this directive.

Because the directives will rely largely on EC standards (CEN/CENELEC) to achieve their objectives, there has been much interest by U.S. manufacturers and standards groups in international and EC standards-setting activities related to medical equipment. The U.S. Association for the Advancement of Medical Instrumentation (AAMI) scored a major victory in the international standards arena when it assumed a leadership role in international standards development for electromedical devices and safety, sterilization technologies, cardiovascular implant devices, and biocompatibility and toxicity testing devices. ANSI named AAMI administrative secretariat for a new international technical committee on medical device sterilization as well as administrator of the new U.S. Technical Advisory Group for an ISO committee on biological evaluation.⁵²²

U.S. industry officials indicated that AAMI's new role in international standards activities should increase the U.S. medical industry's influence on EC standards development. They expressed concern, however, that the EC Commission may be placing too much emphasis on developing new EC standards for medical devices through CEN/CENELEC when similar work is being done in international standards bodies such as the ISO.⁵²³ Separate EC standards could serve as a barrier to trade for U.S. and other non-EC companies producing medical equipment to international standards. Officials of the U.S. Food and Drug Administration, the Federal agency responsible for regulation and approval of medical devices in the United States, were also concerned since the FDA has been advising U.S. medical firms and their related voluntary standards committees to move toward international standards as a means of harmonizing medical regulatory approval processes throughout the world.

On July 26, 1990, several FDA officials met with EC Commission officials (DG IIIB) in Brussels to express their concern that it seemed that CEN/CENELEC was moving out in front of ISO standards committees in drafting new EC standards that would affect medical equipment.⁵²⁴ The FDA believes that CEN/CENELEC officials should work with and through the ISO since two ISO standards (ISO 9000 and ISO 601-1) related to good manufacturing practices (GMP) and horizontal

⁵²² Gary M. Stephenson, "International Standards: Harmonizing to a European Tune," *Medical Device and Diagnostic Industry*, June 1990, p. 98.

⁵²³ Official of the National Electrical Manufacturers Association, telephone conversation with USITC staff, June 24, 1990.

⁵²⁴ Official of the U.S. Food and Drug Administration, telephone conversation with USITC staff, on July 24, 1990.

standards are directly related to the current standards activities of CEN/CENELEC. The FDA officials left the meeting satisfied that the EC Commission would urge CEN/CENELEC to cooperate more closely with ISO officials in drafting new standards related to the medical industry.⁵²⁵

There has also been some discussion of the possibility of future memorandums of understanding (MOUs) between the FDA and the EC that would allow for mutual recognition of testing and certification activities. Currently, the FDA has an agreement with the British Department of Health and Social Security for the mutual recognition of inspections of manufacturers of medical devices. That is the only country with which the FDA has thus far established an MOU for the exchange of medical device inspection data.⁵²⁶ The FDA is presently negotiating with the United Kingdom to iron out differences and difficulties with the present MOU. Although FDA officials believe that an MOU between the FDA and EC is a future possibility, much work remains before such an agreement could be negotiated.⁵²⁷

The FDA has agreed to continue to meet regularly with EC Commission officials involved in medical device regulatory and standards activities to exchange information and to work in parallel directions with respect to new rules concerning the regulation and approval of medical devices.⁵²⁸

Automobiles

Background

Previous USITC reports discussed the general thrust of EC work in the automobile industry, provided some background on the process being employed to accomplish it, and analyzed in detail directives on certification, emissions, motor-vehicle parts, roadworthiness, weights and dimensions, and use of leaded and unleaded fuel.⁵²⁹ These directives basically harmonize a wide range of vehicle standards and are part of an overall effort to achieve type-approval of cars. Type-approval of cars would reduce costs, administrative burdens, and duplicative testing requirements, and allow for economies of production, engineering, and styling. U.S. suppliers have been generally supportive of this process, although they have expressed reservations about EC test procedures. Ideally, U.S. manufacturers would like the option of self-certifying conformity to EC regulations, the standard operating procedure in the United States.

⁵²⁵ Ibid.

⁵²⁶ FDA officials indicate that in order to establish an MOU, the countries involved must have comparable GMPs and inspection programs and that to date, the United Kingdom is the only country with a program comparable to the FDA program. Ibid.

⁵²⁷ Ibid.

⁵²⁸ Ibid.

⁵²⁹ USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, pp. 11-9 to 11-12, and pp. C-4 to C-7; USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-84 to 6-89.

During the period under review, the EC Commission introduced the three remaining directives on automobiles regarding weights and dimensions, safety glazing for windshields, and tires for motor vehicles. Final adoption of the directives would make it possible for suppliers to obtain "whole type approval," a one-stop process that once completed, would allow all vehicles of the same make and model to be placed on the EC market without further tests and inspections. Final passage of the directives is not expected until the EC resolves the question of voluntary restraints on Japanese cars. In a conference with the USITC, one of the largest U.S. investors in the EC auto industry stated that the directive on weights and dimensions would pose no problem for them, but that there were now two differing standards in the United States and EC on glazing of windshields. They were unable to comment on the tires directive, because they were unsure how the EC would apply this directive.⁵³⁰ The EC Commission has also sought to extend the strict emissions requirement already proposed for smaller cars to larger cars.

Of the directives proposed, the directive on emissions has emerged as the one of most interest to U.S. industry. The specifics of EC-wide emissions legislation were spelled out in a 1970 directive (70/220). Since the 1970 core directive, there have been seven additional directives and numerous proposals passed by the EC Commission to amend the original. The most recent such proposal is Com (89) 662 final, which aims to extend the shorter compliance cycle and stricter emission standards to include larger vehicles, with an engine size of 1.4 liters or more. This proposal essentially covers the entire EC vehicle population up to 2.5 tons of gross vehicle weight, regardless of engine size.

The overall impact of EC emission standards on the U.S. auto industry continues to be positive. These more stringent emission-control requirements closely resemble emission standards already in force in the United States. Although U.S. suppliers are generally supportive of the new EC emission standards, some have voiced concerns with regard to testing and certification requirements.⁵³¹ The U.S. Federal Test Procedure (FTP) uses a test protocol developed by the Environmental Protection Agency. The EPA test protocol incorporates all of the items being proposed by the EC: low emission limits for new vehicle certification and the evaporative emission test and limits specified therein. Furthermore, the EC limits for hydrocarbons (HC), carbon monoxide (CO), and oxides of nitrogen (NO_x) were developed using vehicles designed to meet U.S. EPA standards.

⁵³⁰ Meeting with USITC staff, Detroit, MI, May 11, 1990.

⁵³¹ As stated in a Mar. 30, 1990, communique by the Motor Vehicle Manufacturers Association of the United States, Inc.

For the aforementioned reasons, representatives of U.S. industry recommend that the U.S. EPA test cycle continue to be allowed as an alternative to the EC cycle. The same representatives also call for an integrated test cycle, i.e., combining the EC-wide present urban driving cycle (UDC) and the proposed extra urban driving cycle (EUDC). Such integration would reduce testing complexity. U.S. industry representatives unequivocally state that the EC-proposed new emission limits cannot be more stringent than current U.S. requirements, primarily because of technological limitations. EC laws currently permit the acceptance of U.S. emission certificates only for a transitional period. Motor Vehicle Manufacturers Association (MVMA) and other U.S. industry sources conclude that continued acceptance of emission certificates based on current U.S. emission limits and test procedure requirements is highly desirable as an alternative to the newly commissioned EC cycle. The U.S. motor-vehicle and parts industries have major interest in having such an alternative approved by the EC.

Other Machinery

Small and medium-sized firms that export to the EC (accounting for nearly 80 percent of machine sales) are most likely to be directly affected by the directives analyzed in previous USITC reports — mobile and lifting machinery, agricultural and forestry tractors, machinery-safety, simple pressure vessels, lawn mowers, and household electrical appliances. These directives could conceivably serve to harmonize divergent machinery standards; however, some U.S. producers worry that they could also be used to limit their exports of these products to the EC. Numerous U.S. firms that export to the EC do not maintain a production facility in Europe, and instead have opted to work through an established EC-based distribution network. U.S. producers continue to assert that they are at a competitive disadvantage with respect to their European counterparts because of a lack of timely information regarding technical standards, often not being able to view these standards until they are in final draft form — which is often 6 months or more after their EC counterparts. During the first 6 months of 1990, attention appeared to shift from the contents of directives themselves to issues associated with product liability, testing and certification, and the standards being drafted by CEN/CENELEC.

Because of the scope of machinery affected (nearly 55,000 types of machines will eventually be covered), the machine safety directive is likely to have the greatest impact on U.S. exporters.⁵³² Primary issues of concern include the prospect of increased product-liability exposure as a result of this directive. Specifically mentioned was the

implementation of requirement 1.1.2(c) of annex 1, which states that "machinery must be designed to prevent abnormal use if such a device will result in a safety risk." A large producer of industrial forklift trucks indicated that his firm could not begin to envision all the possible "abnormal" uses that could result from operation of his machinery.⁵³³ Other machine safety directive concerns significant to U.S. exporters of machine tools include clarification of what is meant by certain phrases such as one that requires manufacturers to employ "user friendly software" in their machinery. Various producers indicated that they might have to redesign some of their machinery to comply with this particular requirement.

Additional concerns of U.S. exporters of machinery involve testing and certification issues. Nearly all medium- and small-sized firms that produce heavy machinery indicated particular difficulty concerning third-party inspection. According to these producers, it would be excessively costly and physically impossible to ship large, heavy equipment (machine tools or industrial forklift trucks) to designated testing and certification laboratories in the EC unless these facilities were equipped with special hoists and heavy-duty foundations on which to place this equipment. To alleviate these potential problems, all U.S. exporters of machinery indicated that in order to maintain current U.S. export levels it was necessary for the EC to allow U.S. laboratories to certify their products.⁵³⁴

Furthermore, several producers of machine tools expressed concern about the extent of the certification process that might emerge. According to these producers, a diverse group of machine tools that are exported by U.S. suppliers may be considered to be custom-finished machinery (e.g., plastic injection equipment) that is manufactured in very limited quantities. These producers have to frequently manufacture products in accordance with the buyer's individual technical requirements, not standards per se. These industry sources questioned whether or not each custom-finished product would have to endure third-party certification, even if each machine required only minor changes from previously approved machines. This lack of certainty is a major factor in long-term business planning for nearly all firms surveyed. Determining the total cost of the testing and certification process for this equipment would enable U.S. producers to determine the competitiveness of their machinery in a highly price-sensitive market. Finally, some U.S. producers claimed that the costs and time associated with testing and certification may have a chilling effect on the incorporation of subsequent technical advances in their machines.⁵³⁵

⁵³³ Taylor Machine Works, interview by USITC staff, June 25, 1990.

⁵³⁴ The Association for Manufacturing Technology, meetings with USITC staff, June 28, 1990.

⁵³⁵ Cincinnati Milacron Corp., meetings with USITC staff, May 25, 1990.

⁵³² USITC staff meetings with CEN officials, Brussels, Belgium, Jan. 8, 1990.

The recent establishment of a European Organization of Testing and Certification (EOTC) should facilitate mutual recognition of testing results throughout the EC, U.S. machinery interests believe. According to these sources, broad product sectors such as machine tools for the aerospace, automotive, construction, and plastic machinery sectors may be covered by the organization's sectoral committees or agreements groups.⁵³⁶ Exporters of machine tools are anxious to know how individual machine tool sectors will be classified by EOTC, so they may set up appropriate mechanisms to interface with their European counterparts.⁵³⁷

Additional issues of concern to exporters of machinery to the EC include the implementation of ISO 9000 quality assurance standards. These exporters indicate that implementation of these standards may require third-party assessment of each firm's quality-control procedures. Conformity to this distinctive standard will require that a team of assessors visit a production facility to verify production processes and product design and to ensure that an updated quality-control manual be maintained at each individual production facility. As noted in the section on "testing and certification" above, the EC has not agreed to allow U.S. organizations to perform required quality assessments. According to various producers of machinery, any such program should also consider the cost of ensuring quality as well as the cost of nonquality criteria (e.g., machining/finishing both sides of a machine when only one is exposed after assembly).⁵³⁸

Currently, there are only a small number of U.S. laboratories that would be willing to certify a production process as a result of prevailing U.S. product-liability laws. Conforming to these quality standards may be a potential obstacle to these producers since there are no such existing requirements on U.S. producers. U.S. regulation focuses on employer responsibility for workplace safety; with few exceptions, it does not specifically regulate the safety of the machines themselves.

Although the United States continues to inch towards the use of metric measurements, the economic integration in the EC has apparently been beneficial in compelling U.S. exporters to begin producing a limited amount of metric-designed machinery. However, various industry sources indicate that a more rapid and widespread transition to metric measurements is critical if U.S. exporters are to gain an increasing share of the EC market.⁵³⁹ Nearly all firms interviewed in various industry sectors (e.g., air-conditioning and printing

equipment) agreed that world trade is increasingly geared to the metric system of measurement. Virtually all firms indicated that they are often at a competitive disadvantage in the global marketplace because of not conforming to this standard measurement system. Spokesmen for some of these exporting firms indicated that they have at times been excluded from some potential contracts when they were unable to deliver products measured in metric dimensions (i.e., motors and hydraulic valves). Industry sources estimate that, on average, the cost of shifting production to metric specifications will increase a firm's cost by approximately 3 to 10 percent. Nearly all of the firms cite the cost of retooling and training workers as the primary reason for delaying conversion to the metric system.⁵⁴⁰ Furthermore, a few major purchasers, such as automobile and aerospace companies, continue to decline implementation of metric measurements in their production processes (i.e., steel) or to purchase metric-designed machinery or components. The decision by these large customers not to require small and medium-sized firms to make greater use of metric products was also cited as a deterrent to wider utilization of metrication.

Several leading associations including NMTBA/The Association for Manufacturing Technology indicated that they have implemented metric standards programs to promote greater use of metrication. In addition, a few of these associations are encouraging greater participation by small and medium-sized firms in international standards activities. Organizations such as the National Electrical Manufacturers Association (NEMA) report that some parts of their associations currently fund U.S. delegates to international meetings and also support technical advisory groups to the International Standards Organization (ISO). Because of the expense and time involved in attending ISO committee meetings worldwide, several industry sources have recommended that the U.S. Government be more involved in assisting small and medium-sized exporters in joining ISO technical committees to help promote greater use of ISO technical standards.⁵⁴¹

In conclusion, all U.S. exporters of machinery to the EC agreed that harmonization of technical product standards of the 12 member countries would result in long-term export benefits for their firms. Nearly all small and medium-sized firms surveyed indicated that they will continue to serve the EC primarily by exporting. Several industry sources cited the high cost of social overhead expenses that can total up to nearly half of an annual salary in nations such as France and West Germany as the primary reason for continuing to rely primarily on exports rather than EC-based production.

⁵³⁶ EC Commission officials, meetings with USITC staff, July 20, 1990.

⁵³⁷ The Association for Manufacturing Technology, meetings with USITC staff, June 28, 1990.

⁵³⁸ "U.S. Manufacturers Quality Control Program Vital to Entering New European Market," *Air Conditioning, Heating & Refrigeration News*, May 28, 1990.

⁵³⁹ Hitachi Seiki USA, Inc., field interview by USITC staff, June 5, 1990.

⁵⁴⁰ The Association for Manufacturing Technology, meeting with USITC staff, June 14, 1990.

⁵⁴¹ Cincinnati Milacron, field interview by USITC staff, May 25, 1990.

The majority of firms interviewed indicated that they did not anticipate being hindered in exporting their products to the EC as a result of the machine safety, mobile and lifting machinery, and agricultural and forestry tractor products directives. These same firms indicated that, because of their lack of economic resources and manpower, they will continue to rely on their respective trade associations and the U.S. Government for timely information regarding technical product standards. A few leading industry associations, such as the Association for Manufacturing Technology, have reported limited success in influencing CEN technical committees in transferring certain types of standards for nonelectrical machinery such as machine tools to ISO. However, they point out that ISO has not traditionally been active in the development of machinery safety standards as a result of differences in national regulations among ISO members. U.S. exporters' participation in ISO standards development will be essential if they are to gain an increasing share of a highly competitive EC market for machinery.

Telecommunications

Background

The telecommunications sector is one of the keys to the successful integration of the EC member states, and the establishment of common standards, testing requirements, and operating conditions is a key element of the EC's 1992 strategy. In particular, such harmonization is necessary if the benefits of liberalization of telecommunications services and expanded competition and choice in telecommunications equipment are to be realized. Many of these standards are voluntary and are being developed by the European Telecommunications Standards Institute (ETSI). It is expected, however, that some such standards and most testing and approval requirements will be made mandatory by EC directives and regulations. In previous reports the U.S. International Trade Commission has examined the EC's proposals on open network provision, telecommunications terminal equipment, electromagnetic compatibility, and television broadcasting. This section will provide an update on the changes to such directives as well as an analysis of the EC proposals affecting cellular telephones and pagers.

One issue not examined here bears watching in the future. The EC Commission is expected to issue a paper on satellite communications policy in 1990. The policy paper will discuss the use of satellites in telecommunications networks and in relation to direct-broadcast television.

Update

Telecommunications Terminal Equipment

Proposed Directive Com (89) 289 would require that telecommunications terminal equipment meet

certain essential requirements before it could be placed on the market, but once a piece of terminal equipment is certified by one member state, it could then be marketed throughout the Community without having to be certified in all 12 member states.⁵⁴²

The European Parliament described the proposed directive on type-approval for telecommunications terminal equipment as "too vague" at its April 1990 plenary session. The Parliament supported the initiative but voted for a number of amendments designed to clarify the wording of the text.⁵⁴³ In particular, the Parliament called for a clarification of the definition of a "telecommunications terminal" and of the requirement, in "justified cases," for the interworking of the equipment.⁵⁴⁴ The International Chamber of Commerce (ICC) also criticized the wide definition of terminals and the definition of "interworking" contained in the proposal. The ICC went on to say that the proposed directive would actually raise costs and make the system more costly for industrialists while protecting the monopolistic control of national PTTs.⁵⁴⁵

Electromagnetic Compatibility

The EMC directive ((89) 336) defines essential protection requirements for equipment that may cause or be affected by electromagnetic disturbances.⁵⁴⁶

In the area of telecommunications equipment, the EMC directive would be the first directive to require third-party testing and, as a result, could harm U.S. laboratories, according to Charles Ludolph, director of the Commerce Department's Office of European Community Affairs. Mr. Walter Poggi of Retlif Testing said he would not be able to send test data to Europe after December 1990. Both gentlemen were testifying at a hearing before the Small Business Export, Tax Policy and Special Problems Subcommittee on April 30, 1990.⁵⁴⁷

Open Network Provision

The open network provision (ONP) directive ((89) 325) lays down conditions of access to the telecommunications network that telecommunications authorities are to follow when giving competitive telecommunication-service providers access to the network. The ONP conditions are

⁵⁴² See "Telecommunications Terminal Equipment," in the previous report. USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-107 to 6-109.

⁵⁴³ *European Report* (Apr. 7, 1990), Internal Market p. 9.

⁵⁴⁴ *EC Business Report*, May 1, 1990, p. 11.

⁵⁴⁵ *European Report*, Business Brief, May 16, 1990, p. 4.

⁵⁴⁶ See "Electromagnetic Compatibility," in the previous report. USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-109 to 6-112.

⁵⁴⁷ 1992—*The External Impact of European Unification*, May 4, 1990, p. 3.

to aid in the establishment of competitive telecommunication services.⁵⁴⁸

The Council of Ministers formally adopted a "common position" on the ONP directive (Com (89) 325) in February 1990. The Council had reached a political compromise on the ONP directive and the draft EC Commission directive on liberalizing telecommunication services during meetings held in December 1989. A major feature of the revised proposal is that technical interfaces and service features will become the subject of European standards to be adopted by ETSI. The standards will be voluntary, but the EC Commission can make the reference to a particular standard mandatory in order to guarantee the interoperability of transfrontier services. Mandatory standards, if they are in fact employed, are likely to apply only to packet-switched data transmission and integrated services digital networks (ISDNs). No mandatory standards are contemplated for value-added telecommunication services. Service providers that comply with voluntary standards will be able to offer their services throughout the Community. Even if mandatory standards are established, service providers will be able to offer other services, presumably those that do not use mandatory standards, in order to improve the freedom of choice for users. The Council also laid out the work program for future ONP directives: technical interfaces and service features for packet-switched data transmission and ISDN are to be established by January 1, 1991; ONP conditions, in the form of recommendations, will be adopted by July 1, 1991, for packet-switched data transmission and by January 1, 1992, for ISDN; and, in 1992, the Council will examine the EC Commission's proposals to determine which should be transposed into directives. Specific ONP directives will be issued concerning leased lines and voice telephony. The ONP directive was approved during the June 28, 1990, meeting of Telecommunications Ministers and will go into effect on January 1, 1991.⁵⁴⁹

The principle of the ONP directive is welcomed by businesses. However, concerns exist that ONP conditions for technical interfaces, supply and usage conditions, and tariff principles that might apply to users and private service providers are not adequately defined. Therefore, it is hard to judge the potential impact of the proposed directive. U.S. industry feels that the ONP conditions that may be applied to such private service providers should not be as stringent as those applied to the PTTs. The business community is also concerned that the ONP conditions may delay the creation of an open market for competitive telecommunication services.⁵⁵⁰

⁵⁴⁸ See "Open Network Provision," USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-106 to 6-107.

⁵⁴⁹ U.S. Department of State Telegram, June 1990, Brussels, Message Reference No. 09935.

⁵⁵⁰ *Business Guide to EC Initiatives*, American Chamber of Commerce in Belgium, Spring 1990, p. 83.

Cellular Digital Mobile Communications

On June 25, 1987, the Council of Ministers of the European Communities passed a "Recommendation on the Coordinated Introduction of Public Pan-European Cellular Digital Land-Based Mobile Communications in the Community," 87/371. On the same date, the Council adopted the Council Directive on the Frequency Bands to be Reserved for the Coordinated Introduction of Public Pan-European Cellular Digital Land-Based Mobile Communications in the Community, 87/372.

Background

There are a number of largely incompatible land-based mobile communications systems currently in use in the EC, including cellular telephone systems. In most cases these systems are analog, not digital, the general trend in information-transmission technology is to switch from analog to digital technology.

Anticipated Changes

It is anticipated that the telecommunications administrations of EC member countries will implement certain detailed recommendations concerning the coordinated introduction of public pan-European cellular digital land-based mobile communications in the Community.⁵⁵¹ The telecommunications administrations should plan for a gradual evolution from any existing public mobile radio systems to the public pan-European cellular digital land-based mobile communications system so as to ensure a transition that meets the needs of users, telecommunications administrations, and undertakings established within Community countries. Member states should rapidly complete the technical arrangements necessary to allow unrestricted access to cellular digital mobile communications. Member states are to inform the EC Commission at the end of each year, from the end of 1987 onwards, of the measures taken and problems encountered in the course of implementing the recommendation. It is planned that pan-European cellular digital mobile communications systems will be introduced by 1991, that major urban areas will be covered by 1993, and that the main links between these areas will be covered by 1995. Although initially voice telephony capabilities will constitute the most important

⁵⁵¹ Among these recommendations, the system should be suitable for use in the 890-915 MHz frequency bands, to be made available for the pan-European cellular digital mobile communications system; permit a traffic flow greater than, or equal to, existing networks; provide the user with a voice transmission quality at least equal to that of the existing systems; allow for efficient use of hand-held terminals by encouraging competition amongst manufacturers; and be sufficiently flexible to facilitate the introduction of new services related to integrated services digital networks.

service required, the mobile system must be open to an overall evolution towards ISDN services.⁵⁵²

Use of access signalling should be defined along the principles of the existing Conference of European Postal and Telegraph Administrations (CEPT) recommendations for ISDN. The telecommunications administrations should consider charging service basically according to the duration of the radio channel use, given the scarcity of frequency resources, and take into account the trend towards less distance dependence.

The directive will ensure that the 905-914 and 950-959 MHz frequency bands, or equivalent parts of the 890-915 and 935-960 bands, are reserved exclusively for a public pan-European cellular digital land-based mobile communications service by January 1, 1991. Member states are to bring into force the provisions necessary to comply with this directive within 18 months of its notification.⁵⁵³

Possible Effects

A coordinated policy for the introduction of a pan-European cellular digital mobile radio service will make possible the establishment of a European market in mobile and portable terminals, which will be capable of creating, by virtue of its size, the necessary development conditions to enable undertakings established in member countries to maintain and improve their presence in world markets. Such a market will encourage entry and investment by all world-class competitors, including those of the United States.

U.S. exports to the EC

Cellular telephone equipment may be roughly divided into subscriber equipment and systems equipment. Subscriber equipment is the equivalent of telephone instruments—the units that individuals use. Systems equipment covers the switching and control apparatus. Exports of cellular telephone equipment from the United States to the EC were \$25 million in 1989. Exports reached \$27 million for the first 4 months of 1990, higher than total 1989 exports and up by almost 350 percent over the same period of 1989. These data do not include systems equipment, as no separate statistical reporting categories for such products exist. The only significant U.S. exporter of subscriber equipment is Motorola, which is the largest subscriber equipment company in the world.

⁵⁵² The following mobile services should be available in all member states starting from 1991: nontransparent bearer service for speech; transparent bearer service for data transmission; hand-over services, national/international roaming, telephony at 3.1 kHz; and calling line identification, advice of call duration, and speech encryption.

⁵⁵³ This directive was notified to the member states on June 26, 1987.

Diversion of trade to the U.S. market

It is not likely that the recommendation or directive will lead to a diversion of trade to the United States, since the recommendation and directive will make the EC a more desirable market.

U.S. investment and operating conditions in the EC

It is not likely that U.S. investors will change their investment plans or EC-based production strategies because of this recommendation or directive. The U.S. industry now serves the EC primarily through direct investments in the EC. Motorola is the leading U.S. investor in cellular telephone equipment in the EC. As technical changes to products are required to comply with EC regulations, the U.S. investors will make those changes rather than exit the market. Nevertheless, since this directive is a building block supporting the liberalization of cellular phone services, it is expected to contribute to the expansion of the market for such equipment in the EC and lead to heightened competition among equipment suppliers.

Siemens of West Germany and Alcatel of France are the largest EC competitors in cellular telephone equipment, and neither is significant at this time. Nokia of Finland is the leading European competitor in subscriber equipment, and L.M. Ericsson of Sweden is the leading European competitor in systems equipment. Other third-country competitors in subscriber equipment are Japanese, most significantly NEC. Japanese companies are not major competitors in systems equipment in the EC.

U.S. Industry Response

In general, U.S. firms expect to benefit from the liberalization of the EC market for cellular digital mobile communications. U.S. industry concerns in the cellular digital land-based mobile communications industry are not based on this recommendation or directive. U.S. industry is concerned that it will be required to give up or share its patents for cellular telephone equipment in order to be a member of ETSI, the standards-setting body in the EC. There is also a 50-percent EC-content rule for government procurement that is not addressed in this recommendation and directive, but which is of concern to the U.S. industry.

Pan-European Radio Paging

On February 9, 1990, the Council of Ministers submitted a revised proposal for a Council Recommendation on the Coordinated Introduction of Pan-European Land-Based Public Radio Paging in the Community, 90/C 43/07. On the same date, the Council submitted a revised proposal for a Council Directive on the Frequency Bands to be Reserved for the Coordinated Introduction of Pan-European Land-Based Public Radio Paging in the Community, 90/C 43/08.

Background

There are a number of mutually incompatible radio paging services in use throughout the European Community, including incompatible systems within a single member country. The Council of Ministers intends to ensure that the technical conditions needed to support the introduction of pan-European paging service are established in each member state.

Anticipated Changes

The recommendation urges the telecommunications administrations of EC member countries to implement certain detailed recommendations concerning the coordinated introduction of pan-European land-based radio paging service in the Community.⁵⁵⁴ Member-state governments and telecommunications administrations should complete the technical arrangements for the implementation of the means of call routing and processing so that tone, numeric, and alphanumeric messages can be sent from anywhere in the Community to a paging receiver anywhere in the geographical coverage of the European radio-messaging system service (Ermes) by January 1992. By January 1992, service should be started in each member state and should cover at least 30 percent of the population of each member state by January 1993, 60 percent of the population by January 1994, and at least 80 percent of the population by January 1995. The European Parliament is urging the EC Telecommunications Ministers to amend their proposal and bring forward the deadline to January 1, 1991, at the latest.⁵⁵⁵

The directive stipulates that member states shall designate, on a priority and protected basis, four channels within the band 169.4 to 169.8 for the pan-European land-based public radio paging service, and member states shall ensure that plans are prepared as quickly as possible to enable the system to occupy the whole of the band according to commercial demand.

Possible Effects

Creation of a unified market with common standards will lead to an improved telecommunications infrastructure. A pan-European land-based public display paging service will make

⁵⁵⁴ Among these recommendations are that the system should be suitable for operation in the 169-170 MHz frequency band with 25 KHz radio channels; should permit an increase in the number of paging users that can be supported per paging area per unit of spectrum and for the same grade of service compared with systems based on CCIR radio paging code No. 1; should permit easy access through PSTN, PSS videotext terminals, telex, and other forms of direct access such as through ISDN; should permit simultaneous operation of two or more independent systems in the same geographic area; and should permit several independent systems in areas where several national boundaries meet.

⁵⁵⁵ "Telecommunications: Parliamentary Rubber Stamp for Radio Paging," *European Report*, No. 1604, Business Brief, p. 1.

possible the establishment of a European market in paging receivers that will be capable of creating, by virtue of its size, service features, and costs, the necessary development conditions to enable undertakings to maintain and improve their presence in world markets.

U.S. exports to the EC

Exports to the EC of radio paging receivers reached \$12 million in 1989. Exports for the first 4 months of 1990 were \$5 million, 25 percent ahead of the first 4 months of 1989. These data do not include ancillary equipment such as terminal equipment, as no separate statistical reporting categories for such products exist.

Diversion of trade to the U.S. market

It is not likely that the recommendation or directive will lead to a diversion of trade to the U.S. market, since the recommendation and directive will make the EC a more desirable market.

U.S. investment and operating conditions in the EC

It is not likely that U.S. investors will change their investment plans or EC-based production strategies as a result of this recommendation or directive. The major U.S. competitor in the EC pager market is Motorola. Motorola manufactures both pagers and terminal equipment for pagers. It manufactures pagers in the United States and the EC, and terminal equipment in the United States.

Most EC member countries are served by national manufacturers such as Plessey in the United Kingdom and Bosch and Siemens in West Germany. National manufacturers such as L.M. Ericsson in Sweden and Nokia in Finland are major non-EC competitors. In each EC member country, competitors are generally the national manufacturer, Motorola, and Japanese and Korean competitors including NEC, Panasonic, and Casio.

As technical changes to products are required to comply with EC regulations, the U.S. investors will make those changes rather than exit the market. Nevertheless, since this directive is a building block supporting the liberalization of paging services, it is expected to contribute to the expansion of the market for such equipment in the EC and lead to heightened competition among equipment suppliers.

U.S. Industry Response

U.S. industry has expressed no concern regarding the recommendation or directive. The industry has responded favorably, as pagers and terminal equipment intended to serve a single large market using a single standard can be produced more efficiently than pagers and terminal equipment intended to serve multiple markets, each with different incompatible standards.

Construction Products

In the area of construction products, an update will be given on work that is being undertaken in setting phytosanitary requirements for wood products in accordance with Directive 77/93 and also in the creation of standards and regulations under the Construction Products Directive (89/106). U.S. industry responses and concerns will also be discussed.

Phytosanitary Requirements for Wood Products

Background

The EC phytosanitary standards and regulations are restrictions intended to protect native species from foreign insects and diseases. Council Directive 77/93 set up the Community's plant-health regime in an effort to harmonize prohibitions and restrictions applicable to imports of plants and plant products, to prevent the introduction or spread of harmful organisms.⁵⁵⁶ If the EC is satisfied with the exporting country's history of quality control and its ability to meet established standards, the EC will accept grading equivalence. Approximately 25 countries that currently export to the EC would be eligible for equivalence, including the United States.⁵⁵⁷

In recent months, the U.S. wood products sector has shown concern that certain EC regulations may be trade restrictive. They have expressed concern about existing and proposed phytosanitary restrictions on two types of U.S. wood exports to Europe, oak logs and lumber and softwood products.

Anticipated Changes

In order to prevent the spread of oak wilt (*Ceratocystis fagacearum*), all oak logs and lumber imported into the EC must be free of bark and all red oak and white oak logs must be fumigated between April 30 and October 15. Oak wilt⁵⁵⁸ is considered by the EC as a harmful organism whose introduction must be prohibited in all member states.⁵⁵⁹ Oak wilt is an endemic vascular disease throughout the Eastern United States.

In order to prevent introduction into the EC of the *Bursaphelenchus Xylophilus* (the pinewood nematode), the EC Commission plans to have a requirement in place on January 1, 1991, that would

⁵⁵⁶ National Forest Products Association, *U.S. Woods Products Industry Concerns About EC92*, Feb. 15, 1990.

⁵⁵⁷ U.S. Department of State Telegram, 1990, Brussels, Message Reference No. 08406.

⁵⁵⁸ Listed under annex I, sec. A, subsec. d2, of Directive 77/93.

⁵⁵⁹ Directive 77/93, art. 3. Art. 2 of the directive provides that the directive applies to wood only insofar as it retains all or part of its natural round surfaces, with or without bark. Therefore, only logs and waney lumber are covered by the directive.

require softwood fuel wood, logs, lumber, railroad ties, packing containers, and pallets to be either kiln dried prior to importation into the EC or to be stripped of bark and accompanied by an official phytosanitary certificate that the wood has been treated by an EC-approved method. This requirement will apply only to imports from Canada, China, Japan, Korea, and the United States because of the risk of introducing the pinewood nematode from such countries.

Canada will likely receive a derogation (currently in draft form) that would allow sawn lumber exported from Canada to be entered into the EC without meeting the kiln-drying requirements. The derogation, due to expire December 31, 1991, would require exports from Canada to be accompanied by an official "Certificate of Debarking and Grub Hole Control," after in-plant inspections and occasional preshipment inspections by inspectors of Agriculture Canada, Plant Protection Division. The U.S. industry and Government are currently working toward obtaining a similar derogation.

Possible Effects

U.S. exports to the EC

In the absence of such a derogation, enforcement of the proposed regulations regarding the pine wood nematode would likely result in a reduction in U.S. exports of softwood lumber to the EC. Industry sources claim that it is technically infeasible to kiln-dry logs and unnecessary to kiln-dry sharp-edge (bark free) lumber. Currently, only about one-fourth of U.S. exports of softwood lumber from western ports to the EC are kiln dried, whereas most of the exports from southern ports are kiln dried. In 1989, exports of softwood lumber from western ports accounted for 58 percent of U.S. exports to the EC and exports from southern ports accounted for 40 percent. U.S. industry representatives report that domestic kiln-drying capacity is insufficient to meet the demand of the proposed regulation regarding the pine wood nematode. According to the National Forest Products Association, in 1989, domestic production of softwood lumber amounted to 37.3 billion board feet (roughly 88 million cubic meters), worth about \$9.3 billion.⁵⁶⁰ The following tabulation shows 1989 U.S. exports of the products affected by the pine wood nematode regulation (in thousands of dollars):

Product	Total exports	Exports to the EC
Wood chips	226,289	64
Softwood logs	2,180,691	6,349
Softwood lumber	1,404,141	251,014
Railroad ties	5,168	13

⁵⁶⁰ Estimated from U.S. Department of Commerce, 1990 *U.S. Industrial Outlook*.

Because most softwood lumber exports to the EC are currently of green lumber, the type affected by the regulations, and because of the limited kiln-drying capacity of U.S. producers, it is estimated that U.S. exports could decrease by 50 to 75 percent.

Continued enforcement of the regulations regarding oak wilt would likely continue to suppress U.S. exports of oak lumber to the EC. In order to be exported to the EC, oak lumber must be fumigated and certified as such by the U.S. Department of Agriculture Animal and Plant Health Inspection Service (APHIS). The United States is the world's leading producer of oak logs and lumber. According to the U.S. Department of Commerce,⁵⁶¹ domestic production of oak lumber amounted to 3.8 billion board feet (roughly 9 million cubic meters), worth about \$500 million in 1988. Oak lumber accounts for about one-half of U.S. hardwood lumber production. In 1989, the United States exported 399 million dollars' worth of oak lumber, of which \$180 million was marketed to the EC. Most oak logs and lumber that reach the export market are of relatively high quality, often destined for foreign furniture markets. Because of the added cost to exporters for the fumigation, it is believed that exports of oak lumber to the EC are suppressed by 10 to 15 percent.

Diversion of Trade to the U.S. Market

Implementation of the regulations regarding the pine wood nematode will likely result in a diversion of trade in Canadian softwood lumber from the EC to the United States. However, the derogation for Canadian softwood lumber, which will enable the continued exporting of green lumber to the EC through 1991, will mitigate the effects of the expected diversion of trade through 1991. The United States is currently the leading market for Canadian softwood lumber, receiving about 78 percent of Canadian exports, in terms of quantity, whereas the EC receives about 9 percent. It is unlikely that exports from other countries to the EC would be diverted to the United States.

Continued prohibition of unfumigated oak logs and lumber is unlikely to have any further trade-distorting effects. It is believed that if the regulations were eased, U.S. exports to the Pacific Rim countries would decline as U.S. firms sought out more profitable and traditional markets in the EC.

U.S. Investment and Operating Conditions in the EC

U.S. investment in the EC in facilities producing plants and plant products, including forest products, appears to be negligible. In the case of

⁵⁶¹ U.S. Department of Commerce, Bureau of the Census, *Current Industrial Reports, Lumber Production and Mill Stocks*, 1988.

forest products, U.S. investment in the EC log and lumber industry is limited primarily to wholesale operations, not to manufacturing operations in the EC.⁵⁶²

U.S. Industry Response

Thus far, representatives of the U.S. wood products industry have been more vocal in their concerns about phytosanitary regulations in the EC than their counterparts in the seed and plant industries. Representatives of the National Forest Products Association and the Western Wood Products Association have expressed their concern that additional or all-encompassing phytosanitary regulations may be imposed as the EC moves toward 1992. Representatives of the domestic wood products industry say that the domestic industry is hampered by the various actions that may be taken under the directive, such as the restriction of imports of products to prevent the spread of oak wilt or the pine wood nematode. The domestic industry is not opposed to phytosanitary regulations as such, but rather is opposed to the use of such regulations to disrupt trade.

Construction Products Directive

Background

The European Community is now in the process of creating a set of standards that will cover all construction materials affected by the Construction Products Directive (CPD) and also a set of building codes—a challenging task. Besides being faced with the difficulty of distinguishing between regulatory content of the EC directive's essential requirements that will be compulsory and technical standards, which are being developed by CEN/CENELEC, there is also the added complication that the essential requirements of the CPD relate to building works that could be subject to building code regulation at the national level. In translating the scope of standards for products, their classification, testing procedures, and use, CEN will be using interpretative documents as well as mandates from the EC Commission to clarify the legal framework.⁵⁶³ There is some risk, though, that the preparation of these documents could be a standardization exercise in itself.⁵⁶⁴

Anticipated Changes

The Construction Products Directive,⁵⁶⁵ scheduled to be implemented by June 27, 1991, is intended to ensure that construction products sold

⁵⁶² U.S. Mission to the European Communities, meeting with USITC staff.

⁵⁶³ Please see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-99 to 6-102, for a detailed explanation of the scope of EC work in this area and description of the interpretative requirements, Eurocodes, and European technical approvals.

⁵⁶⁴ CEN Conference on the European Harmonization of Construction Products, May 4, 1989, p. 23.

⁵⁶⁵ See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990.

in the EC market are "fit for their intended use," and meet certain general safety criteria. Construction products include those products produced for incorporation in a permanent manner in construction works, including both buildings and civil engineering works, insofar as the essential requirements relate to them. The essential requirements (annex I of the directive) apply to construction works, not to construction products as such, but they will influence the technical characteristics of those products.⁵⁶⁶ Products affected by the directive include timber, concrete, masonry, and steel; as well as installations and equipment and parts thereof for heating, air-conditioning, ventilation, sanitary purposes, electrical supply; storage of substances harmful to the environment; and prefabricated construction works that are marketed as such.⁵⁶⁷

Possible Effects

U.S. Exports to the EC

The CPD will probably have the most impact on U.S. forest products and heating, ventilating, and air conditioning (HVAC) industries. The European Community as a region ranks as the United States' second-largest market for forest products (\$987 million), behind Japan (\$2.8 billion) and ahead of Canada (\$645 million).⁵⁶⁸ Exports to this market continue to grow at a rapid rate, having more than tripled since 1985, and for processed wood products the EC is the United States' primary market. The four largest exports in value terms in 1989 were softwood lumber (\$250 million), hardwood lumber (\$245 million), softwood plywood (\$202 million), and hardwood veneer (\$90 million).⁵⁶⁹ EFTA members of CEN committees as well as Eastern European countries (Bulgaria, Czechoslovakia, Hungary, Poland, and Romania) are likely to adopt CEN standards. Thus, U.S. trade in forest products could be affected throughout the entire European continent.

Our previous report explained in detail the likely affect of the CPD on U.S. suppliers.⁵⁷⁰ While hoping to benefit from the EC's movement toward a more uniform set of regulations, codes, standards, and approval procedures, U.S. firms are concerned that without being able to participate in the creation of these standards and codes, they will lose ground to other European competitors and should technical biases be created against them in the European market.

⁵⁶⁶ British Department of Trade and Industry, *The Single Market, Standards, Construction Products*, April 1989.

⁵⁶⁷ EC Council, *Statements for Entry Into the Minutes*, Dec. 16, 1988.

⁵⁶⁸ National Forest Products Association Europe 1992 Program, *Statement for the Record*, USITC hearing, June 21, 1990, p. 3.

⁵⁶⁹ *Ibid.*

⁵⁷⁰ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-102 to 6-104.

The following CEN technical committees have issued standards⁵⁷¹ that the National Forest Products Association (NFPA) has found to directly affect U.S.-EC trade in wood products:

CEN/TC 33	Technological Tests for Doors, Windows, and Shutters
CEN/TC 38	Methods of Tests for Wood Preservatives
CEN/TC 91	Particleboard/Formaldehyde Determination (has since been incorporated into CEN/TC 112)
CEN/TC 103	Adhesives for Wood and Derived Timber Products
CEN/TC 112	Wood Based Panels
CEN/TC 124	Timber Structures
CEN/TC 127	Fire Safety
CEN/TC 175	Grading Standards for Non-Structural Timber ⁵⁷²

The above committees have dealt primarily with wood products. For example, CEN/TC 124 on Timber Structures is developing a new grading system for wood that differs considerably from U.S. methods and, if adopted, could have the result of grading U.S. timber as a weaker class of wood. If this occurs, U.S. structural timber could virtually lose its European market, as U.S. wood will not be considered as strong or reliable as European species.⁵⁷³ An additional committee, CEN/TC 250 Eurocodes, has been established this year to create a European building code and system design that will in turn affect the degree to which Europe will be able to use wood in commercial or residential structures.⁵⁷⁴

In the certification of products, the letters "CE" would note that the product conformed with the essential requirements. With the CPD, however, prescribed forms of independent endorsement may be required to underpin "CE" marking for products or particular applications as a result of associated risks.

At present the HVAC industry both exports to and has major foreign manufacturing investment in, the EC. Until recent years, this industry relied primarily on exports to serve the EC. The EC represents the second-largest market for these products, following only the United States. According to the Air-Conditioning and Refrigeration Institute, U.S. exports of HVAC products to Europe in 1989 amounted to \$537 million. U.S. firms are estimated to account for a 35- to 40-percent share of the EC market for these products at present. Major types of equipment and components exported to the EC include auto and truck refrigeration and air-conditioning compressors, parts for refrigeration and

⁵⁷¹ Contact USITC staff for a listing of the status of mandated work associated with the Construction Products Directive.

⁵⁷² National Forest Products Association Europe 1992 Program, *Statement for the Record*, USITC hearing, June 21, 1990, pp. 7-8.

⁵⁷³ *Ibid.*, pp. 18-19.

⁵⁷⁴ *Ibid.*, p. 8.

air-conditioning equipment, all types of room air-conditioners, and self-contained split-system heat pumps and air-conditioners. West Germany, France, the United Kingdom, Belgium, and Spain account for the bulk of U.S. exports to the EC.

According to industry officials, the majority of U.S. exports to the EC consists of unitary equipment that has few major world competitors. However, Japanese suppliers of compressor technologies (i.e., rotary and scroll compressors) are expected to make some long-term inroads in select component areas of this industry. There are numerous medium- and small-sized HVAC firms that export to Europe. Nearly all of these firms utilize the services of export-management firms located nationwide. A number of these small and medium sized firms primarily export components and functional equipment. Medium and small producers of HVAC equipment are likely to continue to rely on exporting their products to the EC regardless of minor changes to regulations in the EC.

Diversion of trade to the U.S. market

The CPD is not likely to result in trade diversion from the EC to the U.S. market of HVAC equipment. Because the United States and Japan account for approximately 70 percent of world market share, coupled with a mature market for these products in the United States, third-country exports to the United States are not likely to be a problem should implementation of this directive result in a worsening of the business environment in the EC.

U.S. investment and operating conditions in the EC

In 1987, U.S. direct investment in the EC for manufacturing machinery except electrical (which includes air-conditioning and refrigeration equipment) amounted to \$3.9 billion. U.S. manufacturing investment in the EC for HVAC products is estimated to be nearly \$415 million. Some of the leading U.S. investors in the EC in 1989 were as follows:

1. Snyder General Corp., Dallas, TX
2. York Heating and Air-Conditioning Corp., York, PA
3. The Trane Co., La Crosse, WI
4. Baltimore AirCoil Co., Jessup, MD
5. Honeywell Inc., Minneapolis, MN
6. Lennox International Inc., Dallas, TX

It is not clear at present whether U.S. investors in the HVAC industry are likely to change their investment plans or EC production strategies as a result of this pending directive. Nearly all producers that are currently exporting their products to the EC cite concern regarding high social overhead cost in countries such as France and West Germany as deterrents to increased U.S. investments in the EC. A few small and medium-sized firms indicated to the staff of the USITC their continued interest in either

joint-venture or licensing agreements with potential EC-based companies. Nearly all large firms in the HVAC industry are ensuring that marketing distribution channels be enlarged to accommodate larger economies of production scales.

U.S. Industry Response

The NFPA has expressed concern over certain aspects of the EC's standardsmaking procedures. First, interested and affected parties from the United States are unable to comment on draft standards before they are completed because they are unable to participate in or attend CEN technical committee meetings. Although comments may be made through the American National Standards Institute (ANSI), the NFPA claims that this process is limited in scope, and instead, the NFPA is looking for an increased Government effort on the part of the United States to obtain observer status at these meetings. Secondly, there is further fear that U.S. competitors from EFTA countries, members of CEN committees, will be able to influence procedures to prevent or seriously limit U.S. wood products from being exported to the European Community. Third, NFPA encourages a more balanced membership between producers, users, and general interest in standardsmaking committees, as there is some worry that the current producer dominance on CEN committees will create a bias against U.S. imports. Finally, concerns have been expressed with regard to testing and certification. If products need to be retested and recertified by EC third-party laboratories, U.S. exporters would be faced with significant costs and delays.

The NFPA has established a system to examine and analyze standards being proposed by CEN committees. It has created parallel CEN/TC committees of technical experts in the United States—each to review material, organize an appropriate industry response, and assemble information on actions that are being taken with regard to standards in their EC counterpart.⁵⁷⁵

Nearly all associations and firms associated with the heating, ventilating, and air-conditioning (HVAC) industry say that until it is possible to translate the health, safety, and environmental requirements of this directive into technical requirements for building works themselves, it will be difficult to predict the extent to which U.S. industry will be affected by this directive. The most important issue affecting the HVAC industry is the clarification of the interpretive documents relating to the CDP. Clarification of four of the six essential requirements (1. safety in use; 2. protection against noise; 3. hygiene, health, and the environment; and 4. energy economy and heat retention) will be essential in determining how the HVAC industry will be affected by this directive. Large producers of primarily air-conditioning and refrigeration equipment are already highly involved in standards activities within the EC.

⁵⁷⁵ Ibid., pp. 5-6.

CHAPTER 5
FINANCIAL SECTOR

CONTENTS

	<i>Page</i>
Developments covered in the previous reports	5-3
Background and anticipated changes	5-3
Possible effect	5-3
Recent developments	5-3
Banking	5-3
Investment services and securities	5-4
Investment services	5-4
Capital adequacy	5-4
Stock exchange directives	5-5
Insurance	5-5
Life insurance	5-5
Nonlife insurance	5-5
Motor insurance	5-6
Insurance committee	5-6

CHAPTER 5 FINANCIAL SECTOR

The 1992 program for financial services has raised interest and concern in the United States. EC capital markets and financial firms are likely to become relatively more competitive and efficient. Liberalized and open financial and capital markets in the European Community should create potential business opportunities for U.S. financial services firms. Reciprocity provisions have been included in the financial services directives, however, and the application of the Community's reciprocity policy may have the effect of restricting the future market access of U.S. firms.

Developments Covered in the Previous Reports

Background and Anticipated Changes

The Treaty of Rome set forth the free movement of services and capital as two of its principal objectives. However, barriers to the freedom of capital movements, to cross-border trade in financial services, and to the freedom to establish financial services firms have restricted the full financial integration of the EC market. With the adoption of the White Paper on Completing the Internal Market and the Single European Act, the EC set out to create a single financial market.

The financial services directives, in conjunction with the capital movements directives, are intended to have three broad effects: (1) to liberalize the financial services sectors, (2) to benefit the individuals and firms that consume such services, and (3) to increase the discipline of market forces on the monetary and fiscal policy of member states.

The approach of the EC has been to harmonize essential standards that apply to financial services firms regarding authorization, supervision, and prudential rules and to provide for the mutual recognition of home-country control on the basis of those harmonized rules. Under this regulatory regime, financial services firms will be able to operate throughout the EC with a single license.

The approximately 30 financial sector directives apply to banking, securities, insurance, and the free movement of capital. The Capital Movement Directive provides for the full liberalization of all capital movements as of July 1, 1990. The core banking directive is the Second Banking Directive, which introduces the single banking license and which is deemed by the EC to be "essential" to achieving the internal market. The Own Funds and Solvency Ratio Directives deal with the capital adequacy of banks and will be implemented simultaneously with the Second Banking Directive. A bank with a single license, including an EC subsidiary of a U.S. bank, will be able to undertake banking and securities activities throughout the EC

either through branching or through the cross-border provision of services.

The Investment Services Directive is the core directive for securities firms. It is modeled on and complements the Second Banking Directive. The directive would introduce the single license and provide for the mutual recognition of home-country control for securities firms. Other important securities directives coordinate rules on mutual funds, insider trading, and public-offer prospectuses. Once an investment firm has a single license, it can sell its services throughout the EC.

Two insurance directives deal with the freedom of cross-border services for life and nonlife insurance. The Second Nonlife Insurance Directive provides that firms can sell nonlife insurance on a cross-border basis to industrial and commercial customers with home-country control. The Second Life Insurance Directive would provide that firms can sell individual and group life insurance on a cross-border basis with home-country control, but only when the policyholder takes the initiative in obtaining the policy. In addition, the EC Commission expects to introduce a single license for life insurance and nonlife insurance in forthcoming "framework" directives.

Possible Effects

The 1992 program for financial services creates opportunities as well as challenges for U.S. firms. Although most of the necessary directives in this area, as outlined in the White Paper, have been proposed and adopted, a host of definitional and interpretive uncertainties remain. As more final directives are adopted and as national governments begin to implement the directives, the net effect of the financial services directives in the EC, in individual member states, and in the rest of the world should become clearer. In any case, the liberalization of the EC financial sector has helped prompt further consideration of whether reform of the U.S. regulatory system is necessary to enhance the global competitiveness of the U.S. financial sector.¹

Recent Developments

Banking

As indicated in our earlier reports,² the European Community has made relatively good progress with the package of legislative measures that makes up the 1992 program for the financial sector. In December 1989, the Second Banking Directive was adopted, thereby completing the

¹ See, e.g., General Accounting Office, *European Community: U.S. Financial Services' Competitiveness Under the Single Market Program* (May 1990).

² See U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States* (Investigation No. 332-267), USITC Publication 2204, July 1989, ch. 5, and U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States - First Follow-Up Report* (Investigation No. 332-267), USITC Publication 2268, March 1990, ch. 5.

adoption of the core group of 1992 banking directives.³ In addition, on July 1, 1990, the full liberalization of capital movements became effective. The EC Commission has turned its attention to related matters such as money laundering,⁴ the transparency of cross-border banking conditions,⁵ banking secrecy, deposit insurance, payment cards and electronic payment systems,⁶ consumer protection, and the taxation of savings. Also, the EC Commission is monitoring the implementation of the banking directives and the impact of free capital flows in the individual member states.

Investment Services and Securities

Investment Services

Legislative progress in the securities sector has followed progress in the banking sector. On October 1, 1989, the liberalization of mutual funds became effective.⁷ The EC Council of Finance Ministers is currently seeking to reach a common position on the proposed Investment Services Directive.⁸ The directive would introduce a single license for investment firms that provide investment services throughout the Community. Although the EC's regulatory approach for investment firms follows and is modeled on the approach taken in the banking area, legislative progress has been relatively more difficult for a variety of reasons. Nevertheless, the EC Council has recognized the need to reach a common position in 1990 so that the directive can be adopted and implemented on January 1, 1993, along with the Second Banking Directive.

³ See *Second Council Directive 89/646, Official Journal of the European Communities* No. L 386 (Dec. 30, 1989), p. 1. Since the adoption of the Second Banking Directive, two technical corrections to the text of the directive have been made. See *OJ No. L 83* (Mar. 30, 1990), p. 128, and *OJ No. L 158* (June 23, 1990), p. 87.

⁴ See *Proposal, Com(90) 106, OJ No. C 106* (Apr. 28, 1990), p. 6.

⁵ See *Commission Recommendation 90/109, OJ No. L 67* (Mar. 15, 1990), p. 39.

⁶ In late 1988, the EC Commission issued a recommendation on payment systems and the relationship between cardholders and card issuers. See *Commission Recommendation 88/590, OJ No. L 317* (Nov. 24, 1988), p. 55. In early 1990, the European banking industry submitted a proposed code of best practice to the EC Commission. The EC Commission and European consumer groups are concerned about whether the proposed code appropriately limits the liability of cardholders for losses in cases where the cardholder acts reasonably, provides prompt notice of loss, and does not act fraudulently or with extreme negligence. Moreover, the EC Commission is concerned about the proliferation of payment cards issued by retailers. Following the EC Commission's review of this issue, it may decide to propose a directive or regulation that would contain common, binding rules that would limit cardholders' liability and would apply to both banks and retailers. For a discussion of the issues raised by the proliferation of payment cards and payment systems, see generally OECD, *Electronic Funds Transfer: Plastic Cards and the Consumer* (1989).

⁷ See *Council Directive 85/611, OJ No. L 375* (Dec. 31, 1985), p. 3.

⁸ See *Amended Proposal, Com(89) 629, OJ No. C 42* (Feb. 22, 1990), p. 7.

Divergent views have arisen regarding a provision in the draft directive that would seek to liberalize access to membership in stock exchanges. One issue relates to whether banks should be allowed to be direct members of stock exchanges, without having to establish a securities subsidiary in the host member state. Another issue relates to whether, and the extent to which, a bank or investment firm that is a member of a stock exchange in another member state would have to comply with local exchange rules and practices in the host member state.

The Finance Council is also considering the appropriate allocation of supervisory responsibility with regard to prudential rules that protect investors and consumers in the event of an investment firm's bankruptcy. The amended proposal provides that firms must contribute to the general compensation scheme in the home member state, except that branches of investment firms must contribute and be subject to the compensation regime of the host member state. Also, the Council is examining the scope of the directive and whether a common code of business practice rules would be appropriate.

Capital Adequacy

After considerable debate within the Community, the EC Commission has issued the proposed Capital Adequacy Directive.⁹ Like the Own Funds and Solvency Ratio Directives in the banking area, the Capital Adequacy Directive would set minimum capital requirements for financial firms that undertake investment services. The proposal sets common standards for initial capital, capital reserves, and for monitoring the market risks of investment firms. This harmonization is intended to facilitate the mutual recognition of the single investment firm license and to protect investors, firms and the financial system. The proposal is essential to the authorization and prudential supervision of investment firms and to the adoption of the Investment Services Directive.

The principal difficulty is to devise a capital adequacy regime that will ensure the security and stability of investment firms and also ensure that an equitable regulatory capital cost structure is applied to nonbank investment firms and banking firms operating in the securities markets. In other words, the EC wants banks and nonbank investment firms engaging in securities activities to be subject to comparable capital requirements to ensure fair competition and to avoid favoring one institutional structure over another. The proposal provides that the competent authorities may determine whether the investment services activities of banks should be covered by prudential rules set forth in the banking directives or by the capital adequacy rules in the Capital Adequacy Directive. Thus, banking supervisors can apply the Solvency Ratio Directive to all of a bank's activities, including its trading

⁹ See *Proposal, Com(90) 141, OJ No. C 152* (June 21, 1990), p. 6.

operations, or they can allow banks to apply the capital adequacy provisions to the bank's investment services trading book.¹⁰ In either case, the bank will have to abide by the directive's requirement to set aside capital sufficient to cover foreign-exchange risk (art. 4(2) and annex 4).

In general, investment firms would be required to have initial capital of at least 500,000 ECU (art. 3(2)). However, firms that act as agents or portfolio managers but do not hold trading positions of their own need only to have initial capital of 100,000 ECU (art. 3(4)). Firms that are not authorized to hold customers' monies or securities, nor to act as market makers or underwriters, need only have initial capital of 50,000 ECU (art. 3(3)). In order to ensure the security, stability, and continuity of firms, all investment firms would be required to hold capital equivalent to 25 percent of their fixed overhead for the previous year (art. 4(1) and annex 5). Lastly, local firms and investment advisors do not need to meet the initial capital requirements, and existing firms whose current capital reserves are below the minimum initial capital level may continue operating as long as their capital reserves do not decline.

Investment firms would have to hold enough capital to cover each of the various risks associated with their particular activities. The reserve requirements are based on a complex, risk-weighted formula that takes into account the type and degree of market risk inherent in each activity, as well as whether offsetting positions, through hedging or netting, have reduced the risk.

Stock Exchange Directives

As noted in our previous reports, the Public Offer Prospectus Directive provided for the mutual recognition of a public-offer prospectus, and the Mutual Recognition of Listing Particulars Directive provided for the mutual recognition of listing particulars. In April 1990, the EC Council adopted a directive that provides for the mutual recognition of public-offer prospectuses as stock exchange listing particulars.¹¹ Under this directive, a public-offer prospectus must be accepted as listing particulars when an admission to an official stock exchange listing in one member state is sought within a short period of a public offer in another member state. This directive is expected to make it more efficient and less expensive for a firm to prepare a prospectus and have its shares offered and listed in more than one member state.

¹⁰ Art. 2 defines the "trading book" of a credit institution as "its proprietary positions in transferable securities or derivative instruments, which are taken on by the credit institution in order to benefit from actual or expected differences between their buying and selling prices, or in order to hedge other elements of the trading book."

¹¹ See Council Directive 90/211, OJ No. L 112 (May 3, 1990), p. 24.

Insurance

Life Insurance

The Second Life Insurance Directive would provide that insurance firms may sell life insurance on a cross-border basis with home-country control when the policyholder takes the initiative in seeking the policy. If the policyholder does not take the initiative, then host-country control applies.

Following a preliminary political agreement in December 1989 by the EC Council on the proposed Second Life Insurance Directive, the EC Commission issued an amended proposal in March 1990,¹² the European Parliament delivered its opinion, and the EC Council reached a common position in June 1990.¹³ The amended proposal and common position largely incorporated the changes made in the preliminary political agreement.¹⁴ The proposal would allow firms to sell individual life policies on a cross-border basis with home-country control. The common position extends the scope of the directive to include group insurance coverage (art. 10), it removes limitations on the role of brokers (art. 13), and it generally incorporates the more flexible reciprocity provisions that were contained in the Second Banking Directive (arts. 8 and 9).

The common position also eliminates what were thought to be unnecessary restrictions on cross-border advertising by insurers and brokers (art. 13). The original proposal had provided that home-country control applied only when limited advertising took place; otherwise, if firms or brokers advertised on a cross-border basis, then host-member-state control would apply. The common position provides that, notwithstanding cross-border advertising, home-member-state control would still apply, unless the policyholder was contacted directly or solicited personally. On the issue of the proper allocation of supervisory responsibility between the home member state and the host member state, the common position provides for a transitional period during which host-member-state control applies to cross-border group insurance sales and to sales through brokers. After the transitional period, life insurance firms can sell group policies and individual life policies on a cross-border basis directly or through brokers, with home-country control, as long as the policyholder takes the initiative and is not solicited personally.

Nonlife Insurance

The EC Commission has not achieved the same degree of liberalization in the insurance sector as it

¹² See *Amended Proposal*, Com(90) 46, OJ No. C 72 (Mar. 22, 1990), p. 5. The EC Commission proposed an amendment to the amended proposal for a Second Life Insurance Directive. The amendment would insert two additional recitals. One recital covers the tax consequences of dividing up a composite insurance undertaking, and the other recital notes the importance of an insurance broker's professional qualifications and independence in order to safeguard the interests of consumers. See Com(90) 305, OJ No. C 179 (July 19, 1990), p. 14.

¹³ See EC Council, *Common Position*, June 29, 1990.

¹⁴ See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 5-17.

has achieved or sought to achieve in the banking and securities sectors. For example, the Second Nonlife Insurance Directive introduces freedom of nonlife insurance services for large-risk customers, and the Second Life Insurance Directive would introduce freedom of life insurance services, but only when the policyholder takes the initiative. By comparison, the Second Banking Directive and the Investment Services Directive would authorize banks and securities firms to sell a wide range of financial services, either by establishing branches or by selling on a cross-border basis, throughout the Community to large and small customers on the basis of home-country control.

In July 1990, the EC Commission issued the proposed Third Nonlife Insurance Directive, or Framework Directive.¹⁵ This directive seeks to establish a single insurance license for all insurance other than life insurance.¹⁶ The Framework Directive would authorize insurance firms to establish branches or provide cross-border nonlife insurance services to individual customers on the basis of the mutual recognition of home-country control. The introduction of the single license is made possible because the directive coordinates rules on technical reserves and prudential supervision.

The host member state would be precluded from requiring that firms with a single license operating in its territory be authorized by the host member state. Also, the host member state could no longer require that policies be preapproved, that premiums be set at a certain amount, that firms invest in certain instruments, or that firms invest within the host member state. On the other hand, the host member state will retain certain authority, including being able to require that its own contract law applies to mass-risk policies, that it be notified of policies relating to compulsory insurance, and that it may protect "the general good" in the host member state.¹⁷ The Nonlife Framework Directive will undoubtedly be the subject of considerable debate within the European Community.

Motor Insurance

In June 1990, the EC Council reached a common position on the Motor Services Directive.¹⁸ The directive would generally extend the coordination of the Second Nonlife Insurance Directive to the freedom to provide insurance services against civil liability regarding motor vehicles. The proposal would effectively extend the rule of home-member-state control for cross-border

nonlife insurance services to large risks in the field of motor insurance. Host-member-state control would apply to individuals (i.e., mass risks). The biggest difficulty was in determining whether an insurance firm that sold motor insurance coverage on a cross-border basis would have to meet the capital requirements (i.e., technical reserves) in the host member state, or whether it would be sufficient to meet the requirements in the home member state. The common position provides that, on a transitional basis, the host member state may determine the amount of technical reserves relating to an insurance contract and what type of assets may meet the technical reserves and may require that they be invested in the host member state.

The most significant change in the common position is that the directive has been amended to include a reciprocity provision that is modeled on the Second Life Insurance Directive, and the reciprocity requirement applies to the supply of all nonlife insurance services. In other words, the directive effectively extends the coverage of the EC reciprocity policy to the Second Nonlife Insurance Directive, which was adopted in 1988 and which became effective on July 1, 1990. The general issues and considerations that are raised by the reciprocity provision are the same issues that are raised in the life insurance, investment services, and banking sectors.¹⁹ The United States has continuing concerns about the EC reciprocity policy.²⁰

In May 1990, the EC Council adopted the Third Motor Insurance Directive.²¹ The directive sets a minimum third-party compulsory insurance coverage throughout the Community, thereby eliminating the need for 'green cards.' It also should make it easier for accident victims to get compensation from national guarantee funds when the person at fault is uninsured or unidentified.

Insurance Committee

In July 1990, the EC Commission proposed a directive to establish an insurance committee that would assist the EC Commission in insurance matters in the way that the Banking Advisory Committee assists with banking matters. The committee would assist and advise the EC Commission on the interpretation and application of existing legislation and the drafting of future legislation covering both life and nonlife insurance. It would be composed of member-state representatives from the supervisory authorities for the insurance sector and would be chaired by an EC Commission representative. Also, the insurance committee would provide advisory assistance in administering the Community's reciprocity policy.

¹⁵ See *Proposal*, Com(90) 384. The official text was not available at the time that this report was being completed.

¹⁶ It should be noted that the EC Commission expects to issue by the end of the year a Third Life Insurance Directive that would introduce a single life insurance license.

¹⁷ The concept of the "general good" has developed in the jurisprudence of the European Court of Justice, and it is similarly incorporated in the banking and securities directives.

¹⁸ See EC Council, *Common Position*, June 20, 1990. See also *Amended Proposal*, Com(90) 278, OJ No. C 180 (July 20, 1990), p. 6, and *Proposal*, Com(88) 791, OJ No. C 65 (Mar. 15, 1990), p. 6.

¹⁹ For a summary of this issue, see "Reciprocity," pt. 3, ch. 17 of this report. See also USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, p. 5-10 through 5-12 and USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, ch. 5.

²⁰ See, e.g., U.S. Government Task Force on the EC Internal Market, *EC 1992: An Assessment of Economic Policy Issues Raised by the European Community's Single Market Program* (May 1990).

²¹ See *Third Council Directive 90/232*, OJ No. L 129 (May 19, 1990), p. 33.

CHAPTER 6
PUBLIC PROCUREMENT AND THE INTERNAL ENERGY MARKET

CONTENTS

	<i>Page</i>
Developments covered in the previous reports	6-3
Background and anticipated changes	6-3
Possible effects	6-3
Developments during January-June 1990	6-4
Public procurement	6-4
Background and anticipated changes	6-4
Excluded-Sectors Directive	6-4
Thresholds	6-4
Derogation for the energy sector	6-4
Implementation	6-5
Article 29 and the EC-preference provisions	6-5
Small and medium-sized enterprises	6-5
Possible effects	6-6
General	6-6
Recent studies	6-7
The internal energy market	6-8
Background and anticipated changes	6-8
Thermie	6-9
Security of energy supplies	6-9
Progress report	6-9
Possible effects	6-10

CHAPTER 6

GOVERNMENT

PROCUREMENT AND THE

INTERNAL ENERGY MARKET

At an estimated 15 percent of EC Gross Domestic Product, the EC public sector represents a large and potentially crucial market for a number of U.S. industries. In several key areas—such as telecommunications equipment, power generators, computers, and water-treatment equipment—public purchasers are the most important prospective EC customers for U.S. firms. Currently, however, U.S. suppliers are not ensured access to nearly half of the value of EC public sector contracts because these contracts fall outside the scope of EC and international trading rules. As part of the 1992 program, the EC will put in place rules intended to introduce greater openness, transparency, and nondiscrimination in all phases of public purchasing.

Developments Covered in the Previous Reports

Background and Anticipated Changes

In the 1970s the EC adopted two directives intended to increase competition in member-state procurement. The legislation attempted to increase transparency and reduce opportunities for discrimination in procurement of public works and supplies. Subsequently, the EC joined the Tokyo Round Agreement on Government Procurement, to which the United States is also a signatory.

Despite these steps, progress in opening up public sector markets in the EC was minimal. In its 1985 White Paper, the EC Commission proposed a substantial strengthening of member-state commitments on public procurement.

The legislation envisaged as part of the 1992 program would—

- Close loopholes in existing directives governing central and local government purchases of goods (“supplies”) and public works construction;
- Expand the scope of EC discipline to service contracts and most entities in the so-called “excluded sectors” of telecommunications, water, energy, and transport;
- Require member states to provide effective administrative and judicial remedies for wronged suppliers; and

- Strengthen EC oversight of member-state procurement practices.

As of yearend 1989, the EC had adopted three directives that cover “supplies,” “works,” and “remedies,” and had proposed one directive covering the excluded sectors. In 1989, the EC also introduced a system for monitoring compliance with public procurement rules of projects executed with assistance from the EC’s structural funds and financial instruments.

In addition to proposals to extend coverage of public procurement rules to energy under the excluded-sectors directive, the EC’s energy sector is now the subject of separate initiatives designed to create an EC-wide energy market. During 1989 the EC Commission proposed four measures to (1) improve the transparency of natural gas and electricity prices; (2) coordinate investment projects in the oil, natural gas, and electricity sectors; and (3) improve guarantees for the right of transit on the major grids for both electricity and natural gas. These measures are intended not only to eliminate existing obstacles to a unified energy market but also to take into account the EC’s overall energy objectives of guaranteeing a secure supply of energy, reducing costs, and producing environmentally harmless energy.

Possible Effects

U.S. suppliers and procurement experts generally believe that the EC’s 1992 program will eventually open EC public sector markets. However, U.S. suppliers are concerned that a 50-percent EC-content rule in the proposed excluded-sectors directive will hamper their ability to take increased advantage of more open procurement. This rule would result in an unpredictable bidding situation and could have the effect of requiring U.S. firms to invest in the EC in order to win procurement contracts. Such content rules are among the issues being addressed in ongoing negotiations to revise the GATT Code on Government Procurement.

Because energy—like other public sector markets—is currently one of the EC’s more tightly protected industries at the national level, efforts to complete the internal energy market will likely be long and arduous. Ultimately, companies operating in the EC should benefit from the greater freedom to choose among the types of energy consumed as well as among suppliers. As the energy sector restructures and procuring entities are pressured to lower costs, marketing opportunities for U.S. suppliers of coal and energy equipment and technology should increase. However, U.S. energy firms will continue to face restrictions if more open public procurement procedures in the energy sector are not implemented.

Developments During January-June 1990

Public Procurement

Background and Anticipated Changes

With the adoption by the EC Commission of the three directives covering supplies, works, and remedies by yearend 1989, the major development in the area of public procurement during the first half of 1990 was an agreement for a common position on the directive covering the four excluded sectors of water, energy, transport, and telecommunications.¹ The EC Commission also adopted a communication outlining procedures to increase the participation of small and medium-sized enterprises in public contracts. Proposals for directives covering procurement rules for services and an appeals procedure for contracts covered by the Excluded-Sectors Directive remain pending.² The EC Commission also anticipates a separate proposal for a directive on services falling under the scope of the excluded sectors.³

Title VII of the Omnibus Trade and Competitiveness Act of 1988 requires the administration to submit to Congress an annual report identifying foreign countries that discriminate against U.S. firms in the award of government contracts. The first report, due April 30, cited the EC among other countries as "a procurement market of particular significance and where substantial procurement problems have arisen," particularly in the heavy electrical equipment and telecommunications sectors. However, the report did not identify the EC nor any other country because renegotiation of the GATT Agreement on Government Procurement is the administration's top procurement priority and is progressing "in good faith."⁴

Excluded-Sectors Directive

On February 22, 1990, the EC Council reached an agreement in principle for a common position on the Excluded-Sectors Directive⁵ after over a

¹ For a description and analysis of these directives, see U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States* (Investigation No. 332-267), USITC Publication 2204, July 1989, pp. 4-1 to 4-44, and U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States* (Investigation No. 332-267), USITC Publication 2268, March 1990, pp. 4-1 to 4-7.

² The EC Commission proposed a directive for remedies in the excluded sectors on July 4. A proposal on services is anticipated by September 1990. EC Commission official, interview by USITC staff, Brussels, July 19, 1990.

³ No timeframe has been established for a proposal on services covered by the excluded sectors. U.S. Department of Commerce, telephone conversation with USITC staff, Washington, DC, July 9, 1990.

⁴ The United States Trade Representative, "Fact Sheet, Title VII," Apr. 27, 1990.

⁵ The Excluded-Sectors Directive is also referred to as the Utilities Directive.

year-long debate. On March 29, the Council formally adopted the common position and sent the directive to the Parliament for its second reading. Parliament made minor amendments to the Council's common position.⁶ It is anticipated that the EC Council will adopt the directive by September 1990.⁷

The major changes incorporated into the common position addressed the threshold value of contracts above which the directive applies, the scope of the directive's coverage, and the date of implementation of the directive. Although the most controversial provision of the directive for non-EC firms—the so-called 50-percent-content rule—remained the same, the rule of origin used to determine EC content was changed.

Other changes incorporated into the common position tended to clarify, rather than modify, the original directive. One such revision clarified that the directive would not apply under certain conditions to the supply of drinking water, electricity, gas, or heat to a contracting entity other than a public authority that provides a public service over a network. The directive would not apply when these products are byproducts of or important inputs into the production of the entity's principle service and the entity's service falls outside the scope of the directive nor would it apply when the quantity supplied to the public network falls within certain limits set by the directive.

Thresholds

The common position increased the threshold level for "supplies" contracts above which the procurement rules would apply. In the original proposal, the directive applied to "supplies" and "works" contracts with a value in excess of 200,000 and 5 million ECU respectively. Although the threshold for "works" contracts remained unchanged, the common position set threshold levels of 600,000 ECU for telecommunications supplies contracts and 400,000 ECU for all other supplies contracts.

Derogation for the Energy Sector

The common position also introduced a provision that allows member states to petition for a derogation from complying with the directive's bidding requirements on behalf of entities involved with the exploration or extraction of oil, gas, coal, or other solid fuels. The derogation is granted on an entity-by-entity basis.⁸ Certain conditions must be met before a member state may take advantage of the exemption. The first set of conditions requires that authorization to conduct such exploration or extraction activities be granted on a competitive

⁶ None of the amendments fundamentally changed the directive. U.S. Department of Commerce, telephone conversation with USITC staff, Washington, DC, July 9, 1990.

⁷ EC Commission official, interview by USITC staff, Brussels, July 19, 1990.

⁸ *Ibid.*

basis and on the basis of transparent criteria, and that the terms and conditions of the contract be made available prior to granting the license to operate. The directive also stipulates that member states must ensure through the conditions of the authorization or other appropriate measures that contracting entities award supplies and works contracts on a nondiscriminatory and competitive basis. In particular, these entities are required to make available their procurement intentions. Should the EC Commission discover evidence of discrimination in either the granting of licenses or the award of procurement contracts, it may revoke the derogation. Information on noncompliance with the directive will be made available to the EC Commission through reports submitted by the contracting entities, private complaints, or its own investigation.

Implementation

Because of requests from certain member states, the date of implementation of the directive was delayed for Spain, Portugal, and Greece. All member states are required to adopt the national measures necessary to comply with the directive by July 1, 1992. The directive will enter into force on January 1, 1993, for all member states except Spain (which has until January 1, 1996) and Portugal and Greece (which have until January 1, 1998).

Article 29 and the EC-Preference Provisions

The most controversial provisions of the original directive for non-EC suppliers were the mandatory 3-percent price preference granted to EC bids over equivalent non-EC-origin offers and the so-called 50-percent value-added rule that permits contracting entities to exclude offers when less than half the value of the goods or services to be rendered are of EC origin. The common position incorporated these provisions unchanged under article 29 with the exception of the introduction of a new rule of origin. Due to some confusion and a lack of predictability, the rule of origin used to determine EC content was changed to the EC's generally accepted rule of origin that is based on the last substantial transformation. The directive originally stipulated that a procuring entity "may reject any offer when more than half of the price offered represents the value of products manufactured or services performed outside the Community or a combination thereof." This provision was further clarified by defining the value of products manufactured outside the EC as "including the value of all finished or semi-finished products imported, directly or indirectly, from non-member countries" and defining the value of services performed outside the Community as "including the value of all activities performed on the territory of non-member countries that contribute to the rendering of the services covered by the contract." The language in the revised directive states that "any tender made for the award

of a supply contract may be rejected where the proportion of the products manufactured outside the Community in the total value of the manufactured products constituting the tender exceeds 50 percent." Under the new rule, the origin of a bid is determined by comparing the total value of the component products that are of EC origin with the total value of non-EC-origin component products. The origin of each component of the bid is determined by the last substantial transformation rule. The effect of this change is that the service component will no longer be considered in determining the origin of a bid. The directive also requires that software used in telecommunications equipment be considered a manufactured product rather than a service, so that software will continue to contribute to the determination of origin.⁹

Finally, the original directive provided that the treatment of non-EC-origin bids could be adjusted through bilateral or multilateral negotiations with third countries to secure equivalent treatment. The common position strengthens this linkage by requiring that the EC Commission submit an annual report to the Council (beginning in the second half of 1991) outlining the progress of such negotiations towards an agreement "ensuring comparable and effective access" for EC firms to third-country markets and outlining the implementation of all such agreements that have been concluded. Based on the developments reported, the EC Council can amend article 29 and extend the benefits of the directive to third countries.

Small and Medium-Sized Enterprises

In a communication¹⁰ issued this spring, the EC Commission outlined methods to increase the participation of small and medium-sized enterprises (SMEs) in public procurement markets. Currently, firms employing fewer than 500 people represent about 70 percent of employment in the manufacturing and service sectors, whereas their participation in public contracts reaches at best only 30 percent of the total value of contracts awarded in a member state. Moreover, the EC Commission is concerned that SMEs may not benefit from the directives liberalizing public procurement because of a perceived increased administrative burden resulting from the new rules and intensified competition from larger and perhaps nonnational suppliers. As a result, the EC Commission proposed a number of initiatives to enhance the participation of SMEs in public procurement contracts without imposing higher costs on the purchaser or discriminating against larger enterprises. The EC

⁹ In the original directive, software was considered in determining the origin of a bid. Because the common position excluded services from the origin rule, software was reclassified as a manufactured product so that it will continue to be covered.

¹⁰ EC Commission, *Promoting SME Participation in Public Procurement in the Community*, Communication from the Commission to the Council, Com (90) 166, May 7, 1990.

Commission intends to maintain close contact with the member states and other interested parties to ensure that these goals are met.

The EC Commission proposed three major categories of measures to aid SMEs after dismissing measures that directly discriminate in favor of SMEs and that may infringe EC law. The first group of initiatives are aimed at facilitating access of SMEs to award procedures for public contracts. Under this category, the EC Commission proposes that member states ensure the following:

- that the new public procurement directives are observed;
- that contracting authorities move beyond the minimum requirements established in the directives, such as circulating tender information beyond the minimum advertising requirements;
- that the scale of individual public procurements be adapted to the productive capacity of SMEs, such as dividing larger contracts into lots or promoting forms of association and cooperation among SMEs to reach a scale appropriate to participation in public contracts;
- that unreasonable or unnecessary requirements of qualification be eliminated; and
- that member states encourage subcontracting of work from large contracts.

In order to ensure that the administrative and financial costs imposed by complex public procurement procedures are minimized for SMEs, the EC Commission proposes several measures. These proposals include simplifying procurement procedures with particular emphasis on ensuring that the procedures for small contracts are as straightforward and transparent as possible, providing electronic mailboxes for quick communication of bidding information in order to decrease costs and delays, and minimizing delays in payments to contractors for work already done. The EC Commission is also seeking ways to encourage SME involvement in public contracts by ensuring that contracting entities will not view SMEs as relatively large-risk suppliers in terms of meeting contract requirements.

Finally, the EC Commission outlines several methods to prepare SMEs for effective participation in contract-award procedures. These measures concentrate on improving the dissemination of basic market information and providing training and technical support on procurement procedures and the legal aspects of public contracts. In this regard, the EC Commission advocates more accelerated use of electronic bidding information services and public procurement databases, such as the "Tenders Electronic Daily" (TED) database, which lists all information on tenders published in the *Official Journal*. The EC Commission also notes

the importance of expanding Euro Info Centers to aid SMEs in responding to tenders and fairs and conferences, which may match SME suppliers with procuring entities.

Possible Effects

General

U.S. suppliers remain generally optimistic over the long-run impact of the EC program to open public procurement. However, they also agree that short-run effects are likely to be small due to entrenched attitudes supporting national champions.¹¹ The U.S. telecommunications industry believes that nationalism and historic traditions—including the managed environment of the EC telecommunications market and the history of low, stable bilateral trade flows in telecommunications—will prompt little improvement in U.S. trade with the EC.¹² Moreover, three of the member states—Spain, Portugal, and Greece—are not required to implement most of the EC's public procurement directives for periods ranging from 3 to 5 years after they enter into force in the other member states.

Enforcement of EC directives will remain critical to ensuring greater competition in the EC's public procurement markets. In 1989, the EC Commission introduced a system for monitoring compliance with public procurement rules of projects executed with assistance from the EC's structural funds. According to EC officials, contracting entities have been more "careful" and "liberal" in the award of public contracts as a result of this monitoring mechanism. To ensure compliance, the EC Commission reviews tender notices and member states ensure that information on tender notices published in national publications also appears in comparable form in EC publications.¹³

However, reports are mixed over the effect of the directives—either in force or anticipated—on procurement practices. Evidence indicates that cross-border contracts have been awarded, such as a West German company's contract to build the Marseille metro.¹⁴ However, many regional and local procuring entities have resisted market opening. "To date, for example, most of the County Councils of the United Kingdom, the Departments in France, and the Laender in Germany have ignored the Community publishing requirements."¹⁵

¹¹ For a further explanation, see USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, and USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990.

¹² U.S. International Trade Commission hearing, *Statement by Edwin B. Spievack, President, North American Telecommunications Association*, June 21, 1990.

¹³ EC Commission official, interview by USITC staff, Brussels, July 19, 1990.

¹⁴ National Association of Manufacturers, *Update on EC-92*, April 1990, p. 21.

¹⁵ EC Committee of the American Chamber of Commerce, *Business Guide to EC Initiatives*, Spring 1990, p. 70.

Concern among U.S. suppliers over the EC's public procurement initiatives remains focused on the Excluded-Sectors Directive. According to U.S. companies, both the 50-percent-content rule and the 3-percent price preference for EC-origin products under the Excluded-Sectors Directive would have a negative impact on third-country participation in the EC's public contracts.¹⁶ Suppliers argue that these rules would "interfere with the most efficient functioning of the market" and create unnecessary administrative workloads. The 50-percent-content rule would increase investment flows to the EC and could stimulate an "unbundling" of procurement package bids as firms seek to meet local-content requirements in some areas while avoiding other areas where content requirements are difficult to meet.¹⁷ Even if U.S. suppliers are no worse off than before, it is possible that more open public procurement within the EC will improve the status of Community companies relative to U.S. firms. Some U.S. companies strongly recommend strengthening the GATT Code on Government Procurement because most of their concerns stemming from the directive would be accommodated by code coverage of the excluded sectors.¹⁸

The impact on U.S. suppliers of the new rule of origin introduced in the common position remains unclear. The new rule does not allow services, including the value of research and development, to be considered in determining the origin of a bid. For this reason, some firms may be hurt by the change if they perform services in the EC. On the other hand, some U.S. suppliers argued earlier that the method for calculating local content in the original directive would have negative repercussions. These U.S. firms objected to the old origin rule because it was not clearly defined. "The process of defining local content creates an ever increasing and costly administrative and operational burden for business given today's trend toward global sourcing."¹⁹ Also, the old method could force U.S. firms to increase research and development projects in the EC.

The impact of the status of software in the determination of origin is also unclear. The common position classified software as a manufactured product so that it will continue to be considered in the origin determination. Firms using U.S.-origin software could be affected depending on how the last substantial transformation rule is applied and how large a component of the bid the software represents.

¹⁶ For a further explanation, see USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, and USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990.

¹⁷ U.S. International Trade Commission hearing, *Statement of the United States Council for International Business on the European Commission's Draft Directives on Public Procurement*, May 22, 1989.

¹⁸ *Ibid.*

¹⁹ *Ibid.*

The EC Commission has indicated that the higher thresholds for supplies contracts introduced in the common position should have no real impact on the total value of contracts covered by the directive. EC Commission officials believe that in telecommunications as well as other sectors, the majority of supplies contracts will fall above threshold levels.²⁰

Recent Studies

A recent study by Robert Lipsey²¹ of the trends in U.S. investment in the EC identifies the public procurement sector as one area showing the strongest signs of increased investment in the Community. Lipsey finds in general little evidence of a large shift in plant and equipment expenditures, employment, or financial investment toward the EC by U.S. companies. "The strongest signs of increased fixed investment in the EC so far are not in manufacturing but in wholesale trade, finance except banking, and in the 'other industries' group." The last category includes such public sector industries as mining, construction, public utilities, and transportation. He also claims that survey results indicating a relatively high proportion of firms wishing to participate in joint ventures rather than acquisitions or mergers could reflect a desire by firms to enter markets dominated by public procurement.

Another study,²² which analyzes the recent restructuring of the powerplant equipment industry in Europe, tries to isolate the effect of the EC 92 program on the formation of cross-border alliances. Evidence shows that until 1987, the rationalization of the heavy electrical industry had mostly occurred within national boundaries, but subsequently there has been a wave of international mergers and takeovers. For example, General Electric has embarked on various cooperative ventures in Europe. The paper cites arguments that the Excluded-Sectors Directive is superfluous because it was designed to encourage a process that is already under way. However, the authors conclude that the prospect of "forced rationalization on suppliers" from more open public procurement markets after 1992 as well as concerns of a "Fortress Europe" among non-EC-based companies undoubtedly contributed to firms' decisions to seek new partners. They argue that the directive will play an important role in liberalizing public procurement markets and that the EC Commission must now concentrate on enforcing the directive for all suppliers and on monitoring the consequences of increased industry concentration. Indeed,

²⁰ EC Commission official, interview by USITC staff, Brussels, July 19, 1990.

²¹ Robert E. Lipsey, "American Firms Face Europe: 1992," National Bureau of Economic Research, Inc., working paper No. 3293, March 1990.

²² Francis McGowan and Stephen Thomas, "Restructuring in the Power-Plant Equipment Industry," *The World Economy*, vol. 12, No. 4, December 1989, pp. 539-556.

others²³ have warned that increased concentration could result in the replacement of national champions with powerful EC champions. "Open procurement may not add to competition. Instead, governments will face larger and more politically powerful suppliers, with fewer real alternative sources of supply than before."²⁴

The Internal Energy Market

Background and Anticipated Changes

The period January-June 1990 saw no new proposed directives under the internal energy market program, although those four directives and regulations proposed previously progressed through the EC's decisionmaking process.²⁵ During this period, the European Parliament completed its first reading of the four measures, which cover the transparency of gas and electricity prices, notification of investment projects of Community interest to the EC Commission, the transit of electricity through transmission grids, and the transit of natural gas through the major systems. Because the measures on price transparency as well as investment projects are subject to the EC's consultation procedure, rather than the cooperation procedure under which White Paper directives in general fall, they are referred to the Parliament only once. On June 29, the Council adopted the directive on price transparency²⁶ and approved a common position on the directive on electricity transit.²⁷

In its opinion on the directive addressing the transparency of gas and electricity prices, the Parliament called for the transparency requirements under the directive to allow comparisons with other sources of energy (such as coal and oil) and to extend beyond sales to industrial users to medium- and large-scale users, including large commercial or administrative buildings and domestic consumers.²⁸ Amendments also called for more emphasis on transparency and less emphasis to be placed on assurances of confidentiality "in view of the implications for other sectors and the taxpayer."²⁹ Parliamentary debate over covering cost transparency in the directive prompted the EC Commission to respond that the need for better

²³ "Europe's Companies After 1992," *The Economist*, June 9, 1990, p. 18.

²⁴ *Ibid*

²⁵ For a full description of these directives and regulations, see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 4-7 to 4-12.

²⁶ EC Commission official, interview by USITC staff, Brussels, July 19, 1990.

²⁷ The EC Committee of the American Chamber of Commerce in Belgium, informal communication with USITC staff, July 10, 1990.

²⁸ "Energy: European Parliament Adopts Reports on Electricity Transit, Energy Investment and Price Transparency," *European Report*, No. 1578 (Apr. 7, 1990), sec. 4, p. 2.

²⁹ "European Parliament Plenary Session, Strasbourg, Apr. 2-6, 1990," *European Report*, No. 1583, supplement (May 3, 1990), p. 5.

information on costs would be examined in a future "communication from the Commission."³⁰

The European Parliament approved the EC Commission's proposals for a draft regulation on investment projects with several amendments designed to strengthen the measure. These amendments called for the earlier notification of project details to the EC Commission to facilitate adjustments, as well as for greater attention to environmental concerns and energy conservation. Parliament's amendments to the draft directive on the transit of electricity concentrated on the importance of environmental factors, the involvement of operators and owners of small grids, and links with third countries such as Austria and Switzerland.³¹ The amendments proposed by the Parliament on the Gas Transit Directive focused on deleting references to the directive as a first step in applying the common carriage principle to the gas sector.³² Common carriage refers to the ability of third parties to access existing transportation networks on payment of a reasonable tariff.

On June 29, the EC Council adopted the directive on price transparency. As the directive now stands, gas and electricity producers will submit to the EC's Statistical Office (SOEC) biannual data on the prices they charge to industrial end users, broken down by consumer category rather than individual companies, beginning January 1, 1991.³³

On June 29, the EC Council approved a common position on the draft directive on the transit of electricity. The common position incorporates several changes from the directive as it was originally proposed. First, the common position introduces a conciliation procedure to facilitate the conclusion of transit contracts. The results of such a procedure will not be legally binding. The common position also deletes language that directly linked the directive to future analysis of the application of the common carriage principle to electricity. Finally, the revised directive addresses environmental concerns and now covers transit

³⁰ "European Parliament Plenary Session, Strasbourg, May 14-18, 1990," *European Report*, No. 1594, supplement (June 13, 1990), p. 4. The EC Commission also indicated that in early 1991 it would "be drawing up a regulation to provide information on the costs of producing or acquiring energy and measures to harmonize the principles of passing on costs in prices." See EC Commission, *The Internal Energy Market*, Com (90) 1245, May 18, 1990, p. 18.

³¹ "Energy: European Parliament Adopts Reports on Electricity Transit, Energy Investment and Price Transparency," *European Report*, No. 1578 (Apr. 7, 1990) sec. 4, p. 2.

³² "Energy: CERT Committee Finally Adopts Compromise Amendments on Gas Transit," *European Report*, No. 1597 (June 20, 1990) sec. 4, p. 1.

³³ *Council Directive Concerning a Community Procedure to Improve the Transparency of Gas and Electricity Prices Charged to Industrial End Users*, *Official Journal of the European Communities*, No. L 185 (July 17, 1990), pp. 16-24; and Bureau of National Affairs (BNA), "Energy: Transparency, Transit Rules Get Green Light From Council," 1992: *The External Impact of European Unification*, June 1, 1990, pp. 4-5.

with third countries "when the grid of origin or final destination is situated in the Community."³⁴

The EC Council has not yet responded to the Parliament's opinion on the draft directive covering the transit of natural gas through the major systems. This directive remains fairly controversial for two reasons. Certain member states, particularly West Germany, question the directive's justification because they feel competition already exists.³⁵ Also, member states fear any steps that could move the EC closer to common carriage.³⁶

In addition, the Council did not vote on the controversial regulation covering notification of investment projects of Community interest to the EC Commission. Member states strongly oppose this regulation because they feel it creates unnecessary bureaucratic intervention in investment planning.³⁷ The EC Commission hopes that progress on electricity transit could lead to a less bureaucratic alternative to the regulation to promote EC cooperation on investment.³⁸

Thermie

Another important development in the internal energy market was the adoption by the EC Council on June 29 of the 5-year Thermie program. The aim of this program is to encourage research and development of new and renewable sources of energy, with particular emphasis on increasing energy efficiency and reducing the harmful effects of certain fuels on the environment. The program was originally intended to enter into effect on January 1, 1990, but disagreement over the budget delayed adoption of the program. In order to ensure that some work be accomplished under Thermie during 1990, the EC Commission in March called for project proposals to be submitted by June 20. The types of projects that the EC Commission is seeking are those that advance or implement innovative technologies in the energy field by promoting new applications of established processes or the broader use of innovative technologies. They must meet safety and environment standards and include viable methods for subsequent commercial exploitation. Generally, these projects require EC support because they have substantial technical

³⁴ European Communities, The Council, *Common Position Adopted by the Council on 29 VI 1990 With a View to Adopting a Directive on the Transit of Electricity Through Transmission Grids*, June 29, 1990.

³⁵ "Energy Council: May 21 Session to Focus on Internal Market Directives and Thermie," *European Report*, No. 1586 (May 10, 1990), sec. 4, pp. 7-8.

³⁶ "Energy: European Parliament Committee Gas Hearing Focuses on Transit," *European Report*, No. 1580 (Apr. 20, 1990), sec. 4, p. 4.

³⁷ "Energy Council: May 21 Session to Focus on Internal Market Directives and Thermie," sec. 4, pp. 7-8.

³⁸ "Energy Council: First Steps on the Road to an Internal Energy Market," *European Report*, No. 1589 (May 22, 1990), sec. 4, p. 4. It is anticipated that the investment regulation will be substantially changed. Reportedly, discussions have been postponed for up to 2 years. USEC official, interview by USITC staff, Brussels, July 19, 1990.

or economic risk attached to them. The EC Commission will finance up to 40 percent of innovative projects and 35 percent of dissemination projects. In general, proposals that cost over 6 million ECU must be submitted by two promoters from different countries.³⁹

Security of Energy Supplies

A communication approved by the EC Commission on July 4 proposes a strategy for enhancing the security of energy supplies for the Community as a whole. Presently, member states ensure the security of energy resources at the national level through generous state aids, which often prevent free trade in energy products. The EC Commission aims to minimize national intervention and increase member-state interdependence of energy supplies in order to create more competition and lessen the EC's dependence on imported energy supplies. In 1989, imported energy supplies represented about 49 percent of EC energy requirements.⁴⁰ This strategy represents an important step away from national energy policies, including subsidies, towards the creation of a true internal energy market.⁴¹

Progress Report

In May, the EC Commission issued its first progress report on the internal energy market.⁴² This report was mandated in a communication issued in May 1988 that listed obstacles to a unified energy market and presented a framework for action to eliminate the obstacles.⁴³ The report cited progress in harmonizing standards, liberalizing public procurement, applying EC laws to increase competition, and reducing price opacity and market compartmentalization in the energy field. The EC Commission also cited its priorities to stimulate competition while maintaining security of energy supplies.

The EC Commission does not anticipate any new directives in the energy field. In addition to the three measures that remain pending, the EC Commission plans to concentrate on implementing the Thermie program and addressing the issues of the environment and the security of supply and energy.⁴⁴

³⁹ "Energy: Commission Calls for Projects Within Thermie Programme," *European Report*, No. 1576 (Mar. 29, 1990), sec. 4, p. 6.

⁴⁰ "Energy: European Commission Adopts Communication on Security of Supply," *European Report*, No. 1601 (July 5, 1990), sec. 4, p. 3.

⁴¹ The EC Committee of the American Chamber of Commerce in Belgium, informal communication with USITC staff, July 10, 1990.

⁴² EC Commission, *The Internal Energy Market: First Progress Report*, Com (90) 124, May 18, 1990.

⁴³ EC Commission, *The Internal Energy Market*, Com (88) 238, May 2, 1989. For more information on this document, see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, ch. 4.

⁴⁴ U.S. Department of Energy, telephone conversation with USITC staff, Washington, DC, July 10, 1990.

Possible Effects

Both U.S. companies supplying coal and energy equipment, as well as U.S. firms operating in the EC should benefit from the internal energy market program.⁴⁵ The creation of an internal energy market is likely to increase competition among energy suppliers and cause restructuring of the energy sector. The more competitive environment will likely permit more suppliers of energy and energy equipment from third countries to participate in the market and will lower operating expenses for all firms established in the EC. The prospects for U.S. sales of coal to the Community are particularly positive, especially if the EC maintains pressure on the member states to eliminate subsidies to the coal industry.⁴⁶

⁴⁵ For more information about possible effects, see USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, pp. 4-31 to 4-35.

⁴⁶ U.S. Department of Energy, telephone conversation with USITC staff, Washington, DC, July 10, 1990.

CHAPTER 7
CUSTOMS CONTROLS

CONTENTS

	<i>Page</i>
Developments covered in previous reports	7-3
Background and anticipated changes	7-3
Possible effects	7-3
Developments in 1990	7-3
Free movement of goods	7-3
Background and anticipated changes	7-3
The proposed Common Customs Code	7-4
Objectives	7-4
Title I	7-4
Title II	7-5
Titles III and IV	7-5
Title V	7-5
Title VI	7-6
Titles VII and VIII	7-6
Other measures	7-6
Temporary importations	7-6
Release for free circulation	7-7
Tax-paid allowances	7-7
Statistics on trade among member states	7-7
Statistical classification of economic activities	7-7
Possible effects	7-7
Free movement of persons	7-7
Background and anticipated changes	7-8
Social benefits	7-8
Freedom of establishment	7-8
New Community policies	7-8
Recent developments	7-8
Residence	7-9
Training	7-10
Professional qualifications	7-10
Possible effects	7-10

CHAPTER 7

CUSTOMS CONTROLS

Among the principal goals of the 1992 process is the abolition of border controls within the EC, so that persons, goods, services, and capital may at last move freely among the member states. During the transition period ending at the close of 1992, measures to simplify most frontier procedures and to eliminate others will apply. Controls at external boundaries will be strengthened based upon developing common policies. By 1993, with new statistical programs and tax collection mechanisms in place, all customs formalities at internal borders will end.

Developments Covered in Previous Reports

In previous reports, this chapter covered three categories of directives: those aimed at achieving the free movement of goods, those dealing with the free movement of persons and the mutual recognition of their professional qualifications, and those trying to ensure safe and healthful workplaces. Earlier activities in all three areas will be summarized here, but current developments as to the last category of directives will be discussed in the related chapter concerning the social dimension of integration.

Background and Anticipated Changes

To permit firms in the EC to operate with the greatest economies and competitive advantages, the 1992 program must attain free movement across internal frontiers with the absolute minimum of regulation and interference. Traditional customs checks at these border crossings, together with the collection of taxes and statistics, are to be replaced with other devices for achieving the same level of revenue, information, and control previously available to the member states. Persons and goods from outside the European Community will be subject to customs and immigration procedures at their initial entry into a member state and thereafter (assuming compliance with other provisions of law) will be able to circulate freely through the Community. Significant savings in costs and time should be achieved as frontier formalities are abolished. However, before these measures are made fully effective, it is essential that agreement be reached on tax rate and collection directives. Moreover, the EC Commission has proposed that a common customs code (discussed below) be adopted in the Community to compile the many applicable regulations and directives in a single document. The code, if adopted in the form of a regulation, would take effect in 1993.

If the EC Commission's proposals are accepted, EC residents and nationals will be able to live and work in any member state, and restrictive residence

rules as to nonworkers will be prohibited. During the first stage, vocational and professional qualifications obtained in one member state must be mutually recognized in the others. Holders of such credentials will be able to work in other member states on the same terms as nationals of those member states. Training curricula and professional requirements, and to a lesser extent social benefit programs, are being developed along common lines and may eventually be standardized throughout the EC.

As firms establish operations in new locations throughout the EC, they will be required to meet uniform, general requirements concerning the health and safety of their employees. Personal protective devices, training on their appropriate use and on other safety matters, notification of particular hazards (such as the use of certain substances), and elimination of specified dangerous conditions will be required at all places of work. Moreover, persons performing routine or strenuous tasks will be assured of proper equipment, rest periods, training, and medical reviews. These directives will grant considerably more authority to EC institutions than they had before to ensure the development and implementation of a single set of minimum standards throughout the EC.

Possible Effects

As stated in previous reports, these directives should benefit U.S. business operating in or exporting to the EC. Such firms should experience lower costs and considerably reduced delays in moving goods through the Community, and they will obtain added flexibility in hiring and transferring workers in the EC. It is believed that most U.S. entities already comply with the proposed and enacted directives on workplace safety and so are not likely to require large expenditures. Some firms may need to adopt additional procedures for worker notification and involvement, with accompanying costs. None of these directives discriminates by country and all appear trade neutral, so that little diversion of exports to the U.S. market is expected. U.S. business investment in the EC would not seem likely to be affected solely by these measures. It should be noted that other EC directives and trade policies (especially those not commonly included as a part of the integration program) may have a greater impact on U.S. interests.

Developments In 1990

Free Movement of Goods

Background and Anticipated Changes

Many of the measures needed to achieve the free movement of goods in the internal market have already been adopted, and almost all of the remainder have been presented by the EC

Commission in the form of proposals or amended proposals. Some of these pending directives have already been the subject of additional amendments by the European Parliament; others await action on directives discussed in other chapters of this or previous reports. In any event, most recent changes constitute refinements rather than extensive revisions or additions.

The Proposed Common Customs Code

Perhaps the most significant measure recently presented by the EC Commission—one long included in its work program but not in the so-called 1992 process—is the proposed regulation to establish a Community Customs Code. The draft document was published along with a proposed regulation dealing with temporary importations and their exclusion from duties.¹ Because the code would replace both currently effective directives and proposed measures, its major provisions are outlined here. However, a detailed legal comparison of the entire code (which runs for approximately 200 pages) with existing regulations, and with proposed or adopted measures discussed in previous reports in this study, is beyond the current scope of this chapter.

Objectives

In its explanatory memorandum, the EC Commission states that with this proposal it is “launching the most far-reaching project of legislative consolidation ever undertaken in a field subject to Community law.” The code is described as following the pattern in some member states of consolidating all provisions relating to trade in a single compilation (rather than rewriting them entirely). The code is designed to serve as the basis for a long-term customs harmonization program; that is, its general and uniform provisions will control the narrower, interpretative procedures and rules of the member states and lead to uniformity therein. It would replace over two dozen separate directives, some adopted over 10 years ago and many amended on numerous occasions (requiring that the documents be amassed and interpreted by the user). Effective as of January 1, 1993 (if adopted), the code would apply to trade between the EC and third countries, because of the elimination of customs procedures for trade between member states. The EC Commission stated in the explanatory memorandum that some amendments to existing EC law would be accomplished by the code,² but added that most of the provisions are already in place in separate legal instruments.

Of chief significance, according to the explanatory memorandum, is the procedure for the

¹ Com(90) 71 final, published as a separate issue of the *Office Journal of the European Communities* on Feb. 28, 1990.

² For example, the free circulation provisions have been revised, as have procedures for determining the tariff classification of goods.

release for free circulation of goods from third countries. This concept, linked to article 10 of the EEC Treaty, is basic to achieving a true customs union. Under this procedure, in the internal market, foreign goods will be allowed to move freely in the EC without customs formalities after the importers establish that all legal requirements have been satisfied.³ Seven other customs procedures are covered in detail in the proposed code,⁴ and a new Customs Code Committee would be set up to maintain close cooperation among the member states and with the EC Commission. In addition, article 7 provides persons with the right to request decisions⁵ by customs authorities on the application of customs laws and requires that such decisions generally be issued within 3 months of the request. Other articles provide for the enforcement, annulment, and revocation of such decisions.

The preamble to the proposed regulation notes that the code “is applicable without prejudice to specific provisions laid down in other fields” such as agriculture, commercial policy, or other areas. It also recognized that “the application of customs legislation is economic in character” and that “the charging of import duties must consequently be linked, in general, to the integration of imported goods into the Community economy.” The scope of the code is further delineated in article 1:1, which includes the statement that “National law shall apply only in so far as Community law so provides.” The code would apply uniformly throughout the EC, except in cases specifically provided by conventions and certain autonomous EC measures.

Title I

After setting forth the limits of the customs territory of the EC, allowing for the separate arrangement for German internal trade, and defining many terms, general provisions outlining the rights and obligations of persons are set forth. These involve the right of representation in dealings with customs authorities, the right to and effect of decisions from customs authorities as to the treatment of goods, the right of interested persons to obtain information on the application of customs laws, and documentation requirements. Article 19 would provide that the value of the ECU in each country's currency would be determined annually, unless enumerated special circumstances arise.

Title II

Title II of the code would provide for the imposition of import and export duties and the

³ A similar procedure already exists, but the continued existence of internal customs formalities has meant that such goods are subject to checks and delays when shipped across member-state borders.

⁴ They are transit through the EC, customs warehousing, inward processing, processing under customs control, temporary admission, outward processing, and exportation. Article 5:16.

⁵ These decisions parallel the binding rulings which may be obtained from and “interested party” petitions which may be filed with the U.S. Customs Service.

application of related trade measures. Article 20 describes the EC's customs tariff, rules for the classification of goods,⁶ and the preferential duty arrangements of the EC. Articles 22 through 27 would establish rules on the determination of the country of origin of imported merchandise, and provide for the continuation of existing and agreed measures adopted under preferential tariff schemes. They do not appear to make significant changes in existing measures or in those resulting from the 1992 process. Chapter 3 (arts. 28 through 36) would cover the valuation of imported goods for customs purposes, representing the implementation of the EC's obligations under the Customs Valuation Code.⁷

Titles III and IV

Title III would provide procedures for the entry, unloading, and presentation of goods; the assignment of the use or treatment of the goods; temporary warehousing; and the Community transit procedure. Next, title IV would set forth in detail the methods for assigning the "customs-approved treatment or use" of imported goods, which may dictate the goods' classification or their duty or quota treatment. Article 56 would preserve the EC's right to impose future restrictions or prohibitions on importation and use based on grounds of "public morality, public policy or public security, the protection of health and life of humans, animals or plants, the protection of national treasures possessing artistic, historic or archaeological value or the protection of industrial and commercial property."

Chapter 2 of title IV would specify how goods are to be placed under one of the eight customs procedures enumerated above under the "normal" method and also under the "simplified" manner (based on the number and types of documents submitted in relation to a shipment). It would also authorize and regulate customs officials' examination of imported goods. Section 2 of the chapter would comprise the articles outlining the procedure for release for free circulation, succinctly stated in article 78: "Release for free circulation shall confer on non-Community goods the customs status of Community goods."⁸

The group of "conditional relief procedures," allowing entry in controlled circumstances without

payment of duties, would be covered in section 3.⁹ Unusual among them is the "external Community transit" procedure, covering goods leaving the EC for other countries and returning or reentering. While useful generally, the procedure is necessitated by the geographic separation of Greece. Also notable is the "inward processing" procedure, under which imports are relieved of duties on entry provided that they are processed in the EC into "compensating products" for export. Finally, external processing (occurring outside the EC where the output is to be entered into the EC) and drawback are also the subject of specific provisions.

Articles 135 through 143 would treat temporary importations and the means of obtaining the payment of duties where the goods are subsequently placed under a [dutyable status] procedure. Subsequent provisions would deal with outward processing arrangements, the export of goods, and the EC's internal transit procedure (similar to the U.S. procedure for transportation under bond and customs seal). Free zones and free warehouses would be handled in articles 164 through 179. Article 180 would dictate procedures for reexportation, destruction, or abandonment of non-Community goods.

Title V

Title V would cover "privileged operations," among them article 181's authorization for reliefs from customs duties (including what are known in U.S. law as temporary duty suspension measures):

The Council shall, acting by a qualified majority on a proposal from the [EC] Commission, determine the cases in which, on account of special circumstances, relief from import duties or export duties shall be granted where goods are released for free circulation or exported.

No elaboration on the type or extent of the "special circumstances" is provided; it may be assumed that unavailability of EC-produced goods might be a justification for relief from duties, as is presently the case. This title also treats the status of returned goods and products of the deep seas.

Title VI

Title VI would establish the treatment of customs debt, including appropriate security and the persons liable for payment of particular debts.¹⁰

⁶ A separate proposal for a regulation on information provided by the customs authorities of member states on the classification of goods in the customs (tariff) nomenclature, cited in the first followup report, was amended by the European Parliament. The changes would accelerate entry into force to Jan. 1, 1992, make rulings binding on member-state customs officials, and provide greater administrative guidance. OJ No. C 113 (May 7, 1990), p. 71.

⁷ Agreement on Implementation of Article VII of the GATT, 1979.

⁸ Proposed Council Regulation Com(89) 385 final, OJ No. C 235 (Sept. 13, 1989), p. 16, discussed in U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States - First Follow-up Report* (Investigation No. 332-267), USITC Publication 2268, March 1990) p. 7-6, footnote 24.

⁹ Most of these procedures have already been applied to goods entering the EC, but they will operate to their fullest extent once the single market is implemented and internal controls are eliminated. Technical and conforming changes may be included to update present provisions.

¹⁰ These provisions would incorporate in the code the recently adopted Council Regulation on the security to be given to ensure payment of a customs debt (Regulation (EEC) 4046/89, OJ No. L 388 (Dec. 30, 1989), p. 24) and the proposed regulation determining the persons liable for payment of a customs debt (proposed Council Regulation Com(89) 214, OJ No. C 142 (June 8, 1989), p. 5), discussed in the second report. Also see Decision of the European Parliament on the common position drawn up by the Council on the latter proposal, OJ No. C. 96 (Apr. 17, 1990), p. 81.

Specifically, imported goods liable to import duties and released for free circulation, goods partially relieved of duties under a temporary importation procedure, goods unlawfully introduced (smuggled) into the EC (directly or from a free zone or free warehouse) or removed from other customs supervision, and goods as to which conditions established by customs officials upon entry remain unsatisfied (including conditions of use) would all give rise to customs debt. Goods being exported would give rise to customs debt where covered by export duty provisions, exported without proper declarations or without payment of all import duties, and exported after established time limits. In most cases, the declarant or the person who took the specified action with respect to the goods would be held liable for payment; joint and several liability would be provided where several persons are involved in filings as to a shipment. Procedures for collection and applicable time limits for payment would be indicated, as well as the authority of customs officials to grant a 30-day deferral of payment in particular situations. Last, several articles would relate to the extinction of customs debt and the repayment and remission of duties.

Titles VII and VIII

Title VII would set forth for the first time EC-wide formal procedures for the appeal of customs rulings (encompassing what are known in U.S. law as protests as well as other matters). The right to appeal, procedures and time limits, scope of appeal, "fresh" appeals where an initial appeal is rejected to any extent or results in decisions less favorable than the initial one, and other provisions (including the entities to which appeals are to be brought) would be covered in detail.

Finally, title VIII on "final provisions" would create the Customs Code Committee and outline its powers and procedures. It would also specify the "legal effects in a member state of measures taken, documents issued and findings made in another member state." Earlier and conflicting measures encompassed by the code would be repealed in article 257.

Other Measures

Temporary Importations

The accompanying proposed regulation¹¹ on "determining the cases and the special conditions under which the temporary importation arrangements may be used with total relief from import duties" would be implemented under the terms of article 139 of the code, once the latter is adopted. It would restate in one document the

criteria set forth in three earlier regulations on containers, means of transport, and temporary arrangements generally.

The provisions of the proposed measure may be summarized as follows. Generally applicable definitions are contained in article 1 of the proposal. Means of transport would be covered by articles 2 through 11; the first of these would specify that no guarantee (bond or other security) to ensure payment of any subsequent customs debt would be required when means of transport are placed under this procedure. Provisions for the treatment of parts and accessories and for the control of access to the means of transport would be set forth in articles 2 and 3, respectively. Articles 6 through 11 would cover distinct requirements for means of road, rail, air, and sea and inland waterway transport. These criteria would deal with permitted uses of such transport in the EC, the time limits on the period of temporary importation, and related matters. Article 12 would extend the temporary importation procedures to pallets and article 13 to containers.

The remaining substantive provisions of the regulation would relate to temporary importations of goods, including professional equipment (arts. 14 and 15), goods for displays or fairs (art. 16), teaching aids and scientific equipment (arts. 17 and 18), medical equipment (art. 19), "materials for use in countering the effects of disasters" (art. 20), packings (art. 21), and other situations (arts. 22 to 30). The latter would include a wide range of articles, including art, animals, personal effects, auditory and visual materials, used goods, and goods to be tested or sold. The regulation, if approved, would also be effective as of January 1, 1993.

Release for Free Circulation

In a very short proposal, for a directive amending Directive 79/695/EEC on the harmonization of procedures for the release of goods for free circulation, the EC Commission's suggested language was amended by the European Parliament.¹² The EC Commission would have given member-state authorities the discretion to allow the importation without customs entry of goods of low value or goods imported for noncommercial purposes, with two provisos.¹³ First, consignments sent by parcel or letter post could still be separately treated in special measures. Second, the exemption from filing entry documents would not be given in cases where an import license is required. As amended by the Parliament, the proposed directive would require member-state authorities to exempt the same two classes of goods from entry requirements, instead of permitting member-state governments to do so.

¹² Proposed directive Com(89) 385 final, OJ No. C 235 (Sept. 13, 1989), p. 16. See brief discussion of proposal in USITC *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 7-6, note 24.

¹³ See OJ No. C 54 (Mar. 6, 1990), p. 14 for EC Commission's proposal.

¹¹ Published in the same special issue of the OJ with the code, the regulation has not been assigned a designating number.

On the same proposed directive, the Council had sought the opinion of the Economic and Social Committee, and a document was prepared by the Committee's Section for Industry Commerce, Crafts and Services.¹⁴ The opinion set forth the committee's endorsement of the directive, saying that it was designed to simplify procedures and to place all imported goods on an equal footing. The committee noted the economic importance of the procedure for release for free circulation, stated that importing firms and customs authorities needed agreed rules, and asked that the directive be extended to cover exports as well. In addition, the committee recognized that simplified entry procedures, while helpful to importing firms, often cause customs administrative and monitoring problems and extra documentation.

Tax-Paid Allowances

Another brief proposal, this one emanating from the EC Commission, would amend an outstanding proposed directive¹⁵ to change the terms of the 1969 directive¹⁶ on tax-paid allowances in intra-Community travel. As drafted, the proposal would merely increase the levels of tax-paid allowances set by the 1969 directive. Under this amended language, if adopted, the limits set by the 1969 measure would initially be increased and, as of January 1, 1993, abolished altogether.

Statistics on Trade Among Member States

On May 17, 1990, the EC Commission submitted an amended proposal for a regulation on statistics covering intra-EC trade in goods.¹⁷ As amended, the document would recognize that new data collection systems could not be introduced until the end of the transition to uniform EC tax arrangements by each member state. Thus, several new articles would outline procedures for the transition period beginning in 1993. The proposal would also eliminate a deadline for the EC Commission to enumerate minimum data to be registered by intra-EC operators.

Statistical Classification of Economic Activities

On June 20, 1990, the Council adopted its "Common Position . . . with a View to the Adoption of a Regulation on the Statistical Classification of Economic Activities in the European Community."¹⁸ The proposed regulation would set up a common statistical classification of all economic activities, in order to ensure comparability between

¹⁴ Adopted by the Economic and Social Committee at the 272nd Plenary Session, Dec. 19, 1989, OJ No. C 62 (Mar. 12, 1990), p. 5.

¹⁵ Com(90) 76 final, OJ No. C 70 (Mar. 20, 1990).

¹⁶ Directive 69/169/EEC established limitations on tax paid allowances for EC nationals and other persons moving across internal frontiers.

¹⁷ OJ No. C 177 (July 18, 1990), p. 14.

¹⁸ Separately published as *restreint 6691/90*, with annex attached. The EC Commission's proposal was published in OJ No. C 58 (Mar. 8, 1990), p. 25.

member-state and EC systems and statistics. This new scheme, based upon the United Nations International Standard Industrial Classification, would not force member states to collect or publish data or specify the units of measurement or degree of detail to be utilized. However, any national statistical system would be required to use the same broad descriptive categories and designators, and could employ narrower categories derived therefrom. The new nomenclature would be required to be incorporated in member-state systems by January 1, 1993.

Possible Effects

To date there is no indication that the assessments in previous reports in this study need be revised. The EC's simplification of customs procedures should have a beneficial impact on all firms (EC and foreign) trading with or in the Community. To the extent that U.S. firms established in the EC may adjust more easily to Communitywide free movement of goods than their European counterparts, such U.S. firms may see their competitive position improve, relative both to their prior performance and their present rivals. Individuals will also benefit, especially tourists, persons who travel in the course of business, persons moving to other member states, and those handling affairs in other member states.¹⁹

One aspect of the internal market may warrant consideration. Small businesses outside the EC would seem likely to experience more difficulties entering the EC market or being fully successful there, despite the elimination of burdensome customs procedures, than large non-EC firms and small EC firms. This situation is largely a function of distance, of higher shipping costs, and of smaller firms' problems in establishing distribution and service schemes in the EC.

Free Movement of Persons

Background and Anticipated Changes

As noted in the first two reports in this study, the effort to achieve free movement of persons²⁰ dates back to the early years of the EC's existence. The concept of free movement is a necessary result of the elimination of customs formalities at internal frontiers, and is viewed as essential to EC firms

¹⁹ See, for example, Written Question No. 721/89 and answer (by Mr. Bangemann on behalf of the EC Commission) thereto on the transport of corpses across frontiers, OJ No. C 117 (May 11, 1990), p. 4; and Written Question No. 386/89 and answer (by Mr. Van Miert on behalf of the EC Commission) thereto concerning setting uniform traffic laws, speed limits, blood alcohol limits, etc., in the EC, OJ No. C 117 (May 11, 1990), p. 4. However, other proposals, such as the suggestion that duty free sales shops be eliminated after 1992, may not be easily accepted by ordinary persons.

²⁰ Originally comprising EC nationals who were working or wanted to work or perform services in a member state other than their own, this term will ultimately refer to EC nationals, their families, their dependents, their servants, and certain other nonnationals (such as persons holding valid temporary residence and/or work permits or student visas).

desiring to achieve maximum economies in the single market. Although the directives in this category directly involve and benefit only EC nationals and their families, they are of interest to U.S. firms operating in the EC and employing EC nationals and are part of the "People's Europe"/social dimension aspects of integration.

Social Benefits

The EC Treaty focused only on freedom of movement for workers and on the right of EC nationals to establish themselves for purposes of work or to perform services in other member states. As a result, while workers came to have the ability to migrate to other member states to seek or perform work, their family members often had to remain behind or could reside in the host state only for limited periods. Obtaining needed social benefits, such as unemployment payments and workmen's compensation, and appropriate pensions was not always easy for the workers, whether from their own country or from other member state.²¹ It was frequently impossible for family members to obtain most social benefits in the host country, and such persons even encountered problems from their own countries in qualifying for some payments. One goal of the integration process is attaining real free movement for persons in the EC and providing the means of eliminating many of the complications inherent in such multicountry work and living circumstances.

Freedom of Establishment

An adjunct area of EC legislative activity arose from the guarantee of the freedom to establish oneself and to perform services in other member states—namely, the idea that differing vocational and professional qualifications had to be deemed sufficient to allow their holders to work in other member states. Following lengthy efforts to harmonize qualifications and training curricula for some areas of work, the EC Commission realized that a more efficient approach would be needed if the 1992 deadline were to be attained. Thus, it proposed a principle of mutual recognition of qualifications in those professions or vocations where harmonization had not yet been achieved and continuing efforts to achieve harmonization, even after 1992. Many of the needed measures in this area have been adopted and implemented.

New Community Policies

A last area of legislative activity has been the attempt to achieve consensus on EC-wide policies

²¹ See Written Question No. 1240/89 and answer (by Mrs. Papandreou on behalf of the EC Commission) thereto on freedom of movement for disabled persons, *OJ No. C 125* (May 21, 1990), p. 46. Two regulations, Nos. 1408/71 and 574/72, apply to disabled workers and state that they are to receive the same treatment as persons of the host country. The Community Charter of Fundamental Social Rights (Com(89) 568 final) indicates that a Commission regulation extending full rights to all disabled persons is forthcoming.

for immigration,²² residence, asylum,²³ narcotics interdiction, gun control, and other security concerns. Achieving similar or identical legal criteria in these areas is seen by many in the EC as essential to the completion of the internal market. The concern is expressed that, if persons are to be able to move freely through the Community, the lack of harmonization might give rise to unwanted population flows as people move to those countries whose policies they find to be more desirable. In addition, a shared legal framework for dealing with security matters and the entry of foreign persons will be needed following the elimination of most customs formalities within the EC.²⁴

Many of these questions are of particular interest at present because of the ongoing process of German integration and the signing of the Schengen Agreement on June 19, 1990. This agreement, representing a more detailed version of a previous pact of the same name, will eliminate nearly all controls among France, the Benelux countries, and the Federal Republic of Germany, creating a miniature single market. Many member-state officials have expressed concern that the social welfare schemes and job markets of their countries could not cope with significant numbers of new immigrants from East Germany, who will, once in West Germany, be entitled to free movement in the internal market and, under the Agreement, to free movement immediately in the signatories (Benelux and France).

Recent Developments

Residence

Among recent measures taken up by EC institutions are two modified proposals, one amending a regulation and the second a directive, on the free movement and residence of EC workers and their families.²⁵ Both were discussed in the second report in this study, but both have been

²² Currently handled outside the EC legal framework by a Conference of Ministers Concerned With Immigration. See Written Question No. 153/90 and answer thereto, *OJ No. C 117* (May 11, 1990), p. 28. To date the member states have handled all matters relating to legal and illegal immigration.

²³ See Written Question No. 911/89 and answer (by Mr. Bangemann on behalf of the EC Commission) thereto, *OJ No. C 117* (May 11, 1990), p. 13. The EC Commission is preparing a draft asylum convention as well as internal instruments on this subject, and is attempting to encourage member states to harmonize their legislation.

²⁴ See Resolution on the free movement of persons in the internal market, adopted by the European Parliament Mar. 15, 1990, *OJ No. C 96* (Apr. 17, 1990), p. 274. Among the concerns enumerated is that the resulting information-sharing networks "must not undermine personal liberties or respect for the private lives of individuals" and the need to guarantee respect for human rights at the Community level as an aspect of police cooperation. The resolution calls for Commission draft proposals to deal with asylum, criminal prosecutions, enforcement of child support payments, and other matters.

²⁵ Both these proposals are designated as Com(90) 108 final and were presented by the EC Commission on Apr. 11, 1990, *OJ No. C 119* (May 15, 1990), pp. 10-14. The proposed regulation was modified with respect to contract employees who are EC nationals and who perform temporary duties in other member states. *OJ No. C 177* (July 18, 1990), p. 40.

rewritten and resubmitted following input from the European Parliament and the Economic and Social Committee. According to the preamble to the first proposal, to amend Regulation (EEC) 1612/68, these changes are necessary to ensure that families can remain together, to take into account recent socioeconomic changes, and to incorporate principles from many rulings by the European Court of Justice.

The proposed regulation would provide that workers from other member states would be guaranteed, on the same terms as workers of the host state, full employment opportunities, training and recruitment assistance, safe and hygienic working conditions, benefits for unemployment and disability, retirement payments, contractual and agency authority (needed if the employer is outside the host country), and the right to have family and dependents live with him, all on the same terms as corresponding host nationals. Workers and their families who leave their own member state would, for legal purposes or for tax or social program purposes, be treated as if they were still in their own member state, retaining their rights as nationals thereof. The member states would be directed to take all necessary measures as to natural and legal persons to ensure that the provisions of the regulations are implemented.

The related proposal, for a regulation amending Directive 68/360/EEC, would modify existing restrictions on movement and residence last updated upon the accession of Spain and Portugal to the EC. According to the preamble, its goal is to simplify residence procedures and to reduce related costs, so that persons will be better able to relocate to areas of the Community that have better employment opportunities. Thus, the regulation would create a European Communities residence card for use by persons wishing to migrate, and would provide for certificates showing unemployed workers qualify for unemployment in both their own and their host member states. Nor would workers outside their own member states be forced to return or move in periods of unemployment; instead, after working in a host state for 3 to 12 months (to be set by the member states, except where a worker establishes eligibility in less than 3 months), a worker could remain there until his eligibility for unemployment expires. The residence cards would be automatically renewed if workers continued to be employed or during periods of incapacity for work (including maternity) and would always be issued free of charge. They could not be demanded at internal frontiers and would be required to be valid for at least 5 years, with renewals for 10 years. Family members would receive such documents on the same terms as their respective worker-members.

Training

Because of the high degree of emphasis being placed on training the labor force of Europe, both to

take advantage of employment opportunities in other member states and to enter new, specialized fields, several programs have been established or proposed in order to provide training and/or funding in different areas. Among the broadest of these would be the European Training Foundation, which was the subject of an amended proposed regulation submitted by the EC Commission on April 20, 1990.²⁶ The foundation would benefit workers in Central and Eastern Europe, beginning in Poland and Hungary. This amended proposal contains several articles which refine or slightly expand provisions of the original proposal—namely, that the foundation would locate opportunities for joint-venture or outside-sponsored projects to train or retrain young persons and adults and would be afforded legal personality to permit its effective functioning. In addition, a new provision would add a committee of 15 experts principally representing the social partners²⁷ and international organizations having to do with training. Another would specifically allow outside representatives of the social partners to be involved in Foundation projects, and a third new article would provide for regular review and evaluation of this work.

As to vocational training within the EC, another amendment, this one to a proposed Council decision adopting a Community action program for developing continuing vocational training was submitted by the EC Commission on April 27, 1990.²⁸ The action program would run throughout calendar years 1991-94 and would support and complement member-state initiatives in vocational training. Other than setting the time period, the amendment would change only the timing and recipients of the future interim and final reports on the program to be completed by the EC Commission. A related proposed amendment advocated by the European Parliament would express the right of access of both employed and unemployed persons to vocational training, and would direct the EC Commission to submit a directive on leave for training.²⁹ It would allow workers to undertake training during work time, and uses the word "workers" to include "the working population, the unemployed and young people, including the self-employed, and women wishing to resume an occupation." The Parliament's changes in the proposed decision would encourage cooperation between industries

²⁶ Com(90) 145 final, OJ No. C 119 (May 15, 1990), p. 15. The original proposal appeared at OJ No. C 86 (Apr. 4, 1990), p. 12 as Com(90) 3 final.

²⁷ See ch. 15 of this report for a discussion of the social dimension.

²⁸ Com(90) 188 final, OJ No. C 130 (May 29, 1990), p. 8. The original proposal appeared at OJ No. C 12 (Jan. 18, 1990), p. 16 and was discussed in USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990.

²⁹ OJ No. C 96 (Apr. 17, 1990), p. 68. Based on legislative resolution embodying the opinion of the European Parliament of Mar. 14, 1990, p. 71 of OJ for Apr. 17, 1990.

and public and private training bodies and would prohibit discrimination based on nationality. It would also set up an advisory body to ensure that these objectives are met.³⁰

A new proposed Council decision³¹ would deal with the implementation of a vocational training program in the audiovisual sector, an area whose development became a prominent goal of the member states after the meeting of top member-state officials in Rhodes in December 1988. The preamble stresses the importance of expanding Europe's audiovisual capacity, achieving free movement of programming, promoting high-definition television systems, and encouraging creativity in and portraying the diversity of European culture. It also refers to the October 2, 1989, joint declaration signed by 26 European countries and the EC Commission to create a transnational cooperation structure in this sector and a December 1989 initiative of the heads of member-state governments to encourage development of the industry.³² The proposal states that one of the most important aspects of overall EC policy for the sector is vocational training, with special attention to small and medium-sized businesses.

The program would operate during calendar years 1991 through 1995 and would focus on technical, commercial, and management training for professionals in the sector. It would be based in large part on transnational projects not run by EC institutions whose sponsors would make contracts outlining each scheme with the EC Commission and would provide 50 percent or more of their total cost. While criteria for the award of such contracts would be provided, the EC Commission would be given both the discretion and the responsibility to ensure that the program is carried out.

Another amendment to a proposed Council decision would clarify language relating to the suggested trans-European mobility scheme for university studies (TEMPUS).³³ This plan would allow European students, initially including those

from Poland and Hungary and later from other central and Eastern European countries, to carry out their studies at universities in more than one European country. Active university-industry cooperation in developing and running programs would again be encouraged.

Professional Qualifications

No significant activity has been apparent in relation to the mutual recognition of various professional qualifications. However, considerable monitoring by the EC Commission of member-state implementation efforts indicates that to date not all member states have incorporated in their national laws those measures needed to give effect to EC directives.³⁴

Possible Effects

Again, the assessment of potential effects of these measures set forth in earlier reports in this study is essentially unchanged. Factors such as German unification, cooperation among EFTA countries as 1992 draws closer, closer relations with central and Eastern European countries, and member-state views on security matters bear continued observation. Non-European countries may not have significant influence in these areas where a policy development or change is deemed troublesome. Also, with professionals in particular feeling concern about their competitors in other member states being allowed complete access to all member states, there may be some tendency to try to keep non-EC professionals from entering or obtaining full practice rights.³⁵

The apparent goal of these directives—elimination of nationality as a constraint on residence, work, or other private activity within the EC—means that businesses will be free to make location decisions based on other factors, such as the skills of laborers in an area. Also, businesses that do not choose or need to relocate can seek workers throughout the EC, and persons with desired skills can move easily to work for the highest pay or in the most personally satisfying capacity.

³⁰ See also Opinion [of the Economic and Social Committee] on the proposal for a Council Decision, OJ No. C 124 (May 21, 1990), p. 31. The action program, according to the opinion, fills gaps in existing EC programs such as COMETT, LINGUA, DELTA, ERASMUS, PETRA, and EUROTECNET, discussed in earlier reports in this study. However, the opinion urges that "vocational" not be interpreted as limited to the business context but also include other activities.

³¹ Com(90) 132 final, OJ No. C 127 (May 23, 1990), p. 13.

³² MEDIA, according to its name in French (translated as Measures to Encourage the Development of the Audiovisual Industry).

³³ Com(90) 146 final, OJ No. C 116 (May 11, 1990), p. 12. The original proposal, Com(90) 16 final/2, appeared in OJ No. C 85 (Apr. 3, 1990), p. 9.

³⁴ See Written Question No. 832/89 and answer (by Mr. Bangemann on behalf of the EC Commission) thereto on the pharmacy directives, and Written Question No. 838/89 and answer (again by Mr. Bangemann) thereto on the architecture directive, OJ No. C 125 (May 21, 1990), p. 17. The delays are being monitored and are largely attributed to complex and lengthy national legislative procedures.

³⁵ See, for example Ethan Schwartz, "Legal Revisions Threaten U.S. Law Firms in France", *Washington Post*, July 12, 1990, noting efforts to change French laws and professional codes to minimize foreign participation or even to require reciprocity as a condition of working in France.

CHAPTER 8
TRANSPORT

CONTENTS

	<i>Page</i>
Developments covered in the initial reports	8-5
Recent developments	8-5
Overview	8-5
Air-transport sector	8-6
Liberalization of air cargo	8-7
Background	8-7
Anticipated changes	8-7
Application of the rules of competition	8-7
Background	8-7
Anticipated changes	8-7
Common rules for a denied boarding compensation system	8-8
Background	8-8
Anticipated changes	8-8
Airport user consultation and charging principles	8-8
Background	8-8
Anticipated changes	8-8
Fares for scheduled air services	8-8
Background	8-8
Anticipated changes	8-9
Scheduled air services between member states	8-9
Background	8-9
Anticipated changes	8-9
Agreements and concerted practices in the air-transport sector	8-9
Background	8-9
Anticipated changes	8-9
Road- and rail-transport sectors	8-9
Regulations amending abolition of lodgement of transit advice note and amending regulation for the implementation of the Community transit procedure	8-10
Background	8-10
Anticipated changes	8-10
Final regime for the organization of the market for the carriage of goods by road	8-10
Background	8-10
Anticipated changes	8-11
Market access in the international carriage of goods by road	8-11
Background	8-11
Anticipated changes	8-11
Establishment of common rules for certain types of common carriage of goods between member states	8-11
Background	8-11
Anticipated changes	8-11
Amendment to proposal on the use of vehicles hired without drivers	8-11
Background	8-11
Anticipated changes	8-11
Communication on a Community railway policy	8-11
Background	8-11
Anticipated changes	8-12
Ocean-Transport Sector	8-12
Transfer of ships from one ship register to another	8-12
Background	8-12
Anticipated changes	8-12
Agreements between shipping companies	8-12
Background	8-12
Anticipated changes	8-13

CONTENTS – *Continued*

	<i>Page</i>
Possible effects	8-13
Effects on the air-transport sector	8-13
Effects on the rail- and road-transport sectors	8-13
Effects on the ocean-transport sector	8-14
Diversion of trade to the U.S. market	8-14
U.S. industry response	8-14

CHAPTER 8 TRANSPORT

EC initiatives pertaining to the 1992 program concerning transportation services have two major objectives. The first is creation of a unified transport market among the EC member states. This encompasses simplifying transportation between member states through such measures as eliminating border controls and streamlining customs documentation requirements. It also entails harmonizing technical and safety standards pertaining to transport services.

The second major objective is economic deregulation. This entails removing barriers to market entry affecting new carriers, permitting existing carriers greater flexibility in making routing decisions, and limiting governmental involvement in establishing fares and charges. It also encompasses decreasing the ability of individual member states to prohibit out-of-state carriers from engaging in cabotage – transportation between two points within the same state.

EC initiatives generally do not address transportation services generically. Instead, they almost invariably focus on a particular transportation sector – *air transport* (including both passenger and freight) *surface transport* (including trucks, passenger buses, and to a limited extent rail and combined motor-rail and motor-barge freight services), or *ocean transport* (carriage of goods by ocean vessels).

Developments Covered in the Initial Reports

In its 1985 White Paper, the EC Commission identifies its major goal pertaining to the air-transport sector as that of increasing competition. The White Paper states that this is to be achieved by measures such as changing the system for the establishment and approval of tariffs and limiting the rights of governmental bodies to restrict capacity and access to the market.¹ The EC took initial steps to implement economic deregulation in 1987 by restricting the scope of capacity-sharing arrangements between airlines then in effect on most passenger routes between points in different EC member states. A second deregulation package was proposed in 1989, which limited the power of individual member states to veto intra-EC passenger air fares, further restricted the scope of capacity-sharing arrangements, and relaxed to a limited extent member states' ability to regulate cabotage. The 1989 deregulation package did not address freight-only services or nonscheduled passenger services.

¹ Commission of the European Communities, *Completing the Internal Market: White Paper from the Commission of the European Communities to the European Council* ("White Paper"), June 1985, pp. 29-30.

In surface transport the White Paper describes two priorities: eliminating frontier checks in carriage by road, and easing capacity and entry restrictions pertaining to motor transport.² To help achieve the former objective, in 1989 the EC Commission proposed to eliminate the requirement that persons engaged in EC transit operations submit (or "lodge") a transit advice note to the customs office at the border of each member state through which a shipment is transported. To help achieve the latter objective, the EC Commission has proposed measures relaxing capacity and entry restrictions governing truck transport. In 1989 it proposed increasing the maximum number of authorizations each member state may grant to its trucking companies for Community transport by 40 percent per year for each year between 1990 and 1992. The quota system is scheduled to be eliminated effective January 1, 1993.

The principal objectives of the White Paper in the ocean-transport sector are to permit the freedom to provide ocean-transport services between member states and to establish rules of competition.³ The EC has adopted measures addressing the application of EC competition law to ocean transport and ensuring the right of citizens of one member state to provide maritime transport services among other member states. It has yet to address comprehensively the right of EC-member-state-flag vessels to engage in cabotage within another member state.

Recent Developments

Overview

The major EC transport initiatives issued during the period promoting White Paper objectives were proposals concerning economic regulation of air transport and trucking. Additionally, a substantial number of initiatives, not related to specific White Paper objectives, were issued proposing uniform licensing and operational standards.

The most noteworthy action in the field of air-transport was the EC Council's adoption in June of the 1989 air-transport deregulation proposals discussed above.⁴ The EC Commission had previously submitted amendments to the proposals to modify the circumstances in which discount fares may be disapproved through December 31, 1992, and to increase the scope and delay the effective date of the cabotage provisions. The EC Commission additionally issued a proposed regulation designed to decrease economic regulation of air-cargo services, which were not

² White Paper, pp. 29-30.

³ White Paper, p. 30.

⁴ "Air Transport: Council Adopts Second Liberalisation Package on Time," *European Report*, No. 1596, June 20, 1990, sec. IV, p. 13. The text of the Council action had not yet been published in the *Official Journal* when this report was prepared.

covered in the 1989 deregulation package, by giving EC-based air-cargo carriers the right to engage in cabotage and by increasing such carriers' flexibility to change rates.

In surface transport, the EC failed to adopt the 1989 proposal to increase by 40 percent per year, for each year through 1992, the quotas that determine the maximum number of authorizations each member state may grant to its trucking companies. Instead, the quotas were increased by 40 percent for 1990 only. The EC Commission also issued a proposed regulation that would grant it the authority to intervene in the road-transport market when excess capacity exists, creating the prospect that quantitative restrictions on trucking may continue even after quotas are eliminated in 1993.

Other significant actions in the surface-transport sector during the period related to the objective of reducing delays due to border crossings. The 1989 proposal concerning presentation of transit advice notes was adopted. Additionally, the EC Commission promulgated a number of regulations ancillary to the transit-advice-note initiative simplifying procedures concerning presentation of customs documents.

The EC still has not proposed a definitive cabotage regime for trucking for the post-1992 period.⁵ Moreover, no significant activity occurred during the period in the area of passenger motor transport. The EC Commission has criticized the Council's failure to adopt its 1987 deregulatory proposals concerning intercity bus transport.⁶

Activity in the area of ocean transportation was limited to issuance of two proposed regulations — one requiring member states to grant reciprocal registration privileges for cargo vessels, the other authorizing the EC Commission to exempt categories of maritime joint service agreements from anticompetition rules. The EC Commission has expressed concern at the continued lack of progress since 1986 of proposals intended to permit cabotage in ocean transport.⁷

Air-Transport Sector

The initiatives affecting air transport that were issued during the period may be divided into two categories — one pertaining to economic regulation, the other pertaining to harmonization of standards.

⁵ Commission of the European Communities, *Fifth Report of the Commission of the European Communities to the Council and Commission of the European Communities, European Parliament* ("Fifth Report"), Mar. 28, 1990, p. 22.

⁶ Fifth Report, p. 23.

⁷ Fifth Report, p. 23. See also "Maritime Transport: Parliament Committee Disagrees Over Cabotage," *European Report*, No. 1605 (July 21), 1990, sec. IV, p. 7 (noting continued disagreement among European Parliament's Transport and Tourism Committee members over maritime cabotage issue); "Maritime Transport: Positive Measures Remained Blocked" *European Report*, No. 1596 (June 20, 1990), sec. IV, p. 8 (noting inability of EC Council to agree on maritime cabotage measures).

Economic Regulation. The major initiative on economic regulation introduced during the period was the proposed regulation on air-cargo services. As previously mentioned, both this proposal and the recently adopted regulations on air-passenger transport relate directly to the White Paper objective of increasing competition in the air-transport market by liberalizing the conditions under which new carriers can enter the market, existing carriers can increase capacity, and all carriers can introduce lower fares.

Nonetheless, transport analysts have stated that structural problems in the EC may effectively block the type of expanded competition that the EC's deregulatory initiatives seek to create. The EC's ability to handle increased air-transport competition is limited because its air-traffic controllers are overburdened and its airports running out of room. New airlines are currently encountering difficulties in acquiring the landing rights they need for market entry.⁸ A study done by SRI International for the International Air Transport Association indicates that constrained airspace is costing an estimated \$2.5 billion annually, and that, given current growth rates, European air-traffic systems and the major European airports will reach maximum capacity by 1995 if there are no significant improvements.⁹ An Airbus Industries report reaches a similar conclusion, predicting that, under current trends, 24 European airports will be operating at maximum capacity by 2000 and half of all air passengers will face delays.¹⁰

The problem of air-traffic control was addressed at an April 1990 meeting of transport ministers from the 23 European Civil Aviation Conference members. The ministers voted for a scheme for completely coordinating the continental air-traffic control centers within the next 10 years.¹¹ The scheme contains four phases: (1) appraisal and evaluation, which is essentially complete; (2) program and development, scheduled for completion by 1993, which covers harmonization plans for the existing air-traffic control system and the beginning of airspace and route restructuring; (3) installation of advanced equipment by 1995 to harmonize systems and integrate high-density traffic centers; and (4) after 1995, the gradual integration of the total air-traffic-control system.

The problem of insufficient airport capacity may be more difficult to resolve. One airline analyst has stated that airlines face "astronomical" expenses to improve the European airport structure, and has predicted the costs of such expansion will ultimately be passed on to passengers in the form of

⁸ "Where the Skies Aren't Getting Any Friendlier," *Business Week*, Apr. 16, 1990, pp. 38-39; "Belgian David Takes on Europe's Airlines," *Financial Times*, Mar. 29, 1990, p. 3.

⁹ "Europe Faces Air Traffic Chaos, Says IATA," *Flight International*, Apr. 18-24, 1990, p. 6.

¹⁰ "Airbus Warns on Rising Airport Congestion in Europe," *Financial Times*, Mar. 9, 1990, p. 1.

¹¹ "Europe Votes for ATC Harmony," *Flight International*, May 2-8, 1990, p. 6.

higher fares.¹² One airline official, meanwhile, questions whether expansion is politically possible. According to Heinz Ruhnau, Chairman of Lufthansa German Airlines, environmentalist pressure will prohibit the construction of new airports.¹³

Also cited as inhibiting competition is the current trend towards concentration among EC airlines. Recent examples include a proposed joint service agreement between British Airways, KLM, and Sabena and a merger between the three major French airlines — Air France, UTA, and Air Inter.¹⁴ The EC Commission announced that it would investigate the BA/KLM/Sabena agreement.¹⁵ Additionally, as discussed below, the EC Commission has proposed a regulation giving it the power to take interim action blocking anticompetitive practices in cases of "urgent" need. Nevertheless, there have been numerous predictions that greater concentration of the EC airline industry is imminent and unlikely to result in lower fares.¹⁶

Harmonization of Standards. The initiatives establishing uniform standards for EC air services are typified by proposed regulations issued during the period prescribing uniform rules for denied boarding compensation for all passenger flights departing from EC airports (including those of non-EC air carriers) and standard procedures that EC airports must use in establishing user charges. Although these initiatives do not relate to a specific White Paper objective, the EC Commission perceives that such measures will help create a unified single market and projects that most future initiatives concerning air transport will address standards.¹⁷

Liberalization of Air Cargo

Background

This proposal is styled *Council Regulation (EEC) on the Operation of Air Cargo Services*, Com (90) 63 Final, *Official Journal of the European Communities (OJ)* No. C 88 (Apr. 6, 1990). In the preamble to this proposed regulation, the EC Commission indicates that some member states depend heavily on air cargo as an essential element of trade, but that national barriers still exist to free movement of air

¹² "EC 'Open Skies' May Make Big Airlines Bigger," *Journal of Commerce*, May 24, 1990, p. 1A.

¹³ "Trains to Replace Aeroplanes," *Flight International*, Feb. 21-27, 1990, p. 15.

¹⁴ "Why Open Skies are Under a Threat," *Financial Times*, Jun. 18, 1990, p. 8.

¹⁵ "EC Opposition Throws Doubt on Airline Proposals," *Financial Times*, June 28, 1990, p. 1; "Competition: Commission Objects to BA/KLM/Sabena Joint Venture," *European Report*, No. 1599 (June 30, 1990), sec. III, p. 2.

¹⁶ *Ibid.*; "EC 'Open Skies' May Make Big Airlines Bigger," *Journal of Commerce*, May 24, 1990, p. 1A.

¹⁷ Fifth Report, p. 22. See also the preambles to the proposed regulations on airport services and denied boarding compensation, which are discussed below.

cargo. The Commission proposes to remedy this situation by (1) promulgating common rules for granting operating licenses; (2) allowing EC-based carriers equal market access; and (3) requiring publication of cargo rates.

Anticipated Changes

The proposal mandates that Community air-cargo carriers be duly authorized to exercise third-, fourth- and fifth-freedom traffic rights within the EC.¹⁸ Additionally, carriers would be able to engage in cabotage, which is carrying cargo between two points within the same member state, if they meet that state's operational requirements. The proposal requires the EC Commission to promulgate and the EC Council to adopt EC-wide rules for granting operating licenses to EC-based air-cargo carriers.

Under the proposal, carriers would be required to furnish concerned member states 30 days advance notice of changes in cargo rates. States would have 14 days in which to object to the rates to the Commission on the basis that they are insufficient to ensure satisfactory safety and technical standards, and would have a mandate to "examine in detail" rate reductions in excess of 20 percent. A rate change would become effective unless disapproved by the Commission at least 7 days prior to its effective date. This regulation was scheduled to enter into force on July 1, 1990.

Application of the Rules of Competition

Background

Recent actions partially deregulating the air passenger market have heightened concern that established carriers may utilize predatory pricing and other anticompetitive measures to discourage or drive out new entrants.¹⁹ Current Regulation (EEC) No. 3975/87 provides aggrieved parties a remedy against anticompetitive practices, but does not grant the EC Commission the authority to enjoin such practices temporarily.

Anticipated Changes

A proposed amendment to Regulation 3975/87²⁰ would grant the Commission authority to temporarily enjoin anticompetitive practices that have the object or effect of threatening the viability

¹⁸ The five freedoms of air transport were defined under the Chicago Convention of 1944. These freedom rights include (1) the right to fly over another nation; (2) the right to land in another nation without picking up or disembarking passengers; (3) the right to disembark in another nation passengers boarded in the carrier's home country; (4) the right to carry passengers of another nation to the carrier's home country; and (5) the right to carry passengers from one foreign country to another.

¹⁹ "Brussels Seeks New Powers in Airline Pricing," *Financial Times*, May 3, 1990, p. 1.

²⁰ *Proposal for a Council Regulation (EEC) Amending Regulation (EEC) No. 3975/87 Laying Down the Procedure for the Application of the Rules of Competition to Undertakings in the Air Transport Sector*, Com (90) 167 final, OJ No. C 155 (June 26, 1990).

of an air service or of threatening the existence of an air carrier. Any temporary relief the Commission grants would have a maximum duration of 6 months.

Common Rules for a Denied Boarding Compensation System

Background

This proposal is styled *Proposal for a Council Regulation (EEC) on Common Rules for a Denied Boarding Compensation System in Scheduled Air Transport*, Com (90) 99 final, OJ No. C 129 (May 24, 1990). In it, the EC Commission notes that procedures for denied boarding compensation for scheduled airline passengers differ substantially among carriers. The proposal seeks to establish uniform, equitable, and transparent rules for bumping and denied boarding compensation. It is applicable to all scheduled flights departing from EC states, regardless of carrier or point of destination.

Anticipated Changes

Under the proposed regulation, passengers would be bumped in the following order: (1) volunteers; (2) travel industry personnel traveling on reduced-priced fares unavailable to the public; (3) passengers holding "fully flexible tickets" (i.e. without carrier restrictions); (4) passengers holding tickets limiting flexibility in carrier and flight selection; and (5) aged, handicapped, or child passengers, or those traveling due to family death or illness. The proposal provides a compensation schedule for passengers who have been bumped. Compensation varies from 25 percent to 100 percent of the value of the lowest fully flexible ticket, depending on the arrival time of alternative transportation. The proposed regulation additionally specifies what airlines must provide in food, local transportation, and accommodations to passengers bumped. This regulation is scheduled to enter into force on December 1, 1990.

Airport User Consultation and Charging Principles

Background

As previously discussed, many airports in the EC are operating at or near capacity, landing rights are limited, and expansion is necessary to handle projected traffic growth. In the preamble to this proposed regulation,²¹ the EC Commission notes that efficient airport facilities with reasonable, cost-based charges are critical to providing high-quality air transport. The stated purpose of

²¹ *Proposal for a Council Regulation (EEC) on Consultation between Airports and Airport Users and on Airport Charging Principles*, Com (90) 100 final, OJ No. C 147 (June 16, 1990).

the proposed regulation is to improve airport operations by (1) requiring that airport service users and airport operators consult regularly on matters pertaining to airport operations, facilities, or charges, and (2) ensuring that airport costs are borne in an equitable manner by airport users and that all airport charges are cost-based.

Anticipated Changes

The proposed regulation requires that airport authorities that operate airports with at least one million annual through passengers make annual reports to "users," defined as air carriers and/or air-carrier organizations, organizations representing noncarrier aircraft operators, and representative organizations of passengers, shippers, freight-forwarders, and terminal operators using the airport. These reports are to provide information concerning the airport's passenger and freight volume, aircraft movements, employment, and revenue. Additionally, the authorities would be required to consult with "users" at least 4 months before implementing "important changes" (an undefined term) in aeronautical services and facilities, "substantial development plans" (also undefined), and plans for new airport construction they propose to undertake. Authorities would have to provide at least 2 months' prior notice and consultation to users concerning the imposition of new charges or "important changes" in the level of charges. Conversely, aircraft operators would be required to furnish the authorities estimates of future traffic trends, scheduling information, and aircraft fleet characteristics, and authorities are accorded the right to observe scheduling conferences.

The proposal further requires that costs for airport facilities pertaining to passenger, aircraft, baggage, and freight flow be clear, understandable, reasonably related to costs, and allocated according to "sound business and economic principles." The regulation was scheduled to enter into force on July 1, 1990.

Fares for Scheduled Air Services

Background

In 1989, the EC Commission introduced a proposal for the "second package" of liberalization of air-passenger services.²² A major component of that proposal provided carriers with greater flexibility in establishing fares. Under the proposal, new fares for transportation between member states became effective unless there is "double disapproval"—that is, unless the civil aviation authorities of both member states disapprove the fare.

²² A detailed discussion of the second liberalization package is provided in U.S. International Trade Commission, *The Effects of Greater Economic Integration within the European Community on the United States: First Follow-Up Report* (Investigation No. 332-267), USITC Publication 2268, March 1990, p. 8-9.

Anticipated Changes

The 1989 proposal has been amended to limit the circumstances in which proposed fare reductions through December 31, 1992, would be subject to double disapproval.²³ Double disapproval would be applicable only to (1) unrestricted fares that are 90 percent or more of the "reference fare," defined as the average of the normal economy fares charged by EC-based airlines on the route in question; (2) fares between 60 and 90 percent of the "reference fare" that are subject to a minimum stay, advance purchase, or cancellation penalty requirement; or (3) fares between 30 and 59 percent of the "reference fare" that are for round-trip travel and are subject to a combination of minimum stay, advance purchase, cancellation penalty, off-peak travel, or age requirements. Other fare reductions would have to be approved by the civil aviation authorities of both affected member states.

Scheduled Air Services Between Member States

Background

Another component of the 1989 "second liberalization package" extended cabotage rights on routes to and from a carrier's state of registration provided the route is operated between two airports, one of which is a regional airport, and the air carrier does not use more than 30 percent of its annual seat capacity serving cabotage passengers.²⁴

Anticipated Changes

The EC Commission has amended the 1989 proposal on cabotage.²⁵ As amended, the effective date of the cabotage provision, originally October 1, 1990, is delayed until January 1, 1993. The requirement that cabotage be permitted only on routes to and from its state of registration (i.e. a British carrier could transport passengers on the Nice-Paris leg of a Nice-Paris-London flight) has been retained. The regional airport and capacity restriction requirements have been deleted.

Agreements and Concerted Practices in the Air-Transport Sector

Background

Article 85(1) of the Treaty of Rome prohibits agreements, decisions or concerted practices that may affect trade between member states and that

²³ Amendment to the Proposal for a Council Regulation (EEC) on Fares for Scheduled Air Services, Com (90) 234 final, OJ No. C 164 (July 5, 1990).

²⁴ For a complete discussion, see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 8-9.

²⁵ Commission Proposal for a Regulation on Access for Air Carriers to Scheduled Intra-Community Air Service Routes and on the Sharing of Passenger Capacity between Air Carriers on Scheduled Air Services Between Member States, Com (90) 234 final, OJ No. C 164 (July 5, 1990).

have as their object or effect the prevention, restriction or distortion of competition within the EC. Article 85(3), however, states that agreements or categories of agreements that contribute to technical or economic progress may be made exempt from the restrictions in article 85(1). Regulation (EEC) No. 3976/87 permits the EC Commission to promulgate regulations exempting from the article 85(1) restrictions any agreements on scheduled air-service-capacity restrictions, consultation for common preparation of proposals on tariffs and fares, airport slot allocation, purchase and operation of computer reservation systems, and airport security and handling of passengers, mail, freight and baggage. The regulation imposed restrictions on the binding effect of most categories of agreements permitted under the regulations and terminated the EC Commission's authority to promulgate regulations on such agreements on January 31, 1991. In October 1989 the EC Commission proposed amending Regulation 3976/87 (1) by removing the 1991 termination date for authority to promulgate regulations, but requiring that all regulations have an expiration date, and (2) by removing the restrictions concerning the binding effect of agreements.²⁶

Anticipated Changes

The current proposed amendment²⁷ to Regulation 3976/87 reverses most of the changes proposed in 1989. The termination date for the EC Commission's authority to promulgate regulations has been retained, although it has been extended until January 31, 1992. The provision restricting the binding effect of agreements has been restored.

Road- and Rail-Transport Sectors

The most significant actions in the road-transport sector during the period covered by the report are measures designed to implement the transition towards the scheduled January 1, 1993, termination of quantitative restrictions. The EC modified the system of quotas under which individual member states grant authorizations to trucking companies. The Council increased these quotas, which are scheduled to be terminated at the end of 1992, by 40 percent for the year 1990 only. Some member states resisted the increase on the grounds it was likely to cause excess capacity.²⁸ In response to these concerns, the Council has submitted a proposed regulation that would provide the EC Commission with broad authority to act, including the power to limit capacity, to resolve excess capacity situations, including those limited to specific geographical areas, vehicle categories, or types of activity.

²⁶ This proposal was designated Com (89) 373 final, 89/C 258/06.

²⁷ Proposal for a Council Regulation (EEC), Amending Regulation (EEC) No. 3976/87 on the Application of Article 85(3) of the Treaty to Certain Categories of Agreements and Concerted Practices in the Air Transport Sector, Com (90) 264 final, OJ No. C 159 (June 29, 1990).

²⁸ "40% Increase in Road Haulage Quota Agreed for 1990," *European Report*, No. 1576 (Mar. 31, 1990), sec. IV, p. 9.

Other proposed regulations pertaining to road transport are intended to increase efficiency by eliminating delays at borders between EC member states attributable to customs regulations. Typical of these are the proposed regulations dealing with customs documents. Nevertheless, the continued presence of frontier controls and resulting paperwork and delay (due largely to value-added tax (VAT) adjustment) remains a barrier to the creation of an efficient road-transport system.²⁹ Frontier controls are due to be eliminated after December 31, 1992, and delay presently associated with border crossings between member states is expected to be eliminated and the paperwork substantially reduced. Additionally, the elimination of capacity and cabotage restrictions along with the subsequent elimination of trucks returning empty from their destinations should serve to eliminate a share of congestion and pollution problems currently plaguing the road-transport sector.³⁰

Additionally, the EC Commission continues to propose policies to revitalize rail transport. Currently, on certain passenger routes, the railroads do not possess the speed to compete with air transport, and in freight transport, the railroads on many principal routes possess insufficient height or width clearances to accept intermodal cargo containers.³¹ The EC Commission reports that as freight traffic has grown, the rail share of total freight haulage has declined sharply, indicating railroads' inability to prosper in a more competitive environment.³² In an effort to improve the efficiency and competitiveness of railways, the EC Commission has proposed policies to facilitate development of international joint rail services and high-speed passenger trains.

Regulations Amending Abolition of Lodgement of Transit Advice Note and Amending Regulation for the Implementation of the Community Transit Procedure

Background

The EC has eliminated the requirement that persons engaged in EC transit operations be required to submit a transit note at the border of each member state through which goods are transported.³³ This change required a

²⁹ C. Scrivener, "European Internal Market and the Transportation Issue," paper presented for American Enterprise Institute Conference, Mar. 6, 1990, p. 54.

³⁰ EC Commission, *Communication on a Community Railway Policy* (Communication), Jan. 25, 1990, p. 12.

³¹ *Ibid.*, p. 15. The EC Commission provides in this document information on the various EC transport modes in the EC and deals with the environmental and social dimensions associated with transport.

³² *Ibid.*, p. 12.

³³ This regulation (Com (89) 331), which has been adopted, is discussed in detail in the USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 8-12.

corresponding change in the rule presuming that, when the shipment is not produced at the customs office at the place of destination, any irregularity or offense concerning the shipment will be deemed to have occurred in the member state in which the last transit advice note showed that the shipment entered. Additionally it required a change in procedures concerning furnishing proof of the regularity of the transit operation.

Anticipated Changes

Under the regulation concerning transit advice notes,³⁴ when a shipment cannot be produced at the customs office of the place of destination and the place of irregularity in the shipment cannot be established, it will be presumed to have occurred either in the member state of the place of departure or the member state in which the shipment entered the Community. The member state in which the irregularity actually occurred has 3 years in which to rebut the presumption.

Under the regulation concerning transit procedures,³⁵ proof of regularity of a transit operation requires either (1) presentation of a certified customs document showing that the goods have been produced at the office of destination or to an authorized consignee, or (2) presentation of a customs document issued by a third country showing release for consumption. In the event of irregularity, the customs office of the state of departure has 11 months from the date of registration of the Community transit declaration to notify the principal. The principal has 3 months from the time of notification either to furnish proof of regularity or to indicate where the irregularity actually occurred. Failure to do so can lead to an action for recovery of duties or charges. Both regulations were scheduled to enter into force on July 1, 1990.

Final Regime for the Organization of the Market for the Carriage of Goods by Road

Background

This proposed regulation is styled *Proposal for a Council Regulation (EEC) on the Introduction of the Final Regime for the Organization of the Market for the Carriage of Goods by Road*, Com (90) 64 Final, OJ No. C 87 (Apr. 5, 1990). The road-transport market in the EC has been governed by a quota system specifying the number of authorizations that each member state can grant its trucking companies. By 1993 this system is to be replaced by a Communitywide authorization system. The proposed regulation establishes a safeguard mechanism for periods of

³⁴ Council Regulation (EEC) No. 474/90, *Amending, With a View to Abolishing Lodgement of the Transit Advice Note on Crossing an Internal Frontier of the Community*, OJ No. L 51/1 (Feb. 27, 1990).

³⁵ Commission Regulation (EEC) No. 1429/90, *Amending Regulation (EEC) No. 1062/87 on Provisions for the Implementation of the Community Transit Procedure and for Certain Simplifications of That Procedure*, OJ No. L 137/21 (May 30, 1990).

"crisis" under the new system. A "crisis" is defined as a clear excess of supply over demand, or a situation in which a "properly managed undertaking" cannot cover its costs and finds its future in jeopardy. A "crisis" can be limited to a specific geographic area, vehicle category, or type of activity.

Anticipated Changes

The proposed regulation provides the Commission authority to adopt "whatever measures are necessary" to resolve a crisis, including limiting capacity. It gives member states the right to petition the Commission for a crisis declaration. The measures that would be employed for crisis resolution may not jeopardize the end of Community quotas scheduled for December 31, 1992. The proposal additionally directs the Commission to collect data concerning costs, demand, employment trends, capacity and investment in the road-transport sector. The regulation is scheduled to enter into force on January 1, 1991.

Market Access in the International Carriage of Goods by Road

Background

This regulation is styled *Council Regulation (EEC) No 1053/90 Amending Regulation (EEC) No 3164/76 Concerning Access to the Market in the International Carriage of Goods by Road*, OJ No. L 108/5 (Apr. 28, 1990). As previously stated, Community trucking is currently governed by a quota system. Under article 3(3) of Regulation 3164/76 as amended by Regulation 1841/88, the Council was required by March 31, 1990, to establish increased quotas for 1990. The quota increases are designed to ease the transition to the abolition of quotas in 1993.

Anticipated Changes

The regulation establishes the 1990 quota for each member state.³⁶ In addition to its respective authorization, a member state may request that 20 percent of the additional authorizations approved for 1990 may be converted to "short-haul operations," a term not defined in the regulation.

Establishment of Common Rules for Certain Types of Common Carriage of Goods Between Member States

Background

EC Directive 75/130 established rules for combined motor-rail transport of goods. The directive exempted such intermodal transport

³⁶ A total of 33,635 authorizations are provided for 1990. West Germany, France, the Netherlands, and Italy collectively account for almost 50 percent of the authorizations.

from quota and authorization requirements and established documentation policies for intermodal shipments. In its current proposed amendment to Directive 75/130,³⁷ the EC Commission would make the benefits of that directive available to other types of intermodal transport. The proposal states that such transport should be encouraged because of its potential to reduce road congestion, decrease pollution, and facilitate transit across Alpine states.

Anticipated Changes

The proposed amendment would make Directive 75/130 applicable to combined motor-inland waterway transport as well as to combined motor-rail transport. It would also permit EC-based motor carriers to operate the motor portion of international intermodal transport in any member states without having to establish a registered office or place of business in that member state. The proposal also establishes a method of calculating reimbursement of excise taxes paid by motor carriers in connection with international intermodal transport.

Amendment to Proposal on the Use of Vehicles Hired Without Drivers

Background

Directive 84/647 liberalized the conditions under which EC shippers could use vehicles hired without drivers, but it permitted member states to make the liberalized provisions inapplicable to owner-operated vehicles. In 1989, the EC Commission proposed amending Directive 84/647 to eliminate member states' ability to make the provisions inapplicable to owner-operated vehicles.³⁸

Anticipated Changes

The current proposal³⁹ would amend the 1989 proposed directive to require the EC Commission to submit proposals by January 1, 1993 for the removal of all restrictive conditions on the use of vehicles hired without drivers for carriage of goods by road.

Communication on a Community Railway Policy

Background

Although no longer the dominant transportation mode, EC railroads remain important to the movement of bulk freight and to medium- and

³⁷ Proposal for a Council Directive Amending Directive 75/130 on the Establishment of Common Rules for Certain Types of Combined Carriage of Goods Between Member States, Com (89) 564 Final, OJ No. C 34 (Feb. 14, 1990).

³⁸ The 1989 proposal is discussed in full in USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 8-13.

³⁹ Amendment to the Proposal for a Council Directive Amending Directive 84/647/EEC on the Use of Vehicles Hired Without Drivers for Carriage of Goods by Road, Com (90) 208 final, OJ No. C 150 (June 19, 1990).

short-distance passenger transport. In its *Communication on a Community Railroad Policy*, Com (89) 564 final, the Commission notes that greater integration of the transport sector is an essential objective of EC unification, and that improving the efficiency of railroad sector is critical to achieving this objective. The communication sets forth three proposals in this regard, concerning development on community railways, operation of transport "public services," and establishment of a network of high-speed trains.

Anticipated Changes

The proposal concerning development on community railways encourages the national railroads of the member states to establish "railway undertakings" to operate international joint services. Such "undertakings" are to be autonomous entities that are to be able to make their own decisions on staffing and supply, marketing, and pricing of services. The "undertakings" are to be granted equitable access to the track and equipment of the member-state national railroad, and are to pay access and equipment charges on a fair and nondiscriminatory basis.

The proposal on public service, which amends Council Regulation (EEC) No. 1191/69, is applicable to inland waterway and road as well as rail transport. The proposal authorizes member states to enter "public service contracts" concerning urban/suburban and regional transport services governing the frequency, capacity, quality, and/or fares for such services. Additionally, member states must file annual reports to the EC Commission concerning their public service contracts.

The proposal concerning high-speed trains calls for the Council to establish, by the end of 1990, the form of a European high-speed rail network and timetable for construction of that network. The Council is also to promulgate directives necessary for the network's technical harmonization. A procedure for consultation with member states is established.

Ocean-Transport Sector

Only two initiatives pertaining to the ocean-transport sector were issued during the period of this report. The first proposal would require member states to grant reciprocal registration privileges for certain types of cargo ships. The second would permit the EC Commission to exempt from EC rules proscribing anticompetitive practices joint service agreements pertaining to ocean liner service.

Transfer of Ships from One Register to Another

Background

An ocean vessel must satisfy the safety and operational requirements of the country in which it is registered. In this proposed regulation,⁴⁰ the EC Commission notes that while all member states are parties to four major multilateral agreements governing vessel safety and pollution protection,⁴¹ each member state independently interprets certain provisions of the agreements. Additionally, some member states have technical requirements for ocean vessels beyond those mandated by the multilateral agreements. The proposed regulation seeks to remove these divergent technical and safety requirements as an impediment to shipowners who desire to change their vessel's country of registration from one member state to another. According to the EC Commission, facilitating the transfer of ships among EC ship registers will improve the operating conditions and competitive positions of EC ocean transport.

Anticipated Changes

The proposed regulation would prohibit member states from withholding registration for covered ships (defined as EC-member-state-flag cargo ships of more than 500 tons gross tonnage that have been certified as complying with standards for new vessels built after May 1980) that are registered in another member state.⁴² If a member state nonetheless refuses registration on the grounds that the ship does not conform to that state's interpretation of the four major multilateral vessel safety agreements, the Commission, through a maritime safety committee, would be required to review the denial. This regulation is scheduled to enter into force on January 1, 1991.

Agreements Between Shipping Companies

Background

Article 85(1) of the Treaty of Rome prohibits agreements, decisions, or concerted practices that may affect trade between member states and have as their object or effect the prevention, restriction, or distortion of competition within the EC. Article 85(3), however, states that agreements or categories of agreements that contribute to technical or economic progress may be made exempt from the restrictions in article 85(1). In this proposed

⁴⁰ *Proposal for a Council Regulation on the Transfer From One Register to Another Within the Community*, Com (90) 219 final, OJ No. C 153 (June 22, 1990).

⁴¹ These are the 1974 International Convention for the Safety of Life at Sea, the International Convention on Load Lines 1966, and the International Convention for the Prevention of Pollution from Ships 1973.

⁴² Member states that are party to an agreement on the protection of marine environment in the Baltic Sea area may continue to impose additional safety requirements pursuant to that agreement.

regulation,⁴³ the EC Commission states that joint service agreements between ocean-liner-service companies should be exempted from the article 85(1) restrictions because they help effect cost reductions, increased capacity utilization, and better service quality.

Anticipated Changes

The proposed regulation would grant the EC Commission the authority to promulgate regulations exempting from article 85(1) restrictions categories of agreements for the joint operation of maritime services or combined maritime and land-transport services. The EC Commission may remove the article 85(1) exemption from an individual agreement when it finds the agreement has an unduly anticompetitive effect or when parties to an individual agreement are in breach of its conditions.

Possible Effects

Effects on the Air-Transport Sector

Two prominent European transport officials have indicated that the developments in the internal European market will have significant effects on the EC-member states' external relations concerning aircraft services. In a speech before the Federal Aviation Administration's Aviation Forecast Conference, Mr. Karel van Miert, EC Commissioner for Transport, indicated that the most important of the external relations proposals on air transport relate to the 60 bilateral air-services agreements in force between the member states and third countries.⁴⁴ Mr. van Miert noted that these agreements, which are based on the Chicago Convention of 1944, regulate air services between the member states and establish procedures to fix, among others, the level of tariffs and capacity. He noted further that it was the EC Commission's opinion that as a logical consequence of the gradual development of the internal market, close cooperation in the field of external relations is essential. Mr. van Miert advised that, "Individual member states should therefore not conclude agreements with third countries which directly affect the internal market without consulting the other member states. Therefore, these proposals set up a framework for such consultations. Gradually the Community will become responsible for external aviation relations and the existing bilateral framework will have to be replaced by air-services agreements concluded between the Community as a whole on the one hand and a third country or third

⁴³ Proposal for a Council Regulation on the Application of Article 85(3) of the Treaty to Certain Categories of Agreements, Decisions, and Concerted Practices Between Shipping Companies, Com (90) 260 final, OJ No. C 167 (July 10), 1990.

⁴⁴ K. van Miert, EC Commissioner for Transport, *The External Aspects of the Common Air Transport Policy*, address to the 15th Annual Federal Aviation Administration Forecast Conference, Washington, DC, Mar. 2, 1990.

countries on the other." Mr. van Miert noted that, "The European Community has started a process aimed at replacing gradually the traditional bilateral framework by a multilateral approach on traffic rights, fares and many other areas." Mr. van Miert made clear in his speech that in the future, the EC Commission will become the negotiator with respect to third-country air flights into the EC.

Similar views have been expressed by Daniel Tenenbaum, Director General of French Aviation, who has stated that the strictly bilateral regime of air-services agreements established by the Chicago Convention "is getting old. One of these days it will become necessary to wipe off the dust that has accumulated."⁴⁵ A U.S. transportation analyst has also indicated that "both the logic and effective operation of a barrier-free internal air-transport market ultimately require a common front for negotiating with third parties." The analyst predicts that negotiations concerning air-services agreements with third countries will ultimately be conducted on an EC-wide basis.⁴⁶

Effects on the Rail- and Road-Transport Sectors

The directives and regulations issued during the period are likely to increase the efficiencies of both road-freight transport and the movement of passengers and freight by rail. The gradual elimination of restrictions on road-transport cabotage operations and the elimination of border stops are likely to transform the EC road-haulage sector. The harmonization of railroad standards among the member states and the creation of a high-speed network of trains are likely to make the railroads more efficient and create increased competition for road-haulage firms as well as airlines carrying passengers and freight. The creation of additional competition among the various transport sectors is likely to provide increased benefits to consumers and users of the various transport modes and increase the international competitiveness of European firms. The integration of the single market will require the creation of a highly efficient transport system that is not encumbered by national differences. Major problems outstanding in the rail- and road-transport sectors include the harmonization of value-added taxes, how to allocate the costs of railroad improvement among the member states, and how to deal with differential road taxes imposed by the member states, such as those anticipated by West Germany.⁴⁷

⁴⁵ D. Tenenbaum, "Europe 1993 - What to Expect," speech to the International Aviation Club of Washington, May 10, 1990.

⁴⁶ D.M. Kaspar, "U.S.-European Air Services in the 1990s: A Turbulent Decade?" paper prepared for American Enterprise Institute Conference, Mar. 7, 1990.

⁴⁷ Communication, pp. 3-12.

Effects on the Ocean-Transport Sector

The proposed regulation concerning reciprocal registration would harmonize safety and technical standards. Some in the EC believe such steps insufficient to revitalize what they perceive as a moribund maritime sector and would prefer to go farther and establish a Community ship register, which would permit vessels to sail under the EC flag, rather than under that of a particular state.⁴⁸ The majority of EC shipowners strongly oppose the concept of an EC register, however.⁴⁹

The effect of the proposed regulation concerning joint service agreements is unclear, principally because the proposal does not identify the criteria that such agreements will have to meet in order to receive an exemption from EC anticompetitive practice rules. One report states that the possibility of more onerous regulation has carriers "deeply dismayed."⁵⁰ Another report indicates that interests representing users of such services believe that such arrangements provide carriers with excessive power and expressed disappointment that the EC proposal permits the EC Commission to grant block, rather than individual, exemptions from anticompetitive practice rules.⁵¹

Diversion of Trade to the U.S. Market

The current set of directives and regulations does not address third-country issues. The general impact that creation of a single European market for transport services may have on the U.S. market was discussed fully in the first followup report.⁵²

U.S. Industry Response

Concerns of the U.S. air-transport industry relate to three areas of interest. These include the

⁴⁸ See Economic and Social Committee Opinion, *OJ* No. C 56 (Mar. 7, 1990).

⁴⁹ "Britain Opposes European Ship Register," *Journal of Commerce*, July 19, 1990, p. 1B.

⁵⁰ "Competition: Commission Plans Tighter Regulation of Shipping Industry," *European Report*, No. 1592 (June 7, 1990), sec. III, p. 2.

⁵¹ "EC Eyes Antitrust Break for Shipping Consortia," *Journal of Commerce*, June 21, 1990, p. 1A.

⁵² USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 8-17.

EC Commission's likely designation of the single market as a cabotage area that could subsequently affect U.S. carriers' fifth-freedom rights in the EC, the criteria used by the EC Commission in making slot allocations at major airport centers, and the code of conduct for computer reservation systems. According to an official at the U.S. Air Transport Association (ATA), the current bilateral agreements negotiated between the United States and the EC member states and currently in force are not likely to be changed in the foreseeable future.⁵³ The official indicated that the United States had asked the EC if there was a desire to renegotiate certain selected agreements and was told that the EC lacked the authority to undertake such negotiations. However, according to the official, the EC did indicate that whenever bilaterals are negotiated in the future, both EC officials and officials from the affected member states must be present at the negotiations. The ATA official also indicated that he believed that the current bilateral agreements existing among the various member states would be changed only gradually, and that any new agreements would be controlled by EC directives.

In May 1990, a special U.S. task force released an assessment report on the economic policy issues raised by the EC single-market program and addressed a number of issues, including civil aviation. In the report, the task force indicated that the United States supports the aviation liberalization measures being undertaken by the EC and anticipates that these measures will lead to increased opportunities for both EC and U.S. air carriers across the North Atlantic.⁵⁴ According to the report, the United States urges that commercial opportunities in the EC for U.S. airlines, as well as for associated airline services, are made available on a fair and nondiscriminatory basis. The task force indicated that such treatment should include computer reservation systems, slot allocations, competition rules, air cargo, and other ancillary services.

⁵³ USITC staff conversation with American Transport Association official, May 21, 1990.

⁵⁴ U.S. Government Task Force on the EC Internal Market, *EC 92: An Assessment of Economic Policy Issues Raised by the European Community's Single Market Program*, May 1990, p. 26.

CHAPTER 9
COMPETITION POLICY AND COMPANY LAW

CONTENTS

	<i>Page</i>
Developments covered in previous reports	9-3
Measures adopted	9-3
Merger Regulation	9-3
Eleventh Company Law Directive	9-3
New initiatives	9-3
European Company Statute	9-3
Thirteenth Company Law Directive	9-3
Measures unchanged	9-4
Developments since the first followup report	9-4
Merger Regulation	9-4
Implementing Regulation	9-5
Notification Form CO	9-5
Notice on Ancillary Restrictions	9-7
Joint Ventures Notice	9-8
Thirteenth Company Law Directive	9-9
European Company Statute	9-10

CHAPTER 9 COMPETITION POLICY AND COMPANY LAW

Developments Covered in Previous Reports

Competition and corporate law continue to be important areas of interest for U.S. companies planning to invest in the European Community. Developments in this area are generally favorable to U.S. companies because the harmonization of national laws eliminates the need in some areas to learn and comply with a different legal regime in each member state.

Measures Adopted

Merger Regulation

At the December 1989 meeting of the Council of the European Communities, the Council adopted the Regulation on the Control of Concentrations (Reg. No. 4064/89) (hereinafter "Regulation"). This Regulation grants the Commission of the European Communities (hereinafter "EC Commission") the authority to approve or reject proposed mergers between companies from different member states, provided the companies are sufficiently large to reach the jurisdictional thresholds. The Regulation purports to give the EC Commission sole jurisdiction over these large mergers but, at the same time, creates two exceptions to the exclusive jurisdiction—one giving the member states the authority to reclaim jurisdiction if there are "other legitimate interests," and another permitting the EC Commission to "refer" a merger to the member state if there is a "distinct market" in the member state affected by the merger. The Regulation requires that companies planning to merge notify the EC Commission and temporarily suspend the merger while the EC Commission determines whether the merger would be "compatible with the Common Market." The Regulation establishes traditional competition criteria to determine "compatibility," but concern continues to exist that "industrial policy" will play a role in EC Commission decisions.

Eleventh Company Law Directive

At the December 1989 meeting, the Council also adopted the Eleventh Council Directive on disclosure of the branches. This directive permits a branch of a company located in a member state other than that in which the company is headquartered to submit to the host state the annual accounts and annual report of the company instead of the accounts of the individual branch.

New Initiatives

European Company Statute

The European Company Statute is divided into two parts. The first part is a regulation that covers most of the procedural aspects of establishing a company (hereinafter "Company Regulation"). The Company Regulation dictates how to and who may establish a European Company, or *Societas Europea* (SE), as well as some of the technical aspects of corporate operations. The Company Regulation further provides that national law will apply in some areas such as protection of shareholders, issuance and transfer of shares, and insolvency. The Company Regulation attempts to create a neutral tax structure and, at the same time, to provide tax incentives in order to create a European Company. The second, and most controversial, part of the European Company statute is a directive that mandates worker participation in the administration of the company (hereinafter "Company Directive"). The Company Directive provides three alternative models under which workers are given varying degrees of participation on the supervisory board. The EC Commission does not envision that workers will be involved in the day-to-day management of the company.

Adoption of the European Company Statute Regulation and Directive will likely have a limited effect on U.S. companies exporting to and doing business in Europe, primarily because formation of an SE is an alternative to, not a replacement for, formation of a company under national law. One advantage to forming an SE will be the rationalization of company operations previously spread across national boundaries and the resulting efficiencies. Another advantage to forming an SE will be the tax benefits to be created by the EC Commission as an incentive to form an SE. The greatest disadvantage for U.S. companies will be the worker-participation requirements (most European countries except the United Kingdom already have some form of worker participation). U.S. companies will not be disadvantaged by the requirement that only European companies may establish SEs, because European subsidiaries of U.S. companies may participate in an SE. U.S. companies may face increased competition from SEs enjoying increased efficiencies because of the SE structure.

Thirteenth Company Law Directive

As another step in the harmonization of company law, the proposed Thirteenth Company Law Directive (hereinafter "Directive") is directed at harmonizing law on takeovers and tender offers in the EC. A controversial provision in the Directive requires a person who acquires more than 33.3 percent of a company to make an offer, on equal terms, for the outstanding shares. The Directive also requires that information be provided to the employees of both companies. Another notable aspect of this proposed directive is the limitation on

defensive actions the board of directors of a target company is permitted to take in response to an unfriendly takeover.

The Thirteenth Company Law Directive will likely have a marginal effect on U.S. companies doing business in Europe. If adopted in its present form, the Directive will include some requirements that are unfamiliar to U.S. companies. The Directive requires more information in the offer document than is required under U.S. law. The restrictions on defensive action that can be taken by the target company are unusual in U.S. law. Finally, the obligatory bid requirement, although absent from U.S. law, is not overly burdensome because, in general, persons (or companies) making a takeover bid usually make their intentions known before that threshold is reached. Consequently, this provision is unlikely to discourage investment in the EC.

Measures Unchanged

Two company law directives remain unchanged. The Fifth Company Law Directive concerning the structure of public limited companies continues to be the subject of debate. The future of this directive, especially the provisions mandating worker participation, is tied to the future of the European Company Statute. As reported in the initial USITC report, the success or failure of the Fifth Directive will also affect the Tenth Company Law Directive concerning cross-border mergers. Since the publication of the initial USITC report, however, there have been no new developments on the Tenth Directive.

The Telecommunications Directive, opening the telecommunications terminal equipment market, is still the subject of a challenge by France in the European Court of Justice. In late 1989, the Advocate-General, who advises the Court, but whose opinion is not binding, issued his opinion in support of France's opinion that the EC Commission had exceeded its authority in using article 90. The Court has not yet ruled on this matter.

Developments Since the First Followup Report

Merger Regulation

The EC clearly remains an active arena for mergers, and one in which the United States is an important player. According to the EC Commission's most recent report on competition, from June 1988 to June 1989 there were 1,122 mergers, or concentrations as they are called in the EC,¹ involving companies in the EC.² *Translink's 1992 M & A Monthly* has counted over 600 mergers

and acquisitions involving EC firms in the first 5 months of 1990.³ Except for January 1990, the United States was in the top five spenders in those mergers for which prices were disclosed.⁴ Given the increasing investments by U.S. firms in the EC, the regime under which these mergers will be evaluated is of increasing importance to U.S. firms.

As reported in the first followup report,⁵ the EC Commission passed the Merger Regulation⁶ on December 21, 1989.⁷ The Merger Regulation has, for the most part, been well received by antitrust experts because it offers "one-stop shopping," is administered by the EC Commission rather than the potentially more nationalistic member state merger authorities, and employs competition criteria for evaluating mergers.⁸ It has been criticized, however, for the high jurisdictional thresholds, the potential for consideration of industrial policy in evaluating mergers, and the exceptions to exclusive EC Commission control through which mergers may become subject to member-state control.⁹ Having achieved the authority to vet mergers, the EC Commission promulgated implementing rules addressing the procedural details of merger control and issued "notices" clarifying some of the confusion engendered by the Merger Regulation.

In early 1990, the EC Commission circulated draft implementing regulations, a draft notification form (Form CO), a draft notice on ancillary restriction and a draft notice on cooperative and concentrative joint ventures. A variety of sources submitted comments on these drafts, many of which the EC Commission accepted. On July 25, 1990, the EC Commission approved the final forms of all of these documents.¹⁰

³ *Translink's 1992 M & A Monthly*, March 1990 - July 1990.
⁴ *Ibid.*

⁵ U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States, First Follow-Up Report* (Investigation No. 332-267), USITC Publication 2268, March 1990, pp. 9-4 to -9.

⁶ See Council Regulation No. 4064 on the Control of Concentrations Between Undertakings, *Official Journal of the European Communities*, (hereinafter "OJ") No. L 395, (Dec. 30, 1989) p. 1 (hereinafter "Merger Regulation").

⁷ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 9-4.

⁸ See, generally, USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 9-4 to 9-9. A comprehensive review of the merger regulation will be published in the upcoming volume of the *Antitrust Law Journal*. See, Barry Hawk, "The EEC Merger Regulation: The First Step Toward One Stop Merger Control," *ABA Antitrust Law Journal*, vol. 59, No. 1 (hereinafter "Hawk article").

⁹ See, generally, USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 9-4 to 9-9. One of the exceptions to exclusive EC Commission control permits a member state to review a merger's effect on the plurality of the media. However, the EC Commission does not exclude proposing a directive harmonizing member state legislation on plurality of the media. See, *Communication from the Commission to the Council and Parliament on Audio Visual Policy*, Com (90) 78 (final), (Feb. 21, 1990), sec. 2.2.3. Such a proposal would be a departure from the Community's general approach to assess mergers solely on economic criteria. USITC staff meeting with EC legal expert, Aug. 7, 1990.

¹⁰ "Commission Regulation (EEC) No 2367/90 of 25 July, 1990 on the Notifications, Time Limits and Hearings Provided for in Council Regulation (EEC) No 4064/89 on the Control of Concentrations Between Undertakings" OJ No. L 219 (Aug. 14,

¹ Notwithstanding any differences between the legal meanings of concentration and merger, they are used interchangeably in this report.

² *European Report*, No. 1607 (July 27, 1990), p. 9.

Implementing Regulations

Article 23 of the Merger Regulation empowers the EC Commission to "adopt implementing provisions concerning the form, content and other details of notifications." These Implementing Regulations provide specific rules on notification, hearings, and deadlines. Article 2 of the Implementing Regulations provides that all mergers shall be notified by means of Form CO and that the notifying party must submit twenty copies of Form CO and fifteen copies of all supporting documents.¹¹ Under article 2(3) of the Implementing Regulations, the EC Commission will accept either the original or copies of documents, a change from the earlier requirement of certified copies.¹²

Perhaps the most important revision from earlier drafts of the Implementing Regulations is article 3(4), which permits the EC Commission to waive any requirement in the Implementing Regulations or Form CO if it considers the information requested to be unnecessary to the EC Commission in its evaluation of the anticompetitive effects of the merger. As a practical matter, article 3(4), in conjunction with recital (8) of the Implementing Regulations, which permits informal discussions with the merger authorities prior to notification of the proposed merger, may allow companies to negotiate what information they will provide the EC Commission in Form CO, thereby decreasing the burdensomeness to the parties of the notification process.¹³

Article 5, likewise, contains a time-saving "conversion clause." Under this provision, if a merger notification is filed with the EC Commission, but the EC Commission determines that the merger is in fact a joint venture, the EC Commission may treat the merger notification as a joint venture notification which is required under the Treaty of Rome.¹⁴

¹⁰ - Continued

1990), p. 5 (hereinafter "Implementing Regulations"). Form CO Relating to the Notification of a Concentration Pursuant to Council Regulation (EEC) No. 4064/89. OJ No. L 219 (Aug. 14, 1990), p. 11 (hereinafter "Form CO"). Commission Notice Regarding Restrictions Ancillary to Concentrations, OJ No. C 203 (Aug. 14, 1990), p. 5 (hereinafter "Notice on Ancillary Restrictions"). Commission Notice Regarding Concentrative and Cooperative Operations under Council Regulation (EEC) 4064/89 of 21 December, 1989 on the Control of Concentrations Between Undertakings OJ No. C 203 (Aug. 14, 1990), p. 10 (hereinafter "Joint Ventures Notice").

¹¹ The EC Commission had originally required 20 copies of all supporting documents. Commission Regulation (EEC) No. 90 of July 1990 (rev. 1., June 1, 1990) ("June draft") art. 2(2). See also EC Committee Position Paper on the Proposed Commission Regulation on Notifications, Time Limits and Hearings Provided for in Regulation 4064/89 of the Control of Concentrations, (IV/156/90 EN) May 10, 1990 (hereinafter "Notifications Paper") p. 2.

¹² See art. 2(3), June draft.

¹³ U.S. attorney in Brussels, telephone conversation with USITC staff, Aug. 10, 1990; U.S. attorney in New York, telephone conversation with USITC staff, Aug. 14, 1990.

¹⁴ 1992 - *The External Impact of European Unification*, vol. 2, No. 9 (July 27, 1990), p. 3.

Articles 13-15 provide for a hearing to be held in conjunction with the EC Commission's review of the transaction. Article 14 of the Implementing Regulations provides that the cases will be conducted by "officials appointed by the EC Commission,"¹⁵ but that they will not be public.¹⁶ Parties have the right to be heard, if they can demonstrate "a sufficient interest," a requirement that one organization submitting comments suggested was superfluous considering the self-evident nature of the merging parties' interest.¹⁷ As provided for in article 18(4) of the Merger Regulation, article 15 of the Implementing Regulation allows third parties, including "recognized workers' representatives," access to EC Commission proceedings. Under article 13, the EC Commission may summon any person to give oral testimony whether or not that person has an interest in the proceeding. Some have suggested, however, that persons testifying should be limited to those with a legitimate interest in the proposed transaction.¹⁸

Articles 6 through 10 of the Implementing Regulations set forth the deadlines for the evaluation of the merger, and the means of calculating time limits. Concern has been expressed that the Implementing Regulations exclude certain holidays from time periods allotted under articles 10(1) and 10(3) of the Merger Regulation dealing with EC Commission time limits for vetting the merger¹⁹ but do not extend a similar benefit to the time periods in article 4(1) regarding the deadline for filing a notification; nor do the Implementing Regulations make it clear whether the month of August will be included in the list of holidays.²⁰ As such, parties wishing to merge should carefully note the holiday schedule before filing a Form CO.

Notification Form CO

Of greater importance to U.S. business is the EC's merger notification Form CO, recently adopted by the EC Commission. Article 4 of the Merger Regulation requires that all concentrations that have a "Community dimension" as defined in article 3 and that reach the thresholds established in article 1 must be notified to the EC Commission, and article 2 of the Implementing Regulations requires the use of Form CO for notification. Form CO, similar to the Antitrust Improvements Act Notification and Report Form required under the Hart-Scott-Rodino Antitrust Improvements Act of

¹⁵ It is still unclear just who these "officials" will be, but art. 21(1) of the Merger Regulation provides that the EC Commission has sole competence to take decisions under the Merger Regulation. Cases can, however, be appealed to the European Court of Justice, presumably to the Court of First Instance. Merger Regulation, art. 12(1).

¹⁶ Implementing Regulations, art. 14(4).

¹⁷ Implementing Regulations, art. 13(1); International Chamber of Commerce, *Working Paper on EEC Regulation on Merger Control* (May 10, 1990), (hereinafter "ICC Comments"), p. 7.

¹⁸ *Ibid.*, p. 4.

¹⁹ Implementing Regulations, art. 8.

²⁰ Notification Paper, p. 3.

1976 (hereinafter "HSR Form"),²¹ can be divided into five general sections that request the following data: (1) general information on the notifying parties, (2) the details of the nature of the concentration, (3) the ownership and control of the notifying party(ies), (4) the financial and personal links of the notifying party(ies), and (5) the markets that will be affected by the merger.

Form CO requires the merging parties to supply both objective factual information, similar to that found in the HSR Form, as well as qualitative judgments similar to those requested by the U.S. Department of Justice in its "second request."²² However, according to some U.S. businessmen, much of the information asked for in the Form CO is "irrelevant"²³ and too "detailed."²⁴ Although the final document has eliminated unnecessary detail from earlier drafts, many superfluous and immaterial questions remain. As a consequence, filling out the form in its present state may prove burdensome and time consuming for businesses.²⁵ The EC Commission has stated that Form CO is a compromise between its need for full information necessary to evaluate the likely competitive effects of the proposed transaction and the burden placed on companies in preparing for notification.²⁶ The EC Commission reportedly must ask for all of this information at the outset because, under the Merger Regulation, it must observe a strict, and very short, deadline for completing its review of the proposed transaction.²⁷ With the abundance of information with which the EC Commission then possesses, the need to make additional requests for information, thereby suspending the deadlines under article 10(3) of the Merger Regulation, will decrease.²⁸

The introductory provisions of Form CO require that the notifying party(ies) provide the EC Commission with not only the Form CO, but all

²¹ Hart-Scott-Rodino Antitrust Improvements Act of 1976, Pub. L. No. 94-435, 90 Stat., 1390; see also, 16 CFR Pts. 801-803.

²² U.S. attorney in Brussels, telephone conversation with USITC staff, Aug. 10, 1990. A "second request" is a request by the Department of Justice for additional information under the Civil Investigative Demand Statute, 19 U.S.C. sec. 1312.

²³ General counsel of U.S. multinational corporation, telephone conversation with USITC staff, July 11, 1990.

²⁴ Assistant general counsel of U.S. multinational, telephone conversation with USITC staff, July 12, 1990. American Chamber of Commerce Comments on Notification Form for Notifying a Concentration Pursuant to Reg. No. 4064/89 (DG IV, Draft 2, July 3, 1990) (hereinafter "Notification Comments"); *Comments on the American Bar Association Section on Antitrust Law With Respect to the Draft Form Notification of a Concentration*, transmitted to the EC Commission May 24, 1990 (hereinafter "ABA Comments").

²⁵ USITC staff meeting with EC legal experts, June 26, 1990 and July 3, 1990; General counsel of U.S. multinational corporation, telephone conversation with USITC staff, July 11, 1990; U.S. attorney in Brussels, telephone conversation with USITC staff, July 12, 1990. The ABA Comments suggest that Form CO is so burdensome as to raise the costs of completing it to the point of discouraging some mergers. ABA Comments, p. 5.

²⁶ See *European Report*, No. 1607 (July 28, 1990), pt. III., p.4.

²⁷ U.S. attorney in Brussels, telephone conversation with USITC staff, Aug. 10, 1990.

²⁸ *Ibid.*

relevant supporting documents.²⁹ This provision is similar to, and no more burdensome than, the U.S. procedure under provision 4(c) of the HSR Form.³⁰ The EC Commission, recognizing that some of the information requested will require submission of sensitive market information, the sharing of which with a competitor might raise questions of illegality under U.S. antitrust law, permits a notifying party to submit sensitive information relevant to the transaction under a separate cover.³¹ Concern has been expressed over the protection of this sensitive information, especially since the information is transmitted to all 12 member states. The EC Commission reportedly will limit access to the information and take strict precautions against harmful disclosure, but the risk of disclosure remains.³²

Section 1 of Form CO seeks basic information on the notifying party(ies). Section 2 requests general information on the concentration. Through section 2.4, the EC Commission solicits from the merging companies financial information for the past 3 years (reduced from 5)³³ in large part to determine whether the concentration meets the thresholds set forth in article 1 of the Merger Regulation. This information, if a U.S. parent is involved, may be in an entirely different format and not facily translated into the European format.³⁴ While some sources believe that much of the information asked for by the Form CO is not easily accessible to European subsidiaries of U.S. companies,³⁵ others have noted that firms will have sufficient time to gather the information necessary before filing the notification form and that U.S. firms will have to learn to function according to European rules if they plan to do business in the EC.³⁶

Section 3 of Form CO attempts to discover the corporate families of the notifying party(ies). Section 3.3, going beyond question 6 of the HSR form, which inquires as to the shareholders and holdings of the notifying party(ies), asks for identification of all companies controlled, directly or indirectly, by all parties who control, directly or indirectly, the notifying party(ies).³⁷ Although the

²⁹ Form CO, sec. C.

³⁰ U.S. attorney in New York, telephone conversation with USITC staff, Aug. 14, 1990.

³¹ Form CO, sec. E; see ABA Comments, pp. 7-8; ICC Comments, p. 7.

³² U.S. attorney in New York, telephone conversation with USITC staff, Aug. 14, 1990.

³³ See sec. 7, Draft 2 of Notification Form CO, Mar. 7, 1990 (hereinafter "2d Draft").

³⁴ U.S. attorney in Brussels, telephone conversation with USITC staff, July 12, 1990; Notification Comments, par. 10.

³⁵ General counsel of a U.S. multinational corporation, telephone conversations with USITC staff, July 11, 1990; and U.S. attorney in Brussels, telephone conversations with USITC staff, July 12, 1990.

³⁶ EC legal expert, conversation with USITC staff, Washington, DC, July 3, 1990.

³⁷ This provision touches on a concern raised by the proposed Ninth Company Law Directive concerning groups of companies, that the Ninth Directive might force companies to reveal connections they might prefer were not made public.

amount of information sought in this question is less than requested in earlier drafts, it has been opined that the EC Commission continues to request too much information concerning companies that are not involved in the concentration.³⁸ Another concern with this provision lies in what constitutes "control." Sections 3.1 through 3.3 define control by referring to article 3(3) of the Merger Regulation. This definition may allay the concerns expressed about the ambiguity of the term "control," but even it is not as explicit (e.g., names of shareholders of over 50 percent) as some would have liked.³⁹

Section 4 looks to the personal and financial links of the companies related to the notifying parties as disclosed in section 3. The final document sets forth specific questions concerning the links with which the EC Commission is concerned, replacing the broader request for information regarding "personal and financial links between each party concerned and . . . any other undertaking" found in an earlier draft.⁴⁰ This section only requires information on those companies in which companies disclosed in section 3 have a 10-percent holding.⁴¹ Section 4.3, requesting information on interlocking directorates, is similar to section 8 of the Clayton Act,⁴² which prohibits a person from simultaneously sitting on the boards of two competing companies. Unlike the Clayton Act however, Form CO does not, per se, prohibit interlocking directorates, but it does parallel U.S. law in confining its concerns to interlocking directorates with other companies active in affected markets.⁴³

Sections 5 and 6 seek information on the markets potentially affected by the merger. Section 5 of Form CO defines "product markets," "relevant geographical markets," and "affected markets," and seeks information in each area.⁴⁴ The final definition of "affected market" is narrower than that of earlier drafts, limiting the EC Commission's request for information to markets in which the merging parties have a combined market share of 10 percent or above in the EC market or a single

³⁸ U.S. attorney in New York, telephone conversation with USITC staff, Aug. 14, 1990.

³⁹ ABA Comments, p. 9; ICC Comments, p. 8; David G. Gill, Esq. letter to Denis Cross, May 8, 1990 (hereinafter "Gill letter") P. 2.

⁴⁰ Sec. 6, 2d Draft; ABA Comments, p. 10.

⁴¹ In the corresponding question in the 2d Draft, the threshold was 5 percent.

⁴² 15 U.S.C. sec. 19.

⁴³ Compare, sec. 6, 2d Draft (seeking the names of supervisory and management boards "of any other undertaking" regardless of its connection, or lack of connection, to the affected markets).

⁴⁴ One expert opined that the definitions of "product market" and "individual product groups" do not clearly distinguish the two and may in fact complicate answers on the affected markets. Hawk article. The definition of geographical market differs somewhat from that under U.S. law, relying slightly more on the geographical limits of demand rather than supply. U.S. antitrust attorney in New York, telephone conversation with USITC staff, Aug. 10, 1990.

member-state market (horizontal merger), or 10 percent or more of a market that is "upstream" or "downstream" from a market in which any other merging party is active (vertical merger).⁴⁵ Considerably less information is requested of parties to a "conglomerate merger," which is a concentration in which any one party controls 25 percent or more market share of any product, regardless of market overlap.⁴⁶

Much of the information sought by the EC Commission on "affected markets" has been scaled back from that sought in earlier drafts of the Form CO.⁴⁷ Furthermore, the phraseology of the questions, which asks the parties to "describe" various aspects of the proposed merger rather than answer predetermined questions, permits the parties to focus on important aspects of the market and the merger and to omit information irrelevant to the transaction.⁴⁸ Nevertheless, much of the information requested, such as that regarding market entry,⁴⁹ is considered to be hypothetical and speculative.⁵⁰

Overall, many U.S. experts agree that the EC Commission's final Form CO is a vast improvement over the first drafts but that it continues to solicit superfluous information. Consequently, a merger filing is likely to be a time-consuming, burdensome, and expensive endeavour.⁵¹

Notice on Ancillary Restrictions

The third document published by the EC Commission is the Notice on Ancillary Restrictions. Recital 25 of the Merger Regulation extends the control of the Merger Regulation to "restrictions directly related and necessary to the implementation of the concentration," (emphasis added) referring to what are generally known as "ancillary restrictions." Such ancillary restrictions will be evaluated in conjunction with the merger and hence will not be the subject of separate proceedings at the EC Commission.⁵² Section II(3),

⁴⁵ Compare sec. 5, 2d Draft. An "upstream market" refers to the market for supply and "downstream market" refers to the purchasing market.

⁴⁶ The threshold here was raised from the 10 percent threshold found in the 2d Draft. Sec. 8, 2d Draft.

⁴⁷ Compare sec. 6, Form CO, and sec. 9, 2d Draft; see also ABA Comments, pp. 6 to 7.

⁴⁸ Hawk Article; see also, ABA Comments, pp. 5-7.

⁴⁹ Form CO, sec. 6.4; Notification Comments, par. 10.

⁵⁰ General counsel of a U.S. multinational corporation, telephone conversation with USITC staff, July 11, 1990. See also ICC Comments, pp. 7-8 (The form should differentiate between facts known to the parties and assessments based on their best estimates); Gill letter, p. 2.

⁵¹ ABA Comments, pp. 2-4.

⁵² Notice on Ancillary Restrictions, sec. I, par. 1. To the extent the restrictions affect third parties, the restrictions may be subject to assessment under arts. 85 and 86 of the Treaty of Rome. Notice on Ancillary Restrictions, sec. I, par. 3. In addition, contractual arrangements that relate to the period prior to attainment of full control in a merger that is implemented in stages will be subject to review under arts. 85 and 86 of the Treaty of Rome. Notice on Ancillary Restrictions, sec. I, par. 4.

elucidating the principles of evaluation, however, provides that if "restrictive effects on third persons are separable from the concentration," they may be assessed separately under articles 85 and 86 of the Treaty of Rome. This provision, it is argued, violates article 22 of the Merger Regulation, which states that only the Merger Regulation applies to mergers that fall within the definition provided in article 3.⁵³ If a mere "effect" on third party would create jurisdiction, section II(3) may introduce an "effect's doctrine" into the jurisdictional analysis, in violation of both the letter and the spirit of the Merger Regulation. This approach raises the possibility that articles 85 and 86 will be invoked to evaluate a merger already approved under the Merger Regulation.⁵⁴

The EC Commission's Notice on Ancillary Restrictions attempts to clarify the method the EC Commission will employ in determining whether a restriction is "directly related" to a given merger for the purposes of Recital 25 of the Merger Regulation. Section II of the Notice on Ancillary Restrictions sets forth the principles for the EC Commission's evaluation of ancillary restrictions. These principles require that the restrictions be between the parties to the concentration and that any restriction be directly related and necessary to the concentration. In Section III, the EC Commission describes three examples of types of restrictions that, among others, would meet the criteria to be "necessary" ancillary restrictions: (1) non-competition clauses;⁵⁵ (2) licensing arrangements;⁵⁶ and (3) purchase and supply agreements.⁵⁷ At least one commentator has expressed reservations as to the EC Commission's reliance on these examples, preferring instead a case-by-case basis.⁵⁸ It is important to bear in mind, however, that the Notice sets forth general criteria and that

the list of necessary ancillary restrictions is illustrative, not exhaustive.

Recital 24 of the Merger Regulation brings within the purview of the Merger Regulation a joint acquisition of a third company with the intent of dividing the assets of the target company among the acquiring companies. Therefore, ancillary restrictions necessary to divide an acquired company will be considered directly related to the transaction and the competitive effects of such restrictions will be assessed in conjunction with the merger itself.⁵⁹ In cases of concentrative joint ventures,⁶⁰ the Notice on Ancillary Restrictions provides that, as with standard mergers, noncompetition clauses and licensing arrangements and, occasionally, purchase and supply arrangements will be evaluated along with the merger and not face separate proceedings under articles 85 and 86 of the Treaty of Rome.⁶¹

Joint Ventures Notice

The fourth document stemming from the Merger Regulation is the Joint Ventures Notice. Article 3(2) of the Merger Regulation defines two types of joint ventures for jurisdictional purposes: "concentrative joint ventures," which constitute concentrations for purposes of the Merger Regulation, and "cooperative joint ventures," which are not considered to be concentrations and will therefore be assessed under articles 85 and 86 of the Treaty of Rome.

The Joint Ventures Notice attempts to clarify the differences between a cooperative and concentrative joint venture. It first defines a joint venture as an undertaking that is jointly controlled by its parent companies. U.S. businesspeople have argued that this definition of a "joint venture" requires clarification.⁶²

Under the Joint Ventures Notice, if the EC Commission finds that joint control over an undertaking exists, it must then determine whether the joint venture is cooperative or concentrative as defined by the Merger Regulation.⁶³ To distinguish between the two, the Joint Ventures Notice focuses primarily on defining concentrative joint ventures, defining cooperative joint ventures essentially by default.⁶⁴ The first condition established by the

⁵³ Merger Regulation, arts. 3 and 22; EC Committee Position Paper Regarding the Draft Commission Notice on the Guidelines Relative to Ancillary Restrictions to Concentrations (June 29, 1990) (hereinafter "AMCham Ancillary Paper") p. 1.

⁵⁴ American Chamber of Commerce, *Final Draft EC Committee Position Paper on the Revised Draft Commission Notice on Guidelines Relative to Ancillary Restrictions to Concentrations*, (EC.Com 72/90) June 19, 1990 (hereinafter "Ancillary Position"), p. 1.

⁵⁵ Qualifying noncompetition clauses must be limited in time and geographical scope. Notice on Ancillary Restrictions, sec. III(A). The American Chamber of Commerce (AmCham), however, suggests that such noncompetition clauses are not restraints on trade and therefore are not covered by art. 85(1) of the Treaty of Rome. Ancillary Position, p. 4.

⁵⁶ Licenses may cover both present patents and know how as well as future improvements to those patents and know how. Notice on Ancillary Restrictions, sec. III(B). The necessity of exclusive licenses, and hence their consideration as an "ancillary restriction," will depend on the terms of the agreement; all territorial licenses must be limited. Notice on Ancillary Restrictions, sec. III(B), par. 3.

⁵⁷ Purchase and/or supply agreements between the joint ventures and one or more parent(s) will be permitted for a transitional period. Notice on Ancillary Restriction, sec. III(C). Exclusive purchase and supply arrangements will not be considered ancillary restrictions falling under the Merger Regulation, but instead will be subjected to review under arts. 85 and 86 of the Treaty of Rome.

⁵⁸ ICC Comments, p. 4; Gill letter, p. 3.

⁵⁹ Notice on Ancillary Restrictions, sec. IV.

⁶⁰ See below for discussion of concentration joint ventures. See also Merger Regulation art. 3(2), and Joint Ventures Notice.

⁶¹ *Ibid.*, sec. V.

⁶² The American Chamber of Commerce, noting that minority shareholders frequently have the power to veto various corporate decisions, suggests that joint control exists if a parent company has veto power over commercial decisions of the undertaking. American Chamber of Commerce, *Final Draft EC Committee Position Paper Regarding Revised Draft Commission Notice on the Distinction Between Concentrative and Cooperative Operations Under the Merger Control Regulation*, (EC.Com 72/90) June 19, 1990 (hereinafter "J/V Paper").

⁶³ There has been criticism that the Joint Ventures Notice focuses too much on concentrative joint ventures, and hope that the Commission will issue greater clarification on cooperative joint ventures. U.S. attorney in Brussels, telephone conversation with USITC staff, Aug. 10, 1990.

⁶⁴ U.S. antitrust attorney in Brussels, telephone conversation with USITC staff, Aug. 10, 1990.

Merger Regulation for characterizing a concentrative joint venture is that the joint venture must perform "on a lasting basis all the functions of an autonomous economic entity."⁶⁵ Characteristics such as being an independent supplier and buyer on the market, the ability and intention to carry out a chosen activity for the long term,⁶⁶ and the ability to formulate independent commercial policy suggest that the venture is an "autonomous economic entity."⁶⁷ The second condition established by the Merger Regulation is that the activity of the joint venture must "not give rise to coordination of the competitive behavior of the parties."⁶⁸ The Joint Ventures Notice expands on that provision, stressing that "competitive commercial freedom of the parents and of the joint venture must be preserved."⁶⁹ The definition of a concentrative joint venture is considered fairly strict, and may result in most joint ventures falling outside the Merger Regulation and hence becoming subject to review under articles 85 and 86 of the Treaty of Rome.⁷⁰

The Joint Ventures Notice sets forth four situations as examples of ways in which the EC Commission might differentiate between a concentrative and a cooperative joint venture. First, joint ventures that fully engage in business activities formerly engaged in by the parents are likely to be deemed concentrative joint ventures.⁷¹ Secondly, joint ventures that commence new activities on behalf of the parent companies are likely to be deemed concentrative joint ventures.⁷² Thirdly, joint ventures that operate in the same market as do one or more parent companies are likely to be deemed cooperative joint ventures.⁷³ Lastly, joint ventures that perform in the same upstream or downstream markets as do one or more parent companies are likely to be deemed cooperative joint ventures, although ventures falling within this category will be analyzed on a case-by-case basis.⁷⁴

⁶⁵ Merger Regulation, art. 3(2).

⁶⁶ In determining the intended life of the joint venture, the Joint Ventures Notice stresses that more important than the agreed duration of the joint venture are the human and material resources that have been allocated to the joint venture. Joint Ventures Notice, sec. II(B)(1).

⁶⁷ *Ibid.*

⁶⁸ Merger Regulation, art. 3(2).

⁶⁹ Joint Ventures Notice, sec. II(B)(2). The second paragraph needs clarification as to what types of cooperation between a parent and a joint venture are acceptable. J/V Paper, sec. 4. The joint-venture action as a supplier to or a purchaser from the parent(s) in the initial stages of the joint venture should not always preclude a finding of economic independence. ICC Comments, p. 4.

⁷⁰ Hawk Article; ICC Comments, p. 4.

⁷¹ Joint Ventures Notice, sec. II(B)(2)(a). The impact of the "spill-over effect" in related markets needs to be clarified as references to it throughout the text will lead to legal uncertainty. J/V Paper, sec. 5.

⁷² *Ibid.*, sec. II(B)(2)(b).

⁷³ *Ibid.*, sec. II(B)(2)(c). The presumption that the presence of a parent in the joint venture's market as a supplier or purchaser will lead to coordination is overly restrictive and needs clarification. J/V Paper, sec. 7.

⁷⁴ Joint Ventures Notice, sec. II(B)(3)(d).

The Joint Ventures Notice concludes by discussing other types of relationships between undertakings, such as minority shareholdings, cross-shareholdings, representation in the governing bodies of other undertakings, transfers or parts of undertakings, and joint acquisitions of an undertaking in order to divide the company.⁷⁵ In each of these situations the EC Commission will assess the extent to which one undertaking has acquired decisive control over another and the extent to which there is an economic as well as a legal merger.

Thirteenth Company Law Directive

Since the publication of the first followup Report, little action has been taken on the Proposed Thirteenth Company Law Directive concerning takeovers and other general bids (hereinafter "13th Directive").⁷⁶ Earlier this year, the EC Commission sent to the EC Council a "communication" in which the EC Commission set forth its plans to limit the use of "poison pills" takeover defenses. The EC Commission pointed out two principal means by which companies thwart takeover attempts: (1) a company's ability to buy back its own shares and a subsidiary's ability to buy shares in the parent; and (2) restrictions on voting rights, manipulation of proxy voting, and ability to change the management board of a company.

The communication from the EC Commission to the Council also suggested amendments to other directives to facilitate the takeover process in the EC. Specifically, the EC Commission recommended an amendment to the Second Company Law Directive,⁷⁷ limiting a parent and its subsidiaries to holding 10 percent of the parent company's capital. In addition, the subsidiaries could not exercise their voting rights at a general shareholders' meeting.⁷⁸ The communication also advocated amending the Fifth Company Law Directive⁷⁹ to strengthen the one-share, one-vote principle as well as adding a provision guaranteeing that a simple majority could replace the board of directors.⁸⁰

In addition, a revised proposed Thirteenth Company Law Directive will be submitted to the EC Council incorporating four amendments suggested by the Parliament. The first amendment by the Parliament would limit the application of the 13th Directive to companies quoted on a stock exchange. The second amendment encourages transparency by requiring the acquirer to explain the financing of the takeover bid and the financial consequences for

⁷⁶ *Ibid.*

⁷⁷ *Proposal for a Thirteenth Company Law Directive Concerning Takeovers and Other General Bids*, Com (88) 823, OJ C 64 (Mar. 3, 1989) (hereinafter "13th Directive").

⁷⁸ *Second Council Directive*, 77/91, OJ No. L 26, (Jan. 3, 1977) (on the formation and capital of public limited companies).

⁷⁹ "EC Takeover Rules: Merger Law Develops," *Europe 1992, Law and Strategy*, vol. 1, No. 6 (June 1990), p. 3; European Report, No. 1584 (May 5, 1990).

⁸⁰ *Amended Proposal for a Fifth Directive Funded on Article 54(3)(g) of the EEC Treaty Concerning the Structure of Public Limited Companies and the Power and Obligations of Their Organs*, Com (83) 185 OJ No. C 23/11, (Jan. 25, 1989).

⁸¹ *Ibid.*

the target company following a successful takeover. The third amendment, made necessary if greater power is given to shareholders at the expense of the directors, allows a company to call a shareholders' meeting, suspending the bid for the duration of the meeting. The fourth amendment accepted by the EC Commission dictates general guiding principles for the national merger authorities created by the 13th Directive.⁸¹ Other recent proposals include recommendations for the abolition of laws limiting voter rights,⁸² for restrictions on the number of nonvoting or limited voting shares a company may issue, and for the abolition of rules that require an absolute majority of votes to remove a company's board of directors.⁸³

Resistance to the 13th Directive continues to be expressed by various sectors of the economy. The European Union of Industrial and Employers' Conferences (UNICE) has shown opposition to the facilitation of takeovers, due in large part, to the antitakeover culture prevalent on the continent.⁸⁴ In addition, banks in the Federal Republic of Germany have been resistant to the 13th Directive, mostly because it would restrain the current German practice of the banks voting by proxy for customers whose shares they hold.⁸⁵ Although the French and German views seem representative of most of the continental states, British members of UNICE have been more receptive to the proposal.⁸⁶

European Company Statute

The European Company Statute (ECS) continues to be the topic of discussions in Brussels, but many U.S. companies remain ambivalent about its usefulness or appeal.⁸⁷ The largest remaining problem centers on how a "Societas Europea" (SE) will be taxed. The EC Commission wants the SE to be tax neutral (i.e., paying taxes equivalent to national companies) but recognizes that it must create tax incentives to offset the worker-participation provisions. A package of corporate tax provisions adopted by the finance ministers in mid-June is a step toward harmonizing corporate tax provisions.⁸⁸ These provisions do not

directly address the taxes that an SE would pay, but they do indicate that compromise in the tax area, seen as critical for the success of the ECS, is possible.

The other important activity concerning the ECS is the report from the Economic and Social Committee of the European Parliament.⁸⁹ The committee generally supports the work the EC Commission has done on the ECS. The committee offered both procedural and substantive suggestions to both the Regulation and the Directive.⁹⁰

The committee's procedural comments contained numerous requests for clarification, changes of deadlines, and harmonization of the language among the different-language versions. On the substantive level, the committee encouraged the EC Commission to increase the means under article 2 of the ECS by which small and medium-sized companies can participate in SEs.⁹¹ In commenting on article 38(1) of the regulation, the committee recommended that in addition to having the SE's capital denominated in ECUs, the national currency of the member state in which the SE is based should be an optional accounting unit.⁹²

The committee made numerous suggestions concerning the issuance and purchase of shares, including that an SE should be allowed to acquire its own shares to the same extent as national companies are permitted under the Second Company Law Directive;⁹³ that shares with multiple voting rights should be permitted;⁹⁴ that having national law govern the issuance, replacement, and cancellation of share certificates and the transfer of shares subject to national law is too problematic;⁹⁵ and that SE should be permitted to issue securities to persons who are not shareholders.⁹⁶

In the area of general management, the committee felt that too much authority was granted to the supervisory board at the expense of management,⁹⁷ that the duties of management and the supervisory board should be clearly defined,⁹⁸ that the protection of confidentiality was critical,⁹⁹ that the joint and several liability of all board members might be limited,¹⁰⁰ and that the members of the supervisory and management boards should

⁸¹ "EC Takeover Rules: Merger Law Develops," *Europe 1992, Law & Strategy*, vol. 1, No. 6 (June 1990) p. 3.

⁸² In France for instance, regardless of the number of shares a party owns, that party may not exercise more than 5 percent of the voting shares. Assistant general counsel of a U.S. multinational corporation, telephone conversation with USITC staff, July 12, 1990.

⁸³ "Mergers and Acquisitions in Europe Under the Merger Control Regulation and the Takeover Directive," paper by Gavin Darlington at the ABA Conference "1992 in Europe: A Practical and Legal Guide to Doing Business in the Single European Market," New York (June 7-8, 1990).

⁸⁴ Takeovers, hostile and otherwise, are infrequent occurrences on the continent. *European Report*, No. 1586 (May 12, 1990).

⁸⁵ *Ibid.*

⁸⁶ *Ibid.*

⁸⁷ General counsels of U.S. multinational corporations, telephone conversations with USITC staff, July 10, 1990, July 11, 1990, and July 12, 1990.

⁸⁸ See below, ch. 10, "Taxation."

⁸⁹ "Opinion on: the Proposal for a Council Regulation (EEC) on the Statute for a European Company, and on the Proposal for a Council Directive Complementing the Statute for a European Company with Regard to the Involvement of Employees in the European Company" OJ No. C 124, (May 5, 1990), p. 34 (hereinafter "Committee Opinion").

⁹⁰ As noted in the first follow-up, the ECS is composed of two parts—the Regulation creating a European Company, and the Directive "complementing the Regulation" containing the provisions for worker participation. See USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, p. 9-10.

⁹¹ Committee Opinion, par. 2.2.

⁹² *Ibid.*, par. 2.18.

⁹³ *Ibid.*, par. 2.24.

⁹⁴ *Ibid.*, par. 2.26.

⁹⁵ *Ibid.*, par. 2.28.

⁹⁶ *Ibid.*, par. 2.29.

⁹⁷ *Ibid.*, par. 2.36.

⁹⁸ *Ibid.*, par. 2.38.

⁹⁹ *Ibid.*, par. 2.39.

¹⁰⁰ *Ibid.*, par. 2.41.

be permitted to attend shareholder meetings.¹⁰¹ Concluding its remarks on the regulation, the committee encouraged the EC Commission to adopt tax provisions that would allow the adoption of the ECS itself.¹⁰²

Discussing the worker-participation provisions contained in the directive, the committee stressed that the workers should be involved in the strategic business decisions of the company. The committee expressed concern that the information and consultation provisions ensure that the employee

¹⁰¹ Ibid., par. 2.53.

¹⁰² Ibid., pars. 2.70-2.74.

representatives be informed and consulted *before* the decision is made by the directors in order that the provisions serve their true purpose.¹⁰³ Furthermore, the committee suggested that involvement by the employees of an SE's subsidiary in the decisions of the SE parent was necessary to ensure effective input into the decisions affecting their company.¹⁰⁴ The committee's closing concern was the means by which the EC Commission would guarantee that the parties would keep the agreements.¹⁰⁵

¹⁰³ Ibid., pars. 3.12 and 3.19.

¹⁰⁴ Ibid., par. 3.28.

¹⁰⁵ Ibid., par. 3.55.

CHAPTER 10
TAXATION

CONTENTS

	<i>Page</i>
Introduction	10-3
Developments covered in the previous reports	10-3
Recent developments	10-4
Introduction	10-4
Value-added tax	10-5
Clearing mechanism	10-5
Travelers' allowances	10-6
Reduced-rate VAT	10-6
Excise duties	10-6
Corporate taxation	10-7
Taxation of savings	10-8

CHAPTER 10 TAXATION

Introduction

EC tax initiatives related to the 1992 program have focused on three areas: (1) harmonization of indirect taxes (value-added taxes (VAT) and excise taxes), (2) action on three long-outstanding proposed directives regarding intracompany transfers, and (3) possible tax evasion resulting from the liberalization of capital movements. Amended article 99 of the Treaty of Rome requires harmonization of indirect taxes, and the 1985 White Paper identified harmonization of indirect taxes as being necessary if frontier controls are to be removed. Present border formalities add an estimated 1.5 percent to the cost of goods crossing member-state borders,¹ and an estimated 90 percent of that amount is associated with documentation related to VAT. The Treaty of Rome does not require that direct taxes (e.g., personal and corporate income taxes) be harmonized, and the White Paper made no new proposals with regard to harmonization of direct taxes. However, the White Paper called for action on three existing proposals relating to intracompany transfers. The White Paper also called for the liberalization of capital movements so as to allow the free movement of capital from member state to member state. This measure has given rise to efforts to impose a minimum withholding tax on interest income and to take other measures to discourage tax evasion.

Reaching agreement on tax issues has proven difficult. The process continues to move forward, with some issues resolved or partially resolved and others deferred. In its fifth report on implementation of the measures called for in the 1985 White Paper, issued in late March 1990, the EC Commission expressed concern with the "slowness" of the EC Council in responding to EC Commission taxation proposals, and noted that it had taken the Council more than 2 years to respond to the EC Commission's 1987 proposals on harmonization of indirect taxes. The EC Commission expressed the view that the months ahead represent "a major test of the Council's will" to resolve the more difficult issues.²

Developments Covered in the Previous Reports

The focus of EC tax harmonization efforts has been in the area of indirect taxes because these taxes are applied at member-state borders. Tax harmonization has been one of the most difficult

¹ P. Cecchini, *The European Challenge 1992: The Benefits of a Single Market*, (EC Commission, 1988), p. 9.

² *Fifth Report of the Commission to the Council and the European Parliament Concerning the Implementation of the White Paper on the Completion of the Internal Market*, Com (90) 90 final, Mar. 28, 1990, p. 27.

issues facing the EC 1992 effort because changes in rates and coverage can have significant revenue, political, and social implications for individual member states. Member-state sensitivity to the taxation issue is reflected in the fact that, under the Single European Act, EC actions involving taxation continue to require unanimous approval. All 12 member states have adopted the same basic VAT system, but no two states maintain the same rates or rate categories. Member states similarly employ different rates and approaches to excise, corporate, and other forms of tax.

In the case of indirect taxes, the 1985 White Paper stated that it would be impossible to remove frontier controls "if there are significant tax and corresponding price differences between the member states."³ In August 1987, the EC Commission issued a comprehensive fiscal package comprising seven proposed directives relating to VAT and excise duties and a working paper containing proposals for a VAT clearing mechanism. The package called for each member state to establish two VAT rates—a "reduced" and a "standard" rate—within respective rate bands of 4 to 9 percent and 14 to 20 percent, with the reduced rate to apply to such enumerated necessity products as food and the standard rate to apply to all other products. It also provided for a clearinghouse mechanism to adjust member-state revenues, on the assumption that VAT would continue to be paid in the state where the value was added but would be owed to the state in which the product was consumed (under present practice, when goods cross member-state borders VAT is rebated at the border and reimposed at the rate in effect in the importing member state). The package would also have set specific excise duty rates for alcohol, tobacco, and petroleum products.

Member states raised a number of concerns about various aspects of the package. Denmark and Ireland, which impose high VAT rates, would have been required to reduce rates and would have sustained revenue losses. Luxembourg, on the other hand, which imposes low VAT rates, was concerned about a potential loss of visitors from other EC countries if it had to raise rates. The United Kingdom, which currently zero-rates (imposes no VAT on) such products as food and children's clothing, would have been required to impose a rate of between 4 and 9 percent on such products. The proposed clearinghouse mechanism was criticized as being too complicated. The excise tax proposals, among other things, would have required several southern member states to impose taxes on wine. Such a requirement might have reduced wine consumption in favor of other beverages and thus adversely affected the local wine industry, and would have required West Germany to substantially increase its excise taxes on beer.

³ EC Commission, *Completing the Internal Market: White Paper From the Commission to the European Council*, June 1985, par. 175.

In May 1989, the EC Commission issued a communication outlining a "new approach" that sought to address many of the member states' concerns.⁴ The new approach provided for a transitional phase lasting until the end of 1992, limited zero rating, elimination of the rate cap, simplification of the clearing mechanism, and improved flexibility in excise rates.

In December 1989, the Economic and Financial Council of Ministers (ECOFIN), after taking into account the EC Commission's 1987 and May 1989 proposals, reached agreement on five following points regarding VAT: (1) member states should agree to compulsory VAT rate bands for reduced and lower rates by December 31, 1991; (2) member states should not diverge further from their current standard rates, and any changes should be towards the proposed 14- to 20-percent standard rate band; (3) the lower rates presently operating will remain at their present levels until December 1991; (4) member states that presently apply a zero rate will be able to retain it, but no new introduction of zero rating will be permitted; and (5) in 1992 the new VAT system will follow the simplified destination principle (advocated by the ECOFIN Council, as opposed to the simplified country-of-origin system advocated by the EC Commission). The EC Commission viewed the Council's conclusions as falling "somewhat short of the Commission's proposals."⁵

The EC Commission in June 1989 acknowledged criticism of its excise tax proposals and in November 1989 submitted amended proposals for Council directives on the approximation of taxes on alcohol, tobacco, and mineral oils (principally gasoline, diesel, and heating oil). The EC Commission proposed the introduction of minimum rates for all products subject to excise duty except for certain petroleum products, for which rate bands would be used to avoid possible distortions in competition. Member states would be required to implement the new minimum rates or rate bands no later than January 1, 1993. The EC Commission also presented "target rates" for tobacco and alcohol, which would not be compulsory but would indicate the levels at which the EC Commission desired rates to converge over the longer term. The EC Commission indicated that it would propose target rates for mineral oils by December 31, 1991. Under the amended proposal, the Council would examine the minimum and target rates every 2 years and make adjustments based on changes in real value and budgetary, environmental, health, energy, or transport policy considerations. With the exception of diesel oil, all of the proposed minimum rates were lower than the 1987 proposed rates, but all of the announced target rates were higher than the 1987 rates.

⁴ *Completion of the Internal Market and Approximation of Indirect Taxes*, Com (89) 260 final, June 14, 1989.

⁵ *Fifth Report of the Commission to the Council and the European Parliament Concerning the Implementation of the White Paper on the Completion of the Internal Market*, Com (90) 90 final, Mar. 28, 1990, p. 26.

In anticipation of the liberalization of capital movements on July 1, 1990, the EC Commission, at the urging of several member states, issued a proposed directive in January 1989 providing for the establishment of a minimum 15-percent withholding tax on interest income. The measure was strongly opposed by the United Kingdom, Luxembourg, and West Germany. While opposition to a minimum tax continued, broad agreement was reached at ECOFIN Council meetings in November and December 1989 (with Luxembourg expressing reservations) on methods to reinforce measures on cooperation among national tax authorities in the case of suspected tax evasion.

Significant differences continue to exist between member-state corporate tax systems. Tax rates, systems, and definitions of tax base differ, sometimes widely, from state to state. Corporate tax rates range from 34 and 35 percent in Luxembourg and the United Kingdom, respectively, to 50 percent in Denmark and West Germany. Provisions related to depreciation, other deductions, and investment credits vary. Some member states, such as the Netherlands and Luxembourg, follow a classical system (as does the United States) and in effect tax corporate profits twice—first at the corporate level and again (as dividends) at the shareholder level. The United Kingdom follows an imputation system, under which shareholders receive a tax credit, and West Germany follows a "split-rate" system, under which distributed profits are taxed at a lower rate than undistributed profits. The three proposed intracompany transfer directives addressed by the White Paper date back to 1969 and 1976. The first would eliminate the double taxation that can arise in certain states when dividends are paid by a subsidiary to its parent company; tax would be imposed only at the subsidiary level. The second would facilitate cross-border mergers and demergers within the EC and would lead to deferrals of recapture of depreciation, capital gains, and similar tax charges. The third would provide for an arbitration procedure if competent tax authorities are unable to agree on some kind of relief in the case of double taxation resulting from, for example, conflicts of law or different approaches in collecting revenue.

Recent Developments

Introduction

The EC continued to move forward on taxation matters during the first half of 1990. With regard to VAT, discussions were held in February concerning the scope of a lower rate VAT, and in May the Commission presented proposals for the transitional arrangements for the collection of VAT during the interim period January 1993-December 1996. In April, a compromise proposal was advanced for a phaseout of VAT-related restrictions on out-of-state purchases by travelers, which must

occur by January 1, 1993, but no agreement was reached. With regard to company taxation, in April the EC Commission issued a major communication on company taxation, and in June the Council approved all three of the proposed corporate tax directives after a compromise was reached with West Germany. The liberalization of EC capital movements became effective as scheduled on July 1, 1990, without final action on any of the proposed anti-tax-evasion measures.

Value-Added Tax

Developments in the VAT area during the first half of 1990 focused on three issues: (1) the clearing mechanism to be employed after December 31, 1992, when frontier controls are to be eliminated; (2) the phaseout of VAT travelers' allowances, which must occur by the end of 1992; and (3) the scope of a lower rate VAT.

Clearing Mechanism

In May 1990, the EC Commission proposed a transitional system of VAT taxation, to take effect January 1, 1993, when frontier controls are to be eliminated.⁶ This system generally conforms with that agreed to by the ECOFIN Council in late 1989 (see point 5 of the five points agreed to by the ECOFIN Council in December 1989, listed previously). In late June, the EC Council called for adoption by the end of 1990 of arrangements that are to apply beginning January 1, 1993.⁷ The Council was scheduled to take up the EC Commission proposal in July. Under this system, which would remain in effect through 1996, goods would circulate throughout the Community without being taxed, and VAT would be collected in the country where the goods are consumed. The EC would end its current practice of collecting VAT in the country of origin, at least for the transitional period. Instead, VAT will be paid by the purchaser according to the rate and conditions in the purchaser's country.

The transitional system would make use of tax-declaration procedures already in use in member states, and no new forms would have to be created.⁸ The purchasing entity would declare VAT on its purchases in a periodic declaration already used for internal operations and sent to its national tax administration.⁹ This declaration includes a list of sales and purchases made and exempt operations and indicates whether the enterprise is taxable. VAT

⁶ Proposal for an Amendment to the Proposal for a Council Directive Supplementing the Common System of Value Added Tax and Amending Directive 77/338/EEC, Com (90) 182 final, May 17, 1990, *Official Journal of the European Communities*, No. C 176 (July 17, 1990), p. 8 (hereinafter Com (90) 182 final).

⁷ "European Council Presidency Conclusions," *European Community News*, June 27, 1990, p. 2.

⁸ The EC Commission estimates that the elimination of customs documents and prior checks used intra-Community will ease considerably the administrative burdens on firms and will result in the elimination of 50 to 60 million forms, each with 50 boxes, per year. EC Commission, "The Taxation" dossier, June 19, 1990, p. 4.

⁹ Com (90) 182 final, par. (k)4.

on new motor vehicles would be collected in the country of first registration.¹⁰ Mail-order sales would be covered by a special system, under which the seller (or its representative in the country of delivery) would collect VAT at the rate in effect in the country of delivery. This provision would apply to mail-order sellers with annual turnover in excess of 1 million ECU.¹¹

To reduce the likelihood of fraud, those liable for VAT will be required to have an invoice or similar proof of acquisition that clearly states the price exclusive of tax at each rate and of any exemptions.¹² In the case of a transaction involving taxable persons, the VAT registration numbers of both the supplier and the purchaser of the goods will be required to appear on the invoice.¹³ The periodic declaration will have to list the amount of the intra-Community sales and purchases made by the firm. In addition, the EC Commission is proposing to introduce a system designed to strengthen cooperation between the various member-state fiscal administrations as well as to set up a European statistical system for intra-Community trade to make it possible to identify possible irregularities of operators the basis of on the evolution of intra-Community trade.¹⁴

The EC Commission, however, continues to favor as the ultimate system a modified version of the clearing mechanism it proposed in 1987, under which VAT on goods traded within the Community would be paid in the country of origin at the rate applicable there, but importers would be able to claim it back in the importing country in the same manner as on goods purchased domestically.¹⁵ The EC Commission-proposed clearinghouse system would compensate the various national treasuries for any imbalances, since the tax is ultimately owed to the treasury of the consuming country. This system, in the view of many, would make fraud difficult, because the goods would be traded with the VAT already paid.¹⁶ However, the various

¹⁰ *Ibid.*, par. (k)2.

¹¹ *Ibid.*

¹² *Ibid.*, par. (k)3. See also *European Report*, No. 1583 (May 3, 1990), sec. II, p. 4.

¹³ Com (90) 182 final, par. (k)3(b).

¹⁴ EC Commission information memo, "Commission Supplements Its Proposals for Abolishing Tax Frontiers," May 8, 1990, p. 3; see also, *European Report*, No. 1583 (May 3, 1990), sec. II, pp. 4-5.

¹⁵ In an information memo issued at the time it announced the transitional arrangements, the EC Commission stated that these arrangements would expire at the end of 1996 "at the latest," and that between now and the end of 1996 new arrangements would be proposed "for the transition to the definitive system of taxation in the country of origin." EC Commission, "Commission Supplements its Proposals for Abolishing Tax Frontiers," May 8, 1990, p. 2.

¹⁶ See, e.g., "Single Market Phooey: Europe's 1992 Plans Are Still Threatened by Tax Inspectors," *The Economist*, Jan. 13, 1990, p. 16: "Governments are removing border controls by devising bureaucratic substitutes for them, not by removing the underlying need for them [the differences in excise and VAT rates]. Finance ministers know this, but have postponed until 1996, at the earliest, a fraud-proof VAT system that would indeed allow Europe to become a single market.... Governments should allow VAT paid anywhere in the EC to be VAT

member states objected to this approach out of concern that the various national treasuries would not accurately report the VAT revenues raised.¹⁷ The United Kingdom expressed strong support for the transitional arrangements and expressed the view that they should be made permanent if they work.¹⁸

Travelers' Allowances

Beginning January 1, 1993, all EC citizens are to be able to transport personal goods duty free while traveling inside the Community. In July 1989, the EC Commission had proposed that ad valorem duty-free allowances granted to EC travelers for goods subject to VAT be increased in three roughly equal stages from 390 ECU to 800 ECU as of January 1, 1990; 1,200 ECU as of January 1, 1991; and 1,600 ECU as of January 1, 1992.¹⁹ The EC Commission further proposed, for the most part, a tripling of the quantity of certain goods subject to excise taxes (tobacco, cigarettes, and alcohol) that over this period travelers could enter duty free.²⁰ However, several member states declined to go along with this proposal because of the potential revenue loss.

In early April 1990, the Netherlands proposed a compromise that would raise the ECU limit from 390 to 600, effective January 1, 1991, and would provide derogations for Denmark, Greece, and Ireland, which are particularly concerned about possible revenue loss.²¹ However, the Dutch proposal was opposed by Belgium, Denmark, Ireland, Greece, and Portugal at the Finance Ministers meeting in Luxembourg in late April.²² Denmark and Ireland are concerned about losses of revenue, and Belgium expressed the view that such allowances should not be raised until VAT rates and excise duties are approximated, so as to avoid substantial trade distortions and revenue losses.²³ Italy indicated it

would seek to resolve the travelers'-allowance issue during its presidency, which began July 1.²⁴

Reduced-Rate VAT

At the ECOFIN meeting in December 1989, it was agreed that member states should agree to compulsory VAT rate bands for reduced and lower rates by December 31, 1991 (see point 1 of the five points listed previously). An experts group attached to the EC Council of Ministers discussed the matter in February 1990. Several member states supported the concept of a dual reduced-rate system—one mandatory, covering certain basic goods such as foodstuffs, and the other optional, covering certain goods and services that would not give rise to distortions in trade, such as restaurant and catering services.²⁵ No definitive list of optional goods was produced.

Member states have not yet agreed to a compulsory rate band for reduced and lower rates. The EC Commission proposed a reduced-rate band of 4 to 9 percent in 1987. Italy has suggested an extra lower rate of 2 percent, an even further digression from Denmark's current single VAT rate of 22 percent.²⁶ The EC Commission opposes a dual reduced-rate system out of concern that such a system will produce distortions in competition for imported goods.²⁷

Excise Duties

Member states are to reach agreement on excise duty rates by December 31, 1991. The EC Commission in November 1989 proposed new minimum rates and rate bands to take effect January 1, 1993, and higher "target" rates on alcoholic beverages, tobacco products, and mineral oils, to take effect at some later unspecified date. Member-state experts within the Council of Ministers examined the proposed rates on alcoholic beverages in March, but made little progress.²⁸ No significant developments occurred with respect to proposed rates on tobacco products and mineral oils.

There continue to be major differences in approach between northern and southern countries principally with respect to alcohol and tobacco products, with the former favoring relatively high rates for health and revenue reasons, and the latter favoring lower rates so as not to adversely impact local industries.²⁹ These differences resurfaced at Council of Ministers meetings in February and March. The southern countries traditionally have been large producers and consumers of wine. Greece, Italy, Portugal, and Spain oppose imposition of even a small excise duty on wine

¹⁶ —Continued

deductible everywhere else. They should then use a simple settlement system to steer the accustomed tax flows to each exchequer. They have already conceded the need for this in principle, but would rather delay fiscal 1992 until after 1996, without saying so."

¹⁷ *European Report*, No. 1605 (July 21, 1990), sec. II, p. 2. The Economic and Social Committee (ESC) also expressed concerns about the EC Commission's proposed clearing mechanism. ESC identified two risks in the case of cross-border transactions: (1) an increase in "taxi" operations, in which false VAT bills are issued in one country and the VAT is then refunded in another; and (2) in the black market economy, the fact that a bill could be obtained for refundable (though unpaid) VAT, thereby reducing the tax-free sale price and acting as a powerful incentive to trade in such products. "Opinion on the Communication From the Commission to the Council and to the European Parliament on Completion of the Internal Market and Approximation of Indirect Taxes," *OJ*, No. C 62 (Mar. 12, 1990), p. 18.

¹⁸ L. Kellaway, "Brussels Seeks Early Agreement on VAT Collection Compromise," *Financial Times*, May 9, 1990, p. 2.

¹⁹ *Proposal for a Council Directive Amending Directive 69/169/EEC to Increase in Real Terms the Tax Paid Allowances in Intra Community Travel*, Com (89) 331 final, *OJ*, No. C 245 (Sept. 26, 1989), p. 5.

²⁰ *Ibid.*

²¹ *European Report*, No. 1579 (Apr. 12, 1990), sec. II, pp. 2-3.

²² *European Report*, No. 1581 (Apr. 25, 1990), sec. II, p. 1.

²³ *European Report*, No. 1605 (July 21, 1990), sec. II, pp. 3-4; and *European Report*, No. 1594 (June 13, 1990), sec. II, p. 3-4.

²⁴ *European Report*, No. 1594 (June 13, 1990), sec. II, p. 4.

²⁵ *European Report*, No. 1565 (Feb. 21, 1990), sec. II, p. 5.

²⁶ *Ibid.*

²⁷ *Ibid.*

²⁸ No. 1569 (Mar. 7, 1990), sec. II, p. 2.

²⁹ See, e.g., "Tax: Harmonisation of Excise Duties," *EC Reports*, vol. 2, No. 4 (Apr. 1, 1990), p. 11.

because an excise duty will make wine more expensive, and if local consumers shift to other, less costly beverages, wine industries will be injured.³⁰

Tobacco firms in Italy, Portugal, Spain, Greece, and France have expressed opposition to the EC Commission's tobacco proposals out of concern that their adoption would have the effect of diminishing the price advantage of local products over the products of the large U.S. multinationals. The northern countries impose a "specific" system of taxation on tobacco products that results in relatively small differences in retail prices between different brands. However, the southern countries use a "proportional" system that provides flexibility in setting prices and allows local products to be more price competitive. Firms in the southern countries, particularly in Greece, contend that the changes required by the EC Commission proposal would fall most heavily on them.³¹

Corporate Taxation

In April the EC Commission issued a communication on company taxation,³² and in June the Council issued the three long-outstanding corporate taxation directives. The communication provided a somewhat different approach to harmonization of company taxation than the previous comprehensive proposal issued in 1975. In keeping with the principle of subsidiarity, the communication recommended that the Community "hold back on the harmonization of company tax systems" and that member states "remain free to determine their tax arrangements, except where these would lead to major distortions."³³ The communication acknowledged that there are many factors beyond differences in corporate tax burden that affect the decisions of direct investors, such as proximity to the market served, labor costs, the quality of public services, and local infrastructure.³⁴ The communication recommended that the Community concentrate on the measures essential for completing the internal market, and that the advisability and possible forms of company tax harmonization be "reexamined closely and on new bases before any proposals can be presented."³⁵

³⁰ *European Report*, No. 1567 (Feb. 28, 1990), sec. II., pp. 4-5; and *European Report*, No. 1569 (Mar. 7, 1990), sec. II., p. 2. See also G. Deiore's unpublished monograph involving Italian taxation presented at a conference in Washington, DC, Dec. 10-12, 1989, under the auspices of the Tax Executives Institute and the American Tax Institute in Europe, pp. 18-19; and C. Rodriguez Ramos, "Spain and the European Single Market Tax and Business Aspects," unpublished monograph presented at the same conference, pp. 16-17.

³¹ "Tax: Greece Stands Firm on Burning Issue," *EC Reports*, Mar. 1, 1990, p. 12; and *European Report*, No. 1582 (Apr. 28, 1990), sec. II, p. 2.

³² "Commission Communication to Parliament and the Council: Guidelines on Company Taxation," Sec (90) 601 final, Apr. 20, 1990.

³³ *Ibid.*, par. 5.

³⁴ *Ibid.*

³⁵ *Ibid.*, par. 6.

The communication identified the three outstanding proposed directives (on double taxation of parent company/subsidiary distributions, mergers, and arbitration procedures) and the tax measure linked to the proposal on the Statute for a European Company as measures that needed to be implemented as soon as possible.³⁶ It stated that the EC Commission would soon propose two new directives. The first would permit all companies engaged in transnational activities, irrespective of legal status, to take into account foreign losses at the company level.³⁷ The second would require the abolition of withholding taxes on interest and royalty payments within groups of companies.³⁸

The communication announced that the EC Commission was withdrawing its 1975 proposal for a directive on the harmonization of systems and rates of company taxation because it "no longer corresponds to the current situation in the Community."³⁹ The current Community approach, the communication said, "gives priority to the coordination and approximation of policies rather than to systematic use of harmonization."⁴⁰ The communication announced that the EC Commission would undertake a new study, which would be entrusted to a committee of experts, and would report back in a year's time.⁴¹ The committee would be asked to take into account the current state of Community integration and the results of the major tax reforms of the 1980s,⁴² and to answer four questions related to tax system-induced distortions and to the desirable level of Community company tax harmonization.⁴³

As indicated in the initial USITC report, there is a divergence of views within the EC concerning the desirability of comprehensive harmonization of

³⁶ *Ibid.*, par. 17.

³⁷ *Ibid.*, pars. 23 and 24. The communication stated that this proposal would be similar to its proposal for a Council regulation on the Statute for a European Company. The communication also stated that the proposal would deal with the treatment of losses of subsidiaries established abroad.

³⁸ *Ibid.*, par. 26.

³⁹ *Ibid.*, par. 30. The communication also noted that the 1975 proposal had not been discussed by either the Council or the Parliament in more than 10 years.

⁴⁰ *Ibid.*, par. 30.

⁴¹ *Ibid.*, par. 35.

⁴² *Ibid.*, par. 34.

⁴³ *Ibid.*, par. 35. Specifically (a) do the disparities that exist between corporation taxes and the tax burdens on companies from one member state to the next induce distortions in investment decisions affecting the functioning of the internal market? (b) If so, can those distortions be eliminated simply through the interplay of market forces and competition between national tax systems or are Community measures required? (c) Should any action at Community level concentrate on one or more elements of company taxation, namely the different corporation tax systems, the differences in tax treatment associated with the legal status of companies, the tax base or rates? (d) Should any measures envisaged lead to harmonization, approximation, or the straightforward establishment of a framework for national taxation? What would be the effect of such measures or the absence of such measures on Community objectives such as cohesion, environmental protection and fair treatment of small and medium-sized firms?

corporate tax systems. EC Tax Commissioner Christiane Scrivener reportedly is attracted to a Dutch Government suggestion that a floor be placed under corporate tax rates because "It is clear that we are going to have competition between states to cut rates, causing some governments budgetary problems."⁴⁴ Others have argued that a comprehensive harmonization of systems and rates would likely lead to higher levels of taxation and lower economic growth and that it would be better to let market forces put pressure on member-state governments to narrow their differences.⁴⁵

The ECOFIN Council approved the three intracompany transfer directives on June 11, 1990, after a compromise was reached with West Germany over levels of withholding tax to be applied to profits distributed between a parent and a subsidiary. European companies have regarded adoption of the three directives as essential and have regarded the Council's failure to adopt them as constituting one of the biggest barriers to doing business across the EC.⁴⁶ Under the compromise, West Germany will be initially exempted from the rule requiring elimination of all withholding tax on profits distributed between a parent company and a subsidiary. But it will be required to reduce its withholding tax from 10 percent to 5 percent by January 1, 1992, and to abolish it altogether by January 1, 1996.⁴⁷ Exemptions were also given to Greece, which currently has no corporate tax, until

it introduces a tax reform package, and to Portugal for an 8-year period.⁴⁸ The three measures were scheduled to be formally adopted in July and are to be implemented by January 1, 1992.

Taxation of Savings

The liberalization of capital movements and the opening of borders for capital flows required by Directive 88/361 became effective July 1, 1990, although derogations were provided for four countries (Spain, Ireland, Greece, and Portugal) concerning short-term capital movements until the end of 1992. The large, tax-related speculative capital movements feared by some have not occurred.⁴⁹ In May, Belgium sought to reopen the issue of a minimum withholding tax on savings interest, which the EC Commission had proposed in February 1989 and which Belgium and several other member states favor but West Germany, Luxembourg, and the United Kingdom oppose.⁵⁰ However, no further action was taken on either the withholding tax proposal or EC Commission proposals to strengthen cooperation between national tax authorities when tax fraud is suspected. Luxembourg, which has become a major European financial center, continues to oppose and block the cooperation proposals out of concern that they would abrogate current bank-secrecy commitments and encourage the shift of funds to other financial centers, such as Switzerland.

⁴⁷ - Continued

⁴⁴ D. Buchan, "Brussels Proposes Common Minimum Corporation Tax," *Financial Times*, Feb. 21, 1990, p. 2.

⁴⁵ See, e.g., J. Chown, *Company Tax Harmonisation in the EEC*, unpublished monograph (1989), app. 2, "History of Initiatives Taken," p. 1. There is a "serious danger that imposed harmonization could effectively create a tax collectors' cartel, perpetuating high rates and antiquated structures." Chown, p. 4.

⁴⁶ L. Kellaway, "Commission Reshuffles Cards for Company Tax Coherence," *Financial Times*, Apr. 23, 1990, p. 4.

⁴⁷ *European Report*, No. 1594 (June 13, 1990), sec. II, pp. 4-5. The issue is a complex one and will require changes in German tax law. West Germany imposes a higher rate of tax on undistributed profits than on distributed profits and did not see why it should allow subsidiaries to transfer their profits elsewhere. Further, West Germany has worked out arrangements with other countries, such as France and the United Kingdom, but has not worked out arrangements with any others, such as the Netherlands, which has large subsidiaries in West Germany. The issue had come down to a "trial of strength" between the

Netherlands, which was urging West Germany to abolish the tax, and West Germany, which was willing to reduce it but not abolish it. *European Report*, No. 1581 (Apr. 25, 1990), sec. II, p. 4; and L. Kellaway, "EC Tax Chief Enjoys a Rare Compromise," *Financial Times*, June 13, 1990, p. 20.

⁴⁸ *European Report*, No. 1594 (June 13, 1990), sec. II, pp. 4-5.

⁴⁹ *European Report*, No. 1600 (July 4, 1990), sec. II, p. 5.

⁵⁰ *European Report*, No. 1586 (May 12, 1990), sec. II, p. 5. See also "Resolution on Taxation of Interest," from the European Parliament, Doc. B3-398/90, Feb. 15, 1990, OJ No. C 68 (Mar. 19, 1990), p. 145, wherein the European Parliament expressed the view that "in the absence of appropriate approximation and tax cooperation measures the liberalization of capital movements entails a risk of delocalization of capital, tax evasion and tax avoidance, given the significant differences in rates of taxation on savings"; expressed regret that the Council had been unable to reach agreement on the establishment of a Community system of taxation on interest; and reaffirmed its position "that either a system of statement of income or a system of deducting tax at source will be necessary to solve the problems mentioned."

CHAPTER 11
RESIDUAL QUANTITATIVE RESTRICTIONS

CONTENTS

Developments covered in the previous reports	<i>Page</i>
Background and anticipated changes	11-3
Possible effects	11-3
Developments during January-June 1990	11-3
	11-4

CHAPTER 11

RESIDUAL QUANTITATIVE RESTRICTIONS

The elimination of intraborder controls in the EC's effort to create a single internal market will pressure the EC to transform existing or residual national quantitative restrictions (QRs) into EC-wide quotas or other protective measures, particularly in sensitive sectors. Although new EC-wide quotas are likely to be directed at Asian exporters rather than exports from the United States, new EC-wide barriers could intensify trade-diversionary effects, increase competition facing U.S. exporters in certain member-state markets, or increase competition for U.S. subsidiaries already located in the EC.

Developments Covered in the Previous Reports

Background and Anticipated Changes

EC member states impose numerous QRs in the form of quotas or gray-area measures (usually voluntary restraint agreements) on a large variety of products originating primarily in Eastern Europe and Asia. Many of these QRs were established by member states prior to the time they joined the EC and were grandfathered in. Others are linked to agreements concluded by the EC Commission, such as the Multifiber Arrangement and the Generalized System of Preferences. Effective enforcement of national QRs is currently safeguarded by article 115 of the Treaty of Rome.

Because the EC intends to remove all border controls between the member states by 1992, national QRs will be unenforceable in the integrated single market. Therefore, the EC has indicated that it plans to eliminate all member-state QRs and article 115 by 1992. However, the EC Commission has not issued any regulations or directives addressing QRs. The options facing the EC appear to be threefold: first, to unilaterally abandon existing national quotas; second, to transform existing national restrictions into EC-wide quotas; and third, to replace current national QRs with other EC measures, such as increased reliance on antidumping statutes, subsidization of sensitive industries, and higher tariffs.

The EC Commission has not yet identified those sectors that would require an EC-wide quota, with the exception of automobiles. Efforts to identify sensitive sectors and the impact of the elimination of article 115 are still under way. An EC Commission document issued in October 1988 listed two sectors in addition to automobiles that could require EC-wide measures—shoes and consumer electronics. The document also identified 12 sectors

that have trade problems that are not EC-wide in dimension and that accordingly would warrant more defined solutions, such as subsidization. EC Commission officials have acknowledged that certain struggling industries will require some form of protection from imports after the national restrictions are lifted. However, they claim that the plan for a transitional EC-wide import restraint in the automobile sector would not be extended to other industries.

Certain QRs are already being addressed by the EC Commission. For example, the EC is negotiating bilateral trade and economic cooperation agreements with Central and Eastern European countries and the U.S.S.R. that call for the elimination of national QRs imposed on exports from these countries. Also, the EC and Japan are consulting regularly over the removal of national QRs directed at Japan. The EC agreed to persuade individual member states to abandon certain QRs aimed at Japan after Japanese officials threatened to request dispute-settlement procedures in the GATT. Finally, the group of developing countries that are signatories to the Lome Convention grew concerned that the EC 1992 program would cause them to lose their preferential access to certain member-state markets for bananas and rum. However, the recent renegotiation of the Lome Convention incorporates provisions that should safeguard their privileged access.

Possible Effects

The first report identified three sensitive sectors—automobiles, footwear, and textiles and apparel—that would most likely be subject to EC-wide QRs after 1992. However, EC-wide quotas on these products would probably be directed at Far Eastern rather than U.S. products. Nonetheless, U.S. producers could be indirectly affected by this course of action. In footwear and textiles and apparel, a shift to EC-wide quotas could cause controlled suppliers to redirect shipments to markets where they have the greatest competitive advantage but that had been previously limited by a member-state QR, thereby increasing competition for U.S. exports in these markets. EC-wide QRs in footwear could also cause trade diversion to the United States.

Both U.S. automobile exporters and U.S. automakers with production facilities in the EC could benefit from the dismantling of member-state quotas and the subsequent protection afforded by an EC-wide restraint on Japanese automobile imports. U.S. automobile producers and their EC subsidiaries may be presented with increased marketing opportunities in the EC and should compete effectively as the EC's national automakers restructure because of the U.S. producers' reputation for quality. Although Japanese producers may continue to shift production facilities to the EC to avoid the threat of external trade barriers, U.S. firms are well positioned to meet

the competition. However, if the EC institutes local-content requirements on automobiles, Japanese-owned automakers in the United States could face barriers in exporting to the EC.

Developments During January-June 1990

The EC plan to remove national QRs imposed on imports of Japanese automobiles remained the central concern of the United States during the first 6 months of 1990. The U.S. Government continued to monitor EC efforts to replace member-state quotas with an EC-wide voluntary restraint arrangement with Japanese auto producers for a transitional period beginning no later than January 1, 1993. The administration aims to ensure that U.S. auto exports are not hurt by any change in EC auto policy, particularly that automobiles produced in the United States by Japan-based manufacturers will not be included in the voluntary restraint arrangement with Japan.¹ For a complete discussion of developments in the automobile sector during January-June 1990, see chapter 20 of this report.

The EC Commission still has not indicated how it intends to address national QRs in sensitive sectors other than automobiles.² However, EC Commission officials claim that the plan for a

¹ For more information, see U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States* (Investigation No. 332-267), USITC Publication 2204, July 1989, ch. 11; and U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States First Follow-Up Report* (Investigation No. 332-267), USITC Publication 2268, March 1990, ch. 11.

² For more background, see USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, ch. 11; and USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, ch. 11.

transitional EC-wide restraint in the automobile sector will not be extended to other industries. Caribbean nations continue to express concern that their preferential access to certain member-state markets for bananas will be eroded after the internal market is completed, but the EC Commission remains undecided on how to organize a common market for bananas after 1992.³ In another sector under discussion, on June 27 the EC invoked a safeguard action against imports of shoes from Korea and Taiwan. The Korean Government and the Taiwan manufacturers' association agreed to respect specified shoe quotas on exports to the EC for the next 3 years.⁴

The EC Commission continued to negotiate the removal of national QRs on imports from the Central and East European countries and the U.S.S.R. The first phase of negotiations establishing bilateral trade and economic cooperation agreements with the European CMEA countries⁵ is almost complete. As of June 30, 1990, the EC had signed bilateral agreements with Hungary, Poland, the U.S.S.R., Czechoslovakia, East Germany, and Bulgaria. An agreement with Romania has been initialed but awaits official signatures. For further information on the status and contents of these agreements, see chapter 1 of this report.⁶

³ "Bananas: Brief Calm in Intra ACP Storm," *European Report*, No. 1586 (May 9, 1990), sec. 5, p. 5.

⁴ Lafayette Publications, Inc., "EC to Monitor Shoe Imports," *Europe 1992, The Report on the Single European Market*, July 11, 1990, p. 711.

⁵ CMEA — the Council for Mutual Economic Assistance — consists of the U.S.S.R., Czechoslovakia, Hungary, Poland, Romania, East Germany, Bulgaria, Mongolia, Cuba, and Vietnam. The European CMEA includes all of the CMEA countries except Mongolia, Cuba, and Vietnam.

⁶ Also see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 1-6 to 1-8.

CHAPTER 12
INTELLECTUAL PROPERTY

CONTENTS

	<i>Page</i>
Developments covered in the previous reports	12-3
Background and anticipated changes	12-3
Semiconductor mask works	12-3
Trademarks	12-3
Copyright	12-3
Patents	12-3
Possible effects	12-3
Semiconductor mask works	12-3
Trademarks	12-3
Copyright	12-3
Patents	12-4
Developments since the last followup report	12-4
Patents	12-4
Background	12-4
Anticipated changes	12-4
Possible effects	12-5
U.S. exports to the EC	12-5
Diversion of trade to the U.S. market	12-5
U.S. investment and operating conditions in the EC	12-5
U.S. industry response	12-5

CHAPTER 12

INTELLECTUAL PROPERTY

Intellectual property rights in the EC are important to U.S. business interests, particularly for firms selling high-technology products that require significant development expenses and investments. With the advent of the 1992 program, the EC is establishing EC-wide regimes or partial harmonizations of national law on intellectual property.

Developments Covered in the Previous Reports

Background and Anticipated Changes

Semiconductor Mask Works

Council Directive 87/54 directs EC member states to enact laws for protection of semiconductor topographies (mask works), conforming to minimum standards in the directive. Most member states have complied or are complying with this directive.

Trademarks

Most member states have well-developed and generally similar trademark laws and have sought harmonization by creating an EC trademark regime parallel to the existing national regimes and by seeking partial harmonization among national regimes. Council Directive 89/104 is not a full-scale harmonization but is intended to approximate member-state laws on trademarks acquired by registration. Proposed Regulation (84) 470 would establish an EC-wide regime for trademarks with enforcement in the national courts. Proposed Regulation (85) 844 would implement the Regulation on the Community Trade Mark. Proposed Regulation (86) 731 would set rules of procedure for the Board of Appeals.

Copyright

Most of the member states have well-developed copyright laws. Green Paper (88) 172 is a consultative document discussing piracy, home-copying of sound and audiovisual works, distribution and rental rights for sound and video recordings, computer programs, data bases, and external aspects of copyright protection. It contains suggested courses of action that may be formally proposed and implemented by the EC or member states. In one area, computer software, a directive has been proposed ((88) 816). It would require member states to conform or to enact laws to treat computer programs as literary works under their national copyright laws and sets certain minimum standards and rights.

Patents

Although most member states have well-developed patent laws, the patent protection of biotechnological inventions is a major new issue. Proposed Directive (88) 496 would achieve partial harmonization of the patent laws of the member states with respect to biotechnological inventions. It provides, among other things, that an invention cannot be considered unpatentable simply because it is composed of living matter.

Possible Effects

Semiconductor Mask Works

Directive 87/54 should provide increased market opportunities in the EC for U.S. semiconductor firms. The United States has more than \$2 billion invested in semiconductor operations in the EC, and U.S. firms account for more than 40 percent of the European market, through local production and exports combined. Protection provided by the directive should facilitate both U.S. investment and, to a lesser extent, exports. Strong U.S. protection makes trade diversion to the United States unlikely, but competition in some third-country markets may increase as a result of trade diverted from the EC.

Trademarks

The creation and administration of an EC trademark will simplify the acquisition of trademark protection by non-EC suppliers, in addition to enhancing the average protection—and presumably enforcement—EC-wide. Similarly, the approximation of the trademark laws of member states can be expected to enhance protection and somewhat simplify acquisition by ensuring that registration and protection are handled similarly by all the member states. U.S. firms own a disproportionately large share of internationally well-known trademarks and should benefit accordingly. The effect of an adequately enforced EC trademark would be to protect and encourage U.S. investment. However, the overall benefit is expected to be moderate at best, because trademark protection is already very good in the EC as a whole and U.S. losses due to violations of trademark rights in the EC are on the low end of the scale internationally.

Copyright

Assuming that directives result from the Green Paper, the harmonization and strengthening of the member states' copyright laws will reduce piracy within the EC and increase the market for legitimate products regardless of origin. As such, both U.S. exports and U.S. investment in the EC would benefit to a great degree. The extent of protection in the proposed computer software directive is controversial, and its possible effects depend on how that controversy is resolved.

Patents

The proposed directive will probably liberalize trade by creating opportunities for U.S. producers of biotechnological products to enter the EC market. Greater patent protection would not only stimulate research and development in this industry, it would also reduce the risks associated with introducing biotechnological products into a new market. U.S. industries most likely to benefit are agriculture and chemicals. The proposed directive will probably benefit U.S. investment by creating opportunities for scale economies in research and development, thus allowing firms to more easily expand across member-state borders.

Developments Since the Last Followup Report

Since the last followup report, the EC Commission has proposed a Council regulation on the creation of a supplementary protection certificate for medicinal products ((90)/101), which is discussed below.

In addition, the European Parliament has given its opinion on the proposed computer software directive that was discussed previously in the first followup report. While approving of the proposed directive, the Parliament has called for several amendments.

Finally, the EC Commission has proposed continuing the extension of protection under the already-adopted mask works directive, discussed in the original report, for natural and legal persons of third countries past the current November 7, 1990, deadline. In doing so, however, the EC Commission has drawn a distinction between those third countries that have accorded full and unconditional protection to EC mask works and those countries, such as the United States, that have accorded protection to EC mask works on an interim basis until the end of 1992. The former would be accorded full protection under the proposal; the latter, interim protection. The EC Commission has also commenced formal complaint proceedings against Greece under article 169 of the EEC Treaty for the failure of that member state to timely implement the mask works directive.

Patents

Background

Member states of the EC provide patent protection for pharmaceutical products, processes, and methods of use under their national patent laws and pursuant to the European Patent Convention. However, as is the case in the United States, many pharmaceutical products require regulatory approval by national health authorities prior to marketing. Such regulatory approval may take considerable time and substantially reduce the period of exclusivity granted by the patent. The EC

Commission has proposed a regulation which would create a Communitywide system for obtaining "supplementary protection certificates" for the restoration of at least part of this period. The proposal is analogous to (and indeed was prompted by) legislation on pharmaceutical patent term restoration already in effect in the United States and Japan. Similar legislation was recently enacted in France. While the proposed regulation is not part of the White Paper, the explanatory memorandum that accompanies it states that it "represents a significant element of Community policy in the fields of industrial property and the pharmaceutical sector" and calls for its implementation by January 1, 1993, the same date as that set for completion of the internal market.

Anticipated Changes

Proposed Regulation (90)/101 on the creation of a supplementary protection certificate for medicinal products was submitted to the EC Council of Ministers by the EC Commission on April 3, 1990, and published in the *Official Journal* on May 8, 1990 (No. C 114/10). If adopted, the proposed regulation would create an instrument called a "supplementary protection certificate." This certificate would extend the term of patents for medicinal products granted by the member states under their national laws or patents granted under the European Patent Convention for those products.

Any preventive, diagnostic, or therapeutic medicinal substance that is protected by a patent in a member state and that is subject to a marketing authorization requirement as set out in Council Directive 65/65/EEC or Council Directive 81/851/EEC may be the subject of the proposed new certificate. The certificate would also extend to methods of making and using such substances. However, what is protected under the certificate is not necessarily coextensive with what is covered by the patent. Rather, protection is for the product covered by the marketing authorization and for any authorized use of the product before the expiration of the basic patent. Subject to this limitation, the certificate would confer the same rights as those conferred by the basic patent and would be subject to the same limitations as that patent.

An application for the certificate would be filed in the industrial property office of the member state that granted the basic patent and in which marketing authorization has been obtained. The application must be filed within 6 months of obtaining the marketing authorization or grant of the patent, whichever occurs last. To obtain the certificate, the patent covering the product (the basic patent) would still have to be in force, marketing authorization would have had to have been granted in that member state and would have to be the first such authorization therein, and the product could not have been previously the subject of a certificate in that member state. A fee may be

charged for the application and for maintenance of any certificate granted.

The duration of the certificate extends from the end of the term of the basic patent for a period equal to that which elapsed between the filing date of the basic patent and the date on which the first marketing authorization was granted by any member state, reduced by a period of 4 years. However, in no case may this additional period extend beyond 10 years.

Transitional provisions in the proposed regulation would extend its application retroactively to products protected by a patent on the day the regulation enters into force but for which marketing authorization has not yet been obtained. Further, the regulation would apply to products covered by a valid patent on the date the regulation enters into force if that patent will expire after July 1, 1992 and if the first marketing authorization in the Community was obtained after January 1, 1984. In the latter case, however, the maximum term of the certificate would be 5 years.

Possible Effects

In general, the possibility of extending the patent term for medicinal products for which marketing has been delayed pending the appropriate regulatory authorization will increase the period of exclusivity under the patent and thus increase the period during which the firm holding the patent may recover its investment in that product, thus encouraging research and development and innovation. These benefits would apply to U.S. firms operating in the EC.¹

U.S. Exports to the EC

As a result of an extended period of exclusivity, exporting firms whose patents would be extended under the proposed regulation could expect to maintain their market position in the EC for a longer period of time against generic competition. U.S. exports of pharmaceuticals amounted to approximately \$1.9 billion in 1989. However, most U.S. efforts in the EC involve local investment and production rather than U.S. exports.

Diversion of Trade to the U.S. Market

Since the U.S. already has pharmaceutical patent-term legislation in force, the proposed

regulation would not be likely to cause any diversion of trade to the U.S. market.

U.S. Investment and Operating Conditions in the EC

The extension of patent terms for medicinal products and the uniform application of the supplementary protection certificate will generally benefit U.S. investments in the EC and improve operating conditions, since it would provide a longer period of exclusivity to recover the ever-rising costs of research and development (R&D). Continued R&D is necessary for producers to maintain a level of innovation required to compete with sales of less expensive generic pharmaceuticals.

U.S. Industry Response

The Pharmaceutical Manufacturers Association (PMA) filed a submission in which it stated that the supplemental protection certificate will compensate for time lost in regulatory delay and will make an important contribution to restoring the economic viability of the pharmaceutical industry in Europe. PMA stated that this, in turn, should enable the industry to maintain its research and development commitment, which, according to PMA, amounts to an aggregate of over \$7 billion per year and some \$200 million per product.

PMA also stated that the proposed certificate should substantially enhance the competitive posture of European pharmaceutical companies relative to their U.S. and Japanese counterparts, which benefit from similar legislation in those countries. PMA states that the proposed certificate would place all parties on an equal footing and that it represents principles currently being debated in the Trade-Related Intellectual Property negotiations in the GATT. However, PMA states that the adoption of the proposed regulation will enhance the challenges facing U.S. industry as it strives to compete in Europe and in the global market place.

Despite these perceived relative adverse competitive effects, the PMA stated that it could not object to the proposed regulation since U.S. industry sought a similar measure in the United States and it was adopted in 1984.

¹ See ch. 22 for additional discussion of the possible economic effects.

PART III
IMPLICATIONS OF EC MARKET INTEGRATION FOR GATT, THE
URUGUAY ROUND, AND OTHER INTERNATIONAL
COMMITMENTS

CHAPTER 13
EC INTEGRATION, THE GATT, AND THE URUGUAY ROUND

CONTENTS

	<i>Page</i>
Developments covered in the previous reports	13-3
Background and anticipated changes	13-3
Possible effects	13-3
GATT implications	13-3
Uruguay Round implications	13-3
Developments during January-June 1990	13-4
GATT implications	13-4
Uruguay Round implications	13-4
Services	13-4
Trade-related intellectual property rights	13-4
Nontariff measures	13-5
Subsidies	13-6
Textiles	13-6
Agriculture	13-7
Subsidies	13-7
Quotas	13-7
Sanitary and phytosanitary standards	13-8

CHAPTER 13

EC INTEGRATION, THE GATT, AND THE URUGUAY ROUND

This chapter discusses the relationship between the Uruguay Round and the EC 92 initiative, particularly the extent to which it could affect attainment of U.S. trade policy goals. It also updates developments affecting existing GATT mechanisms that could be used to rectify problems associated with the internal market program. The information in this chapter has been culled from public reports and may not necessarily reflect the current negotiating positions of any particular party to the GATT.

Developments Covered in the Previous Reports

Background and Anticipated Changes

The restructuring of the EC internal market has led some to question whether all the changes envisioned will conform to the EC's international trade obligations under the GATT. Specific areas of concern include reciprocity, transparency, and the EC's transitional measures on autos and textiles. The GATT sets certain parameters for EC actions and contains a variety of mechanisms for dealing with 1992-related concerns.

The Punta del Este Declaration in September 1986, which set forth the goals of the Uruguay round, identified services, trade-related investment measures, and trade-related aspects of intellectual property rights as areas to be brought within GATT's scope. Efforts to reform the GATT involve some areas of overlap with the EC 1992 plan. It is unclear to what degree the initiatives will ultimately reinforce one another or will conflict. Several persons familiar with the present negotiations and also familiar with the 1992 program have suggested that the EC's negotiating positions on most issues in this round would have been the same or substantially the same with or without the 1985 White Paper and the 1992 program. The round is scheduled to end in December 1990.

Possible Effects

Previous USITC reports have suggested that the GATT represents a forum for addressing disputes on traded goods and the Uruguay Round, an opportunity, both to change 1992-related policies of concern to U.S. industry and to ensure that U.S. suppliers benefit more fully from 1992 initiatives.

GATT Implications

The trading partners of the European Community have already been affected by some elements of the EC 1992 program, and the incidence of disputes related to the program is likely to increase over the next few years. Three methods exist under the General Agreement on Tariffs and Trade (GATT) to address the issues arising from the EC 1992 process—streamlined GATT dispute-settlement procedures, the Trade Policy Review Mechanism (TPRM), and an examination of customs union. The principal and preferred means of resolving trade disputes is through GATT dispute-settlement procedures.¹ One of the first agreements reached in the Uruguay Round was to streamline the existing dispute-settlement procedures.

Another mechanism for reviewing the EC 1992 program was implemented in early May 1989. The Trade Policy Review Mechanism is a new GATT device to encourage greater compliance with GATT rules, to increase the transparency of trade policy actions taken by contracting parties, and to assist other countries in understanding such actions. The format for the late 1990 review of the EC trade regime has not been determined, but because of its broad scope, the review should provide the other contracting parties with information on the internal market process.

Uruguay Round Implications

As EC integration progresses, internal market policies may affect the EC's Uruguay Round positions. Furthermore, the timing of the two initiatives suggests that 1992-related directives may ultimately become the basis for the EC's implementing legislation for agreements reached in the course of the Uruguay Round. The 1992 initiative appears to have given the EC the ability to move forward in the Uruguay Round in areas like financial services and government procurement, where the United States has expressed an interest in expanded GATT rules. On the other hand, some concern has been expressed about the impact of the 1992 program on the Uruguay Round's success. In some areas at least, the EC is seeking credit for liberalization measures taken as part of the 1992 program or is pressing GATT trading partners to adopt policies crafted as part of its internal market exercise. Moreover, there is some concern that agreements reached internally as part of the 1992 exercise may limit the EC's negotiating flexibility, since they may represent tradeoffs among the member states that are not easily undone in a multilateral context. Absence of agreement internally in the EC, on the other hand, could slow

¹ The basic procedures are described in U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States*, (Investigation No. 332-267), USITC Publication 2204, July 1989, ch. 14.

progress in the Uruguay Round. How these competing influences will ultimately be sorted out is impossible to predict, given the pace of negotiating activity currently under way in order to bring the round to a conclusion by yearend 1990.

Three areas—services, intellectual property, and investment measures—are being considered by participants in the Uruguay Round for coverage under GATT and are also being addressed in the EC's 1992 program. In the services negotiations, the EC is requesting "credit" in evaluating EC concessions offered in the round and reciprocity from its trading partners for its recent banking liberalization. As to intellectual property, the patentability of biotechnologically derived plants, copyright protection for computer software, and the use of geographical indications in labeling wine are all issues being debated in both Brussels and Geneva. In addition, the EC has supported the prohibition of local-content requirements in the group on trade-related investment measures (TRIMs). However, recent developments in the EC, such as the Broadcast Directive, have given rise to concern among the EC's trading partners that the internal market process will result in trade-restrictive local-content requirements. Whether EC antidumping law or origin criteria will be changed, either during integration or after the Uruguay Round, is unclear.

A further correlation between EC 1992 activities and the EC's negotiating stance in the Uruguay Round may be found in the areas of subsidies, textiles, and agriculture. The EC Commission recently began a campaign to eliminate several national state-aid programs. However, it has pressed to retain the option of offering EC firms domestic subsidies in the subsidies negotiating group. In the textiles negotiating group, the EC has linked its willingness to agree on the phaseout of the Multifiber Arrangement (MFA) with the possible establishment of a textile safeguard or transitional measure. The debate on whether animal and plant health and human safety standards should be based on pure scientific evidence or on social and economic concerns continues in both Geneva and Brussels.

Developments During January-June 1990

GATT Implications

Discussions continued during 1990 on further ways to improve the GATT's dispute-settlement mechanism.² The participants are concentrating on four major themes: adoption of panel reports,

² See the previous report for discussion of new dispute settlement procedures, which became effective May 1, 1989. USITC, *The Effects of Greater Economic Integration Within the European Community on the United States: First Follow-Up Report*, USITC Publication 2268, March 1990, ch. 15.

including possible appeals procedures; implementation of adopted decisions and recommendations; compensation and retaliation; and strengthening commitments to comply with the GATT dispute-settlement rules and procedures and to refrain from taking unilateral measures.

Uruguay Round Implications

Services

The United States and the EC have proposed different methods for handling trade in services in the Uruguay Round. One sector on which the EC and the United States disagree is banking. The United States supports a special or separate agreement, whereas the EC advocates a complete liberalization of the financial industry modeled after its own 1992 banking directive.³ Some U.S. experts have expressed the view that a GATT agreement fashioned after the EC's banking directive could necessitate the removal of restrictions imposed on the U.S. industry by the McFadden Act and the Glass-Steagall Act.⁴ The United States has argued that sectoral reservations or sector-specific annotations in banking are necessary, given the key role of financial-services regulation in carrying out monetary and fiscal policies.⁵ In March 1990, after extensive consultations with the EC, the United States tabled an informal paper. However, sector coverage remained under dispute.⁶

Trade-Related Intellectual Property Rights

The United States seeks strong standards for protection of intellectual property rights through multilateral agreement.⁷ Of relevance to the 1992

³ See *International Trade Reporter*, Oct. 25, 1989, p. 1368 for a discussion of the U.S. position. See Sir Leon Brittan, Vice President of the EC Commission, "Developments in Banking Supervision on the Last Ten Decades and New Challenges," Address at the Conference at the 10th Anniversary of the EC Banking Advisory Committee, Brussels, Nov. 27, 1989.

⁴ Gary Clyde Hufbauer, ed., *Europe 1992 An American Perspective*, (Washington: The Brookings Institute, 1990), pp. 94-97. The study analyzed the implications of the EC's Second Banking Directive for the U.S. financial industry. For the short term, the study concluded that the multinational U.S. financial sector would gain considerably more wholesale business since the U.S. sector is characterized as experienced, aggressive, and objective. On the other hand, the long-term outlook would be for a major restructuring of the U.S. banking industry. One consequence of EC 1992 may be the elimination of present barriers to financial services. A bank with a single license, including an EC subsidiary of a U.S. bank, will be able to undertake banking and securities activities throughout the EC either through branching or through the cross border provision of services. See ch. 5 of this report, entitled "Financial Sector," for a discussion. For a detailed discussion of the EC's Second Banking Directive, see USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, ch. 5, and *Effects of EC Integration*, USITC Publication 2268, March 1990, ch. 5.

⁵ Keith Rockwell, "Treasury To Brief Bankers, but Row May Hinder Talks," *Journal of Commerce*, Jan. 19, 1989.

⁶ The United States and the EC submitted a joint proposal on services in March. See *International Trade Reporter*, Apr. 4, 1990, pp. 476-477.

⁷ See, for example, Congress, House, Committee on Energy and Commerce, Subcommittee on Oversight and Investigations, United States Trade Representative Carla A. Hills, statement, Sept. 24, 1990, p. 16.

program is that the United States is seeking to strengthen protection for biotechnology patents and computer software during the course of the Uruguay Round.⁸

The EC presented a new proposal in the trade-related intellectual property rights (TRIPs) negotiating group on April 2, 1990. The United States generally supported the plan but was concerned about the lack of patent protection for biotechnologically derived plants.⁹ The EC's submission excludes "plant or animal varieties or essentially biological processes for the production of plants and animals" from patent protection.¹⁰ This exclusion apparently reflected policy being framed as part of the 1992 program.¹¹

The U.S. tabled its own TRIPs proposal in May 1990.¹² The U.S. plan states that "patents shall be granted for all products and processes, which are new, useful, and unobvious."¹³ The U.S. proposal does not specifically exclude any items from patentability, as long as they meet the criteria.

In the case of computer software, the EC's recent TRIPs proposal offers copyright protection to computer programs "as literary works."¹⁴ In comparison, the U.S. submission is more comprehensive and includes "applications programs and operating systems expressed in any language, whether in source or object codes which shall be protected as literary works."¹⁵

A draft EC directive that attempted to introduce common Community rules for copyright protection for computer software programs was initially put forward in April 1989.¹⁶ By May 1990, a consensus among member states had still not emerged.¹⁷ One major issue concerns whether or not to allow reverse engineering.¹⁸ Some companies in the

⁸ Ibid.

⁹ Congress, House, Judiciary Committee, Subcommittee on Courts, Intellectual Property, and Administration of Justice, United States Trade Representative Carla Hills, statement, July 25, 1989, as reprinted in *Department of State Bulletin*, November 1989.

¹⁰ WIPO, vol. 4, No. 5 (May 1990), p. 111.

¹¹ An internal market proposal for biotechnology patent protection first emerged in the EC in October 1988 ((88)496), reprinted in the Jan. 13, 1989, *Official Journal*. The proposed directive excluded the patenting of plant and animal varieties and precludes the possibility of plant and plant materials "produced by nonpatentable use of a previously known biotechnological process." U.S. Department of Commerce, *EC 1992: A Commerce Department Analysis of European Community Directives*, vol. 3, March 1990, p. 99. The directive has been discussed extensively. No consensus has been reached on how to deal with biotechnology developments.

¹² The United States Trade Representative released a copy of the U.S. proposal to the public on May 31, 1990.

¹³ "Useful and unobvious" mean "capable of industrial application" and "inventive step," respectively. U.S. proposal, p. 9.

¹⁴ WIPO, vol. 4, No. 5 (May 1990), p. 108.

¹⁵ U.S. proposal, p. 3.

¹⁶ For a detailed description of the directive, see USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 12-2 to 12-4.

¹⁷ *Eurobrief*, vol. 2, No. 12 (Feb. 23, 1990), p. 140.

¹⁸ Ibid. Reverse engineering is the breakdown (decompilation) of the machine code of the program into

EC oppose the directive because it "could seriously hinder innovation and create problems for competition in Europe."¹⁹ Other European companies and some U.S. firms support the directive.²⁰

Nontariff Measures

U.S. efforts in the nontariff measures group have been focused on rules of origin, among other things.²¹ Origin rules are not directly specified or changed in any EC integration measures but have been cited by many non-European interests as being of great concern.²² Some U.S. Government officials have expressed concern about the EC's origin rules,²³ particularly since the EC will use such rules to determine the type of activities that are European and are thus not subject to 1992-related procurement discrimination and residual quantitative restrictions. Moreover, recent EC regulations and rulings have created uncertainty as to the EC standard for conferring origin, notably the 1989 decision applied to Ricoh, the Japanese photocopier maker alleged to have circumvented EC antidumping duties by exporting from its California plant to Europe.²⁴

During the first half of 1990, the Uruguay Round negotiating group began working on a draft text. To reduce the possibility for trade distortion by rules of origin, participants are calling for rules that are nondiscriminatory, predictable, and transparent.²⁵ Under discussion during the period were the treatment of preferential rules, notification requirements, establishment of a permanent Rules of Origin Committee in the GATT, the role of the Customs Cooperation Council, and positive versus negative origin determinations.²⁶

¹⁹ -Continued

readable code. A computer expert can then analyze how the code works and reproduce the program without actually copying the code, which would constitute copyright infringement of the original program.

²⁰ Ibid.

²¹ Ibid.

²² Congress, House, Committee on Energy and Commerce, Subcommittee on Oversight and Investigations, United States Trade Representative Carla A. Hills, statement, Sept. 24, 1990, p. 5.

²³ See, for example, United States Council for International Business, *The European Single Market*, pp. 35-38, and U.S. Chamber of Commerce, *EC 1992: A Progress Report*, March 1990.

²⁴ Peter Allgeier, Assistant USTR for Europe and the Mediterranean, stated, "While not formally a part of the White Paper or single market program, EC technical restrictions such as rules of origin or quantitative restrictions obviously become more important as the European market becomes more lucrative and united." Congress, House, Foreign Affairs Committee, Subcommittee on International Economic Policy and Trade and Subcommittee on Europe and the Middle East, Peter Allgeier, statement, Feb. 20, 1990.

²⁵ See USITC, *Effects of EC Integration*, March 1990, pp. 14-3 to 14-9 for a discussion of U.S. concerns regarding EC-origin rules and local-content criteria.

²⁶ GATT, *News of the Uruguay Round of Multilateral Trade Negotiations*, NUR 031, Oct. 16, 1989.

²⁷ *News of the Uruguay Round*, NUR 34, Feb. 23, 1990 and NUR 35, Apr. 19, 1990.

Subsidies

The subsidies negotiating group is examining subsidies-related provisions (arts. VI and XVI) of the General Agreement as well as the Multilateral Trade Negotiation (MTN) code on subsidies and countervailing measures. The United States advanced two proposals for prohibiting and disciplining subsidies in February and March 1990; an EC proposal was tabled in 1989.²⁷ A major issue concerns identifying the types of subsidies that should be prohibited. Recently, proposals in this negotiating group have been structured according to a so-called "traffic light" framework, under which subsidy practices are classified either as prohibited ("red light"), actionable ("yellow light"), or permissible ("green light").²⁸ The United States has proposed expanding the list of subsidies that are prohibited ("red light") to include measures that directly encourage exports and trade distorting domestic subsidies, and has opposed the establishment of significant loopholes in discipline through placement of trade distortive practices in the "green light" category.²⁹ Under the EC proposal, no domestic subsidies would be prohibited; instead, the EC proposal focuses on the definition of subsidy, which could limit the types of practices that would be subject to countervailing duties.³⁰ The EC has taken the position that its regional and structural adjustment subsidies are necessary, especially in light of the EC 92 process, and that such domestic subsidies are "legitimate instruments of social and economic policy" that should remain "non-prohibited but countervailable"³¹ if they have an identifiable effect on international trade.³² In the EC's view, government interventions having no identifiable effects on international trade should not be actionable.³³

²⁷ The EC presented its proposal in late November 1989. See *News of the Uruguay Round*, NUR 033, Jan. 11, 1990 and NUR 035, Apr. 19, 1990.

²⁸ See, for example, Congress, Senate, Committee on Governmental Affairs, Subcommittee on Oversight of Governmental Management, Deputy Assistant Secretary of Commerce for Import Administration Marjorie A. Chorlins, statement, Sept. 26, 1990, p. 6.

²⁹ *Ibid.* See also the written statement of U.S. Trade Representative Carla Hills issued in connection with appearance Sept. 24, 1990, before the House Energy and Commerce Committee, Subcommittee on Oversight and Investigations, pp. 8-9:

In the subsidies negotiation, our objective has been to extend the existing prohibition against export subsidies to trade-distorting domestic subsidies. In May, the Chairman of the Subsidies Negotiating Group circulated a draft text, which introduced a few useful concepts. However, it does little to increase discipline on domestic subsidies, while providing for a category of permitted subsidy practices.

For a discussion of the U.S. position on export subsidies see *News of the Uruguay Round*, NUR 035, Apr. 19, 1990, p. 8; and *International Trade Reporter*, Apr. 4, 1990, p. 477.

³⁰ U.S. Dept. of Commerce, *Uruguay Round Update*, February 1990, p. 8.

³¹ A copy of the EC proposal is reprinted in *Inside U.S. Trade*, Dec. 1, 1989.

³² *News of the Uruguay Round*, NUR 033, Jan. 11, 1990, p. 11.

³³ *Ibid.*

Despite the differences evidenced thus far in the Uruguay Round, it is possible that the 1992 program may ultimately move the EC in the direction of exerting greater discipline over the domestic subsidies provided by member states. The EC Commission fears that member states will be tempted to resort to state aids to counter increased competition resulting from the removal of barriers under the single-market program.³⁴ The EC Commission is currently examining member-state aid programs and has proposed stricter criteria for the granting of state aids.³⁵

Textiles

A major objective of the Uruguay Round is to formulate a modality by which to integrate textile trade into the GATT after the current Multifiber Arrangement protocol expires on July 31, 1991.³⁶ The choice of a single modality is "the major outstanding issue impeding progress" in the textiles and clothing negotiations, GATT Director General Arthur Dunkel reported in July.³⁷ The modality proposed by the United States is a new system of global quotas that would be gradually liberalized over a 10-year transition period, after which textile trade would return to GATT rules.³⁸ In mid-May 1990, the EC proposed transition quotas that would be eliminated step by step over an undetermined transition period, to be negotiated by the participants. The EC also called for strengthened GATT safeguard rules that would enable importing countries to impose curbs on textile imports that disrupt or threaten domestic markets.³⁹

Because national quotas will be unenforceable in the single, integrated EC market, the EC has indicated it intends to eliminate or replace all member-state quantitative restrictions on imports of

³⁴ "State Aid in the EEC: Battle of Britain," *The Economist*, June 10, 1990, p. 65.

³⁵ For more information on EC state aids, see EC Commission, *First Survey of State Aids in the European Community*, May 1989.

³⁶ The Punta Del Este Declaration, pt. I(D) states that "Negotiations in the area of textiles and clothing shall aim to formulate modalities that would permit the eventual integration of this sector into GATT on the basis of strengthened GATT rules and disciplines." At the Montreal midterm review, GATT Ministers stated that one of the objectives of the negotiating group on textiles was "a phasing out of restrictions under the Multi-fibre Arrangement." *News of the Uruguay Round*, NUR 027, Apr. 24, 1989. The General Agreement prohibits the use of quantitative restrictions, whereas the MFA, implemented under GATT auspices in 1974, is built on a system of bilateral agreements between importing and exporting countries to limit international trade in textiles and apparel. It also permits importing countries to impose unilateral restraints (also prohibited by the GATT) on specific products for up to 2 years in the absence of an agreement to control textile trade and thus prevent market disruption.

³⁷ *News of the Uruguay Round*, NUR 039, July 30, 1990, p. 4. Mr. Dunkel continued, "I have noted the very wide support in the TNC [Trade Negotiations Committee] for a modality based upon the MFA."

³⁸ Peter Steele, "The MFA and Beyond: The EC Perspective," *EIU Textile Outlook International*, May 1990, p. 64.

³⁹ *News of the Uruguay Round*, NUR 036, June 1, 1990.

textiles, including those imposed under the MFA, by 1992.⁴⁰ Of concern to the United States is whether the EC will construct EC-wide safeguards or transitional measures to protect the domestic industry during the transition to a more open market.⁴¹ EC Industry Ministers have requested the EC Commission to study the impact of EC 92 and the Uruguay Round on the EC textiles industry.⁴²

Agriculture

The EC Commission and EC member states maintain that the 1992 initiative does not encompass a substantial revision of the Common Agriculture Policy (CAP).⁴³ Nevertheless, the agricultural sector will likely be affected by the 1992 program in four respects: (1) the harmonization of taxes on food and agricultural products and inputs; (2) the elimination of agricultural border taxes and subsidies; (3) the elimination of national quotas and other assistance programs that are incompatible with the 1992 program; and (4) the harmonization of plant and animal health standards, food labeling, and ingredients and packaging laws. Since the beginning of the Uruguay Round, deliberations in the negotiating group on agriculture have focused on four areas: (1) internal support (subsidies), (2) market access (quotas), (3) export subsidies, and (4) harmonization of plant and animal standards. Below is a discussion of those three issues in agriculture that are being addressed in the context of both the EC integration process and the Uruguay Round.

Subsidies

Both the subsidies and agriculture negotiating groups are addressing subsidies, although the EC has maintained that agricultural subsidies should only be considered in the agriculture group. The major debate in both groups is how to discipline the use of export and domestic subsidies. The EC does not support the total elimination of subsidies on agricultural products, be they domestic or export.⁴⁴ Moreover, the EC has only advocated a reduction in subsidies through the lowering of an Aggregate

⁴⁰ EC Commission, "Europe - World Partner, Questions and Answers," Oct. 19, 1988. For a more indepth treatment of the EC's policies towards member-state residual quantitative restrictions in light of the Internal Market program, see USITC, *Effects of EC Integration*, USITC Publication 2204, July 1989, pp. 11-6 and 11-13 to 11-5.

⁴¹ U.S. Government Task Force on the EC Internal Market, "EC 1992: An Assessment of Economic Policy Issues Raised by the European Community's Single Market Program," May 1990, pp. 15-16. See also *News of the Uruguay Round*, NUR 031, Oct. 16, 1989.

⁴² The report was due out in January 1990 but has been delayed.

⁴³ See, for example, U.S. Department of State Telegram, "ITC Commissioner Lodwick's Visit: Italian Agriculture Prepares for 1992," September 1989, Rome, Message Reference No. 19364; and *European Report*, No. 1552 (Jan. 6, 1990), External Relations, p. 4.

⁴⁴ *News of the Uruguay Round*, NUR 031, Oct. 16, 1989, p. 8.

Measure of Support.⁴⁵ The United States supports a total elimination of export subsidies in 5 years and domestic subsidies that distort trade in 10 years.⁴⁶

Several types of subsidies granted to the EC's agricultural sector are being discussed in the context of the EC 92 process. For example, national aids form a significant percentage of overall aid to agriculture.⁴⁷ The use of state aids to agriculture, as well as to other sectors, is likely to be influenced by the EC Commission's desire to prevent an increased reliance on state aids in response to the elimination of barriers under the single-market program.⁴⁸

In addition, the EC Commission is planning to dismantle by the end of 1992 the Community's system of exchange rates for agricultural commodities, known as Monetary Compensatory Amounts (MCAs). MCAs act as border taxes and subsidies between the member states and therefore would be difficult or impossible to collect after 1992, when frontier controls are to be eliminated. Currently, member states can exercise some control over national farm prices and farm incomes through manipulation of the MCAs.⁴⁹

Quotas

Like MCAs, certain agricultural quotas in the EC are nationally based and will be unenforceable under the single market. Some quotas determine the level of aid granted to a particular agricultural sector in a member state (such as national production quotas for sugar and milk), and others are nationally allocated import quotas.⁵⁰

The EC has agreed in principle to the U.S. concept of tariffication of nontariff barriers, including quotas.⁵¹ However, the EC states in its proposal that quantitative restrictions may be maintained in exceptional circumstances.⁵² Another provision of the EC plan that differs from the U.S. scheme for farm reform is rebalancing, whereby market access would be improved for some products whereas border protection would be increased for others.⁵³

⁴⁵ See, for example, *European Community News*, No. 47/89, Dec. 19, 1989, p. 6; *News of the Uruguay Round*, No. 030, Aug. 3, 1989, p. 7.

⁴⁶ See, for example, p. 6 and 11 of the *Submission of the United States on Comprehensive Long-Term Agricultural Reform*, as announced by U.S. Secretary of Agriculture Clayton Yeutter in an Oct. 24, 1989, statement, (press release no. 1390-89). See, also, *News of the Uruguay Round*, Nov. 21, 1989, p. 6.

⁴⁷ For a full explanation, see David Kelch and Walter Gardiner, "Europe 1992: Implications for Food and Agriculture," *National Food Review*, October-December 1989, p. 15.

⁴⁸ Bureau of National Affairs, "State Aids: The Last Frontier?" 1992: *The External Impact of European Integration*, Aug. 10, 1990, pp. 9-12.

⁴⁹ For a full explanation, see David Kelch and Walter Gardiner, "Europe 1992: Implications for Food and Agriculture," *National Food Review*, October-December 1989, pp. 14-15.

⁵⁰ For more information on quotas, see ch. 11 of this report.

⁵¹ See, *GATT Focus*, No. 68, February 1990, p. 6. The United States proposed the idea of converting all nontariff barriers into tariffs then gradually reducing the new tariffs over time.

⁵² *European Community News*, No. 47/89, Dec. 19, 1989, p. 6.

⁵³ *Ibid.*

Under the U.S. plan, nontariff barriers would be converted to tariffs, then reduced. As part of the U.S. plan for tariffication, the United States recently estimated the amount the proposed ad valorem tariff should be for various agricultural products.⁵⁴ As for the EC plan, the United States is concerned that the rebalancing concept in the EC proposal is not only inconsistent with the Montreal Mid-Term Agreement, but is also inconsistent with the overall goal of the Uruguay Round.⁵⁵

Sanitary and Phytosanitary Standards

In the United States and the EC, product approvals and mandatory standards for plant, animal, and human health reasons are normally based on three main criteria—safety, efficacy, and quality. The EC Parliament, under the EC 1992 program, is considering a fourth criterion to recognize social and economic concerns before products are approved or licensed. Some member states have suggested using the fourth criterion for bioengineered products such as growth enhancements.⁵⁶ The United States is concerned about the possible ban on growth enhancements since it would put the United States at a disadvantage in the EC market and could discourage biotechnological research in this

⁵⁴ The proposed ad valorem tariff is calculated by subtracting the internal price from the world price and dividing it by the world price. For example, the ad valorem tariff equivalent for butter in 1988 in the EC was 166 percent, whereas in the United States it was 95.9 percent. The tariff equivalent on sugar was 170 percent in the EC whereas in the United States it was 120.0 percent. USITC, *Estimated Tariff Equivalents of U.S. Quotas on Agricultural Imports and Analysis of Competitive*

Conditions in U.S. and Foreign Markets for Sugar, Meat, Peanuts, Cotton, and Dairy Products, USITC Publication 2280, April 1990.

⁵⁵ *International Trade Reporter*, Dec. 20, 1989, p. 1658.

⁵⁶ U.S. Government Task Force on the EC Internal Market, *EC 1992: An Assessment of the Economic Policy Issues Raised by the European Community's Single Market Program*, May 1990.

area.⁵⁷ During 1990, the United States actively monitored the EC commitment to the April 1989 Uruguay Round mid-term review agreement on agriculture concerning the importance of scientific evidence to the standards-setting program.⁵⁸

In the Montreal midterm review, the participants of the Uruguay Round agreed to negotiate disciplines that would require that sanitary and phytosanitary standards (S&P), which relate to trade, be based on sound scientific evidence. Within the agricultural negotiating group, a working group has been established to examine the issues of animal, plant, and health standards. A draft text has been prepared that encompasses common language from the various proposals.⁵⁹ Broad agreement has been reached on three main principles: sound scientific evidence, equivalency, and dispute settlement.⁶⁰

Under the draft text, GATT article XX(b) would be strengthened by requiring that all sanitary and phytosanitary standards be based on sound scientific evidence. Equivalency means that, once a level of health protection is mandated, a country can meet these levels through equivalent standards that need not be identical to another country's standards. Finally, the draft agreement proposes dispute-settlement procedures that would allow international health organizations to determine which standards are based on sound scientific evidence during a dispute.

⁵⁷ See, for example, U.S. Government Task Force on the EC Internal Market, "Harmonization of Health and Safety Measures," *EC 1992: An Assessment of Economic Policy Issues Raised by the European Community's Single Market Program*, May 1990, p. 21.

⁵⁸ See ch. 6, sections on public health and safety policy and agriculture for a discussion of U.S. concerns about the EC's use of a the "fourth criterion."

⁵⁹ *News of the Uruguay Round*, NUR 036, June 1, 1990.

⁶⁰ See, for example MTN.TNC/9, Apr. 11, 1989, p. 7, setting forth the results of the midterm review in the area of sanitary and phytosanitary regulations.

CHAPTER 14
EC INTEGRATION AND OTHER EC COMMITMENTS

CONTENTS

Background	<i>Page</i> 14-3
Developments since the first followup report	14-3

CHAPTER 14

EC INTEGRATION AND OTHER EC COMMITMENTS

Background

In the initial report and first followup report, the chapter on EC integration and other EC commitments considered agreements other than the GATT that might impose on member states obligations that conflict with aspects of the 1992 program. The first followup report considered three specific areas in which possible conflicts might arise: (1) international human rights treaties and the Broadcast Directive, (2) the codes of the Organization for Economic Cooperation and Development (OECD Codes) and reciprocity, and (3) bilateral memoranda of understanding (MOUs) and the EC global approach to certification and testing.

The first followup report began its analysis by discussing generally the web of bilateral and multilateral agreements to which the United States and EC member states are signatories. It then briefly discussed the allocation of responsibilities for external relations between the European Community and the nonmember states set forth by the Treaty of Rome and relevant Treaty provisions and principles of customary international law relating to conflicts between treaties. It then turned to a discussion of the possible conflicts noted above.

During the period covered by the previous report, the U.S. Government raised the possibility that the EC's "Television without Frontiers" Directive might conflict with principles embodied in several international agreements designed to safeguard the free flow of information. The issue of such a possible conflict was raised by a local-content restriction in the directive that stated that when practicable, broadcasters should reserve a majority of broadcasting time for programming with EC content. Such a provision, it was believed, presented a potential conflict with both the specific provisions and the spirit of certain international human rights treaties. These treaties included the Universal Declaration of Human Rights, as well as the Helsinki Final Act and related documents of the Conference on Security and Cooperation in Europe (CSCE) designed to prevent signatories from placing restrictions on freedom of speech.

The previous report also discussed the reciprocity provision of the EC's Second Banking Directive. It pointed out that despite an earlier amendment designed to alleviate similar concerns, the reciprocity provision might be inconsistent with principles embodied in the OECD's Capital Movements Code. The OECD Capital Movements Code sets forth the goal of dismantling barriers to capital movements among its contracting parties, which include the United States and all 12 member states of the EC. To help achieve this goal, the code

requires that its signatories adhere to the twin principles of nondiscrimination and standstill/rollback of restrictive practices. To the extent that the revised Second Banking Directive embodied the concept that the EC will restrict foreign-owned banks to the same scope of operations to which EC banks operating in the foreign country are limited, rather than granting national treatment, it appeared to contravene the principle of nondiscrimination embodied in the code. By mandating that EC member states that currently do not have reciprocity requirements in their financial sectors adopt them, the directive further appeared to run afoul of the principles of standstill and rollback of restrictive measures by code signatories.

The final possible conflict discussed in the previous report was related to the EC's program for harmonizing standards and its related regime for certification and testing of goods to ensure that the goods comply with the harmonized standards. Specifically the report discussed the relationship between the EC's "Global Approach to Certification and Testing" and certain bilateral agreements in the form of MOUs between the United States and EC member states. In 1989 both the EC Commission and Council indicated that the EC's proposed "Global Approach to Certification and Testing" would affect certain bilateral agreements between testing and certification bodies in the EC member states and corresponding entities in the United States. The EC had stated that any existing bilateral agreements between EC member-state testing and certification bodies and third-country bodies would have to be renegotiated as EC-wide bilateral agreements when EC directives covering those products were implemented. Because the EC's approach was not fully developed, its likely effect on existing as well as future agreements between the United States and EC member states was difficult to assess at that time.

Developments Since the First Followup Report

The EC's Second Banking Directive was passed on December 15, 1989. As the previous report mentioned, the compatibility of the directive with the OECD codes, and the possibility of amending the codes to reconcile the two, was expected to be a major topic of discussion at the March meeting of the OECD's Committee on Capital Movements and Invisible Transactions.¹ At that meeting, however, no action was taken to reconcile the two documents.² Sources from the U.S. Mission to the OECD have indicated that recent discussions on the Second Banking Directive have been influenced by discussions regarding another initiative known as the National Treatment Instrument.³ Lack of EC

¹ Interview with personnel from the U.S. Mission to the OECD, Paris, July 11, 1990.

² Ibid.

³ Ibid.

support for that instrument, which could suggest a lack of commitment to the principle of national treatment, has made U.S. officials reluctant to amend the OECD Codes until they are assured that the EC intends to apply a national treatment standard in applying the Second Banking Directive.⁴ The topic is expected to be on the committee's agenda when it meets again in September 1990.⁵

A second topic covered in the first followup report was the EC's "Global Approach to Certification and Testing." There have been few significant developments in this area since that time Certification, and these are discussed in chapter 4, Standards and Testing.

⁴ Ibid.

⁵ Ibid.

PART IV
OTHER POLICIES AND SPECIAL TOPICS

CHAPTER 15
THE SOCIAL DIMENSION

CONTENTS

	<i>Page</i>
Developments covered in the first followup report	15-3
Developments during 1990	15-4
Measures adopted	15-4
New initiatives under the social dimension action program	15-4
Atypical work	15-5
Organization of working time	15-5
Other measures under consideration	15-6
Proof of work contracts	15-6
Cross-border subcontracts	15-6
Worker information, participation, and consultation	15-7
Safety, hygiene, and health agency	15-7
Worker notification of takeover	15-8
The social dialog	15-8
Court of Justice decisions	15-9

CHAPTER 15

THE SOCIAL DIMENSION

The "social dimension" of EC 92 refers to the efforts to harmonize different EC member-state policies on labor markets, industrial relations systems, occupational safety and health regulations, social welfare, and social security systems. Although the White Paper did not call for legislative action in this area, as integration progressed, it was recognized that some harmonization of working conditions was necessary to avoid distortion in the labor market and prevent abuses of competition. Labor has expressed concern that workers' rights and benefits might be eroded as barriers are removed, and member states as well as business concerns likewise recognize a need for some sort of social dimension to balance economic integration and to provide the incentive for people to move and find new jobs. The concerns of U.S. firms in this area closely track those of EC firms.

Developments Covered in the First Followup Report

In 1985, the EC Commission initiated an ongoing social dialog (the "Val Duchesse dialogue") between management and labor. Article 118b of the European Economic Community Treaty (EEC Treaty), as amended by the Single European Act (SEA), endorsed a continuation of dialog on a Community level between management and labor. These meetings continue, with management represented by the employer's European-level organization, the Union of Industrial and Employers' Confederations of Europe (UNICE) and the European Center of Public Enterprises (CEEP), and labor by the European Trade Unions Confederation (ETUC). To date, these discussions have produced nonbinding "joint options."

The 1985 White Paper did not call for the EC Commission to propose any directives addressing the labor aspects of the internal market. Under the SEA, a unanimous vote is required to approve directives addressing the free movement of persons and employee rights and interests, whereas directives in most other areas can be approved by qualified majority. In contrast, the act placed special emphasis on worker safety and health. New article 118a of the EEC Treaty directs the EC Commission to propose, and the EC Council of Ministers (Council) to adopt, directives to help achieve improvements in the working environment as regards worker safety and health. Unlike the unanimous vote needed for adoption of measures regarding other employee rights and benefits, article 118a directives can be adopted by a qualified majority. Finally, worker safety and health, along with environmental protection, is singled out, under articles 100a(4) and

118a(3), as one of the few areas in which a member state can apply its own stricter provisions.

In 1989, the EC Commission focused its efforts in the social dimension area on drafting a Charter of Fundamental Social Rights (the Social Charter). Written in the form of a "solemn proclamation" rather than a binding legal document, the Social Charter lays down general tenets for 12 basic workers' rights, including freedom of movement; employment and remuneration; improvement of living and working conditions; social security; freedom of association and collective bargaining; vocational training; equal treatment and opportunities for men and women; worker information, consultation, and participation; worker health and safety protection; a minimum employment age of 15; rights for elderly persons; and rights for disabled persons. Eleven member states—all except the United Kingdom—approved the Social Charter.

With the Council's adoption of the Social Charter, the EC Commission presented an action program for implementation of the charter. The action program proposed 47 new initiatives in the social dimension area.

In its work program for 1990, the EC Commission promised to take steps to implement the most urgent aspects of the action program, namely the reorganization of working time; atypical work; and consultation, information, and participation procedures for workers. The EC Commission also stated its intention to continue efforts regarding education, vocational training, and worker safety and health. The work program sets out 17 specific proposals to implement the Social Charter with regard to job transparency and creation, worker safety and health, equal treatment, and improvement of living and working conditions.

One of the most controversial topics in the social dimension area, and the labor topic historically of most concern to U.S. firms doing business in the EC, is the degree to which workers participate in corporate decisionmaking. Under the Vredeling proposal, first presented in 1983, companies with more than 250 employees would be required to consult with a worker body before making decisions likely to substantially affect the interests of the workers. One of the most troublesome aspects of the Vredeling proposal for U.S. companies was its extraterritorial effect, in that the proposed directive would have required even multinational corporations headquartered *outside* the EC to consult with worker representatives before making a decision that affected any of its European facilities. Although the proposal itself is not actively under consideration, the subject matter of the proposal is still alive. Industry groups continue to express concern that Vredeling will be resurrected.

In the worker safety and health area,¹ the EC Council adopted in 1989 a Framework directive (89/391) and three specific directives falling thereunder. The three specific directives addressed minimum worker safety and health conditions, work equipment, and personal protective equipment. The Social Affairs Council reached a common position on two other individual directives covered under the Framework directive—visual display units (VDUs) and the handling of heavy loads.

Developments During 1990

Measures Adopted

The EC Council has now adopted the fourth, fifth, and sixth individual directives within the Framework directive for worker safety and health. Directive 90/269 addresses the manual handling of loads that pose a risk of back injury to workers (fourth individual directive).² Directive 90/270 addresses requirements for work with VDUs (fifth individual directive).³ Directive 90/394 addresses worker protection from risks related to exposure to carcinogens (sixth individual directive).⁴ All three directives require appropriate worker training and information, as well as consultation and participation by workers or their representatives.

Given the common use of VDUs, the directive on this subject is likely to require action by most businesses operating in the EC. The VDU directive sets out specific design and ergonomic requirements for display screens, keyboards, work desks, and work chairs. It also requires employers to provide, at no cost to the workers, routine ophthalmological examinations. Implementation is required by 1993 for new workstations, and by 1997 for existing workstations. This directive is seen by some as overreaching and problematic, particularly insofar as it mandates eye examinations. The main complaint is that the directive presupposes a risk from VDUs without any scientific evidence of such risk.⁵

The heavy loads directive requires employers to make efforts to use mechanical equipment rather than manual labor for handling such loads. If manual handling is necessary, the employer must assess the risks of back injury and take measures to

reduce the risks. Although industry representatives do not view this directive as posing a substantial problem for most employers, they do note that, without regard to cost and practical concerns, any load *can* somehow be lifted by mechanical means.⁶

The carcinogens directive provides general guidance for worker protection from 31 agents and 8 industrial processes.⁷ It requires employers to assess the risk of worker exposure to a carcinogen by determining the nature, degree, and duration of the workers' exposure. Employers are asked to "take account of the desirability" of not employing workers in the area where they will come into contact with carcinogens.⁸ When possible, carcinogens should be used in a closed system or replaced by a less dangerous substance. If these options are not technically possible, worker exposure should be reduced to as low a level as is technically possible, through engineering controls, work practices, and protective equipment. The directive includes recordkeeping requirements as well as provisions for appropriate worker training, information, consultation and participation, and health surveillance. Finally, the Council obliges itself to adopt directives setting limit values for the covered carcinogens. The EC directive is not inconsistent with the cancer policy regulation issued by the U.S. Occupational Safety and Health Administration,⁹ and does not appear to impose additional requirements on firms that are already in compliance with U.S. standards.

New Initiatives Under the Social Dimension Action Program

In early 1990, the EC Commission announced its intent to present 17 of the 47 initiatives in the social dimension action program to the Council by the end of this year.¹⁰ Although the European Parliament adopted a measure asking the EC Commission to come up with proposals on all 47 measures by the end of 1990,¹¹ Social Affairs Commissioner Papandreou has stated that the 30 remaining action program measures will be addressed next year.¹² The European Parliament, European unions, and the EC Commission's Economic and Social Committee are anxious for decisions on the social measures linked to the completion of the internal market before January 1993.¹³ The EC recently has adopted several of the action program measures and is in the processing of drafting a number of others.

¹ Discussed in ch. 7 of the Initial Report and the First Followup Report.

² *Official Journal of the European Communities*, (OJ) No. L 156 (June 21, 1990), p. 9. There is a separate proposal under consideration addressing the manual handling of loads involving a risk of musculoskeletal injury. *Reexamined Proposal for a Council Directive on the Minimum Health and Safety Requirements for the Manual Handling of Loads Involving a Risk of Musculoskeletal Injury to Workers*, Com 90 (131), OJ No. C 118 (June 12, 1990), p. 14.

³ OJ No. L 156 (June 21, 1990), p. 14.

⁴ OJ No. L 196 (July 26, 1990), p. 1.

⁵ USITC staff meeting with attorneys of U.S. law firm, Brussels, June 6, 1990; Comments of UNICE officials, Brussels, June 7, 1990 (UNICE comments).

⁶ UNICE comments; EC Committee of the American Chamber of Commerce, *Business Guide to EC Initiatives* (Brussels, Spring 1990), p. 20.

⁷ EC Committee of the American Chamber of Commerce in Belgium, *Countdown 1992* (Brussels, July 1990), p. 42.

⁸ Council Directive 90/394, art. 3.

⁹ 29 C.F.R. 1990 (promulgated 1981).

¹⁰ EC Commission, *Programme of the Commission for 1990*, Jan. 10, 1990 (*Work Program*), p. 19.

¹¹ *European Report*, No. 1564, Internal Market (Feb. 16, 1990), p. 14.

¹² USITC staff meeting with ETUC official, Brussels, June 5, 1990 (ETUC meeting); USITC staff meeting with staff of EC Commissioner, Brussels, June 6, 1990 (EC Commission meeting).

¹³ *Europe*, No. 5198 (Feb. 21, 1990), p. 13.

Atypical Work

On June 26, 1990, the EC Commission presented a package of three proposed directives addressing atypical work.¹⁴ There are three main types of "atypical" or "precarious" work, each of which is addressed by at least two of these directives: fixed duration work, open-ended temporary work, and part-time work.¹⁵ In proposing these directives, the EC Commission emphasized the usefulness of flexible work, viewing this type of work as essential for firms and as meeting the needs of many workers.¹⁶

The necessity of proposing three separate directives arose because of the combined social and economic dimensions of atypical work.¹⁷ Each of the three proposed directives is based on a different article of the EEC Treaty. The directive addressing working conditions (Com 90/228) relies on article 100, which requires unanimous Council approval for measures affecting the functioning of the common market. This directive is intended to avoid abuses and to provide for general improvement of working conditions, such as access to training.¹⁸ The directive is applicable to all three types of atypical work but does not apply to workers whose average weekly working time is less than 8 hours.

The second proposed directive is aimed at preventing distortion of competition and improving the functioning of the internal market.¹⁹ This directive is based on article 100a, which requires a qualified majority approval by the Council of measures for the establishment of functioning of the internal market. The proposal seeks to harmonize costs such as social security, seniority allowances, dismissal allowances, and holiday pay. Currently, there are large differences among the member states regarding the employers' obligations to pay these types of benefits to part-time or temporary workers. For example, some member states currently require social security for part-time workers, whereas others do not.²⁰ The directive covers all three types of atypical work but applies only to workers who average more than 8 hours of working time per week.

The third proposed directive addresses worker safety and health for fixed duration and

open-ended temporary workers. It does not cover part-time workers, because those workers are already covered under the general Framework worker safety and health directive (Com 89/391).²¹ However, the Framework directive does not clearly cover temporary workers because their employer is the employment agency. The newly proposed directive covers these workers, with a particular emphasis on safety training. The directive covers as well other temporary workers, although its major concern is those hired by employment agencies.²² The EC Commission considers this a worker safety and health directive under article 118a of the EEC Treaty. That article provides for input from the European Parliament and for qualified majority approval of the directive by the Council. UNICE (the European employers' association) sees this directive as problematic, because it may be impractical to provide safety training and medical surveillance for workers employed by employment agencies.²³ UNICE believes this type of employment would be better addressed under the subcontracts directive.²⁴

The EC Commission's legislation on atypical work represents a novel approach toward legislating in the social dimension area. The EC Commission has found a unique means of addressing a controversial subject that touches many provisions of the EEC Treaty. However, a representative of the EC Commission has indicated that it presently has no orientation to use the same type of breakdown for other controversial directives.²⁵

These directives are likely to require new legislation in some member states, such as the United Kingdom, where part-time and temporary workers do not have social security and other benefits equivalent to those of full time permanent workers.²⁶ In other member states, however, these directives are unlikely to result in many changes. For example, France already has very precise legislation on atypical work.²⁷

Organization of Working Time

On July 25, 1990, the EC Commission presented a proposed directive on the organization of working time.²⁸ The proposal sets requirements for night and shift work and establishes minimum daily and weekly rest periods. The directive leaves open to member states the choice of meeting the standards through legislation or by assuring that

¹⁴ Proposal for a Council Directive on the Approximation of the Laws of the Member States Relating to Certain Employment Relationships with Regard to Working Conditions, Com (90) 228; Proposal for a Council Directive on the Approximation of the Laws of the Member States Relating to Certain Employment Relationships With Regard to Distortions of Competition, Syn 280; Proposal for a Council Directive Supplementing the Introduction of Measure to Encourage Improvements in the Safety and Health at Work of Temporary Workers, Syn 281 (provisional version, June 26, 1990).

¹⁵ ETUC meeting; EC Commission, Explanatory Memorandum on the Proposals for Directives Concerning Certain Employment Relationships, June 26, 1990.

¹⁶ Ibid.; EC Commission meeting.

¹⁷ EC Commission meeting; USITC staff meeting with DG-V staff, Brussels, June 6, 1990 (DG-V meeting).

¹⁸ Ibid.

¹⁹ Ibid.

²⁰ Ibid.

²¹ Ibid.

²² Ibid.

²³ UNICE comments.

²⁴ Ibid.

²⁵ EC Commission meeting.

²⁶ ETUC meeting.

²⁷ USITC staff meeting with representative of French employers' association (CNPF), Paris, June 11, 1990 (CNPF meeting).

²⁸ Proposal for a Directive Concerning Certain Aspects of the Organization of Working Time, Com (90) 317/2, OJ No. 1022 (July 25, 1990).

the requirements are incorporated into collective bargaining agreements.²⁹

The EC Commission has approached its regulation of working time from a health perspective. As such, the proposed directive is based on the worker health and safety provision of EEC Treaty article 118a and is therefore subject to qualified-majority approval. With regard to work hours and rest periods, the EC Commission justifies reliance on the safety and health provision on studies showing a relationship between hours worked on one hand and worker stress and fatigue, as well as workplace injuries, on the other.³⁰ In support of its regulation of night work and shift work, the EC Commission relies on studies indicating that night and shift workers have higher health and accident risks than other workers.³¹

For day workers, the proposed directive requires a minimum 11-hour rest period for every 24 hour period and a minimum 1-day rest period for every 7-day period.³² For night and shift workers, the directive permits no longer than an average of 8 continuous work hours per 24 hours over a 14-day period. In addition, night workers may not work overtime, are entitled to free health assessments, and must be transferred to day work if they suffer from health problems associated with the night work. In addition, employers who regularly use night workers must keep the workers or their representative informed in safety and health matters.³³

Derogation from the provisions of the directive is permitted by collective bargaining, in cases of force majeure or national emergencies, and for seasonal work or when "the features peculiar to certain activities or exceptional situations limited in time objectively conflict with the [directive's] provisions."³⁴ This latter exception is intended to exempt work on oil rigs (where fortnightly shifts are the norm), as well as workers in the transportation and distribution sectors.³⁵ A U.S. representative of a multinational communications firm has expressed concern about application of the working time directive to journalists, who often must work continuously for periods exceeding those permitted

²⁹ Ibid., art. 12(3); *Explanatory Memorandum Concerning the Proposal for a Directive on Certain Aspects of the Organization of Working Time* (Explanatory Memorandum on Working Time); DG-V meeting; D. Buchan, "Brussels offers flexibility on working hours," *Financial Times*, July 26, 1990, p. 2. EC Social Affairs Commissioner Papandreou has warned, however, that member states will still be open to legal proceedings in the European Court of Justice if such collective bargaining agreements fail to implement the directive. Ibid.

³⁰ *Explanatory Memorandum on Working Time*.

³¹ Ibid.

³² Com (90) 317/2, sec. II.

³³ Ibid., sec. III.

³⁴ Ibid., sec. IV.

³⁵ "EC Lays Out Proposals on Work Hours, Night Work," 1992 - *The External Impact of European Unification*, vol. 2, No. 9 (July 27, 1990), p. 8; EC Commission meeting.

by the directive.³⁶ It appears, however, that the "peculiar features" exception would apply to such work.

UNICE views the proposed directive as breaching the principle of subsidiarity.³⁷ According to UNICE representatives, this directive illustrates an overreaching of EC legislation into areas that are traditionally handled by labor negotiations.³⁸ Further, UNICE objects to the use of article 118a as the basis for this directive and questions the EC Commission's interpretation of the night work studies.³⁹

Other Measures Under Consideration

Proof of Work Contracts

The EC Commission currently is working on a proof of work directive that would require written contracts of employment. Under the directive, workers would be entitled to have the terms and conditions of their employment set out in writing.⁴⁰ Whereas this directive would impose new requirements in some member states, other member states already have legislation on this subject.

Some of the strictest requirements on this subject are contained in existing Spanish laws.⁴¹ In Spain, most employment contracts are already written, except for those covering short-term employment such as construction. In addition, Spanish work contracts are permanent and can only be terminated with grounds for termination. When the Socialists came into power, they had to face high levels of unemployment due largely to the threat of these permanent work contracts. The Spanish Government took a flexible approach and allowed temporary contracts. The Government now allows unlimited temporary contracts for terms of up to 3 years. After 3 years, the company must either terminate the worker or give the worker a permanent contract.⁴²

Cross-Border Subcontracts

The EC Commission is also drafting a proposal on cross-border subcontracts.⁴³ The directive will address the wages, benefits, and work conditions

³⁶ USITC staff meeting with industry representative, Brussels, June 6, 1990.

³⁷ "EC Lays Out Proposals on Work Hours, Night Work," UNICE comments. The principle of subsidiarity and its role in the social dimension is discussed in ch. 18 of the First Followup Report. UNICE General Secretary Tyszkiewicz suggests application of the definition of subsidiarity put forth by Altiero Spinelli in the Askins Memo on Internal Reform: "Where member states acting together can produce a better result, the EC must act."

³⁸ Ibid.

³⁹ Ibid.

⁴⁰ ETUC meeting.

⁴¹ USITC staff meeting with representative of GM Spain, Madrid, June 13, 1990; USITC staff meeting with representative of Spanish Confederation of Business Organizations (CEOE), Madrid, June 14, 1990 (CEOE meeting).

⁴² Ibid.

⁴³ ETUC meeting; DG-V meeting.

applicable to workers from one member state who are sent to work on a project in another member state. Generally, for long-term fixed duration subcontracts, the rules of the country in which the work takes place will apply.⁴⁴ This approach, however, has resulted in a dilemma for France. Pursuant to the applicable EC directive, France proposed a law under which it would pay French social security benefits to workers and their families from other countries when such workers are working in France. The French Court held this law was unconstitutional under the French constitution, because it would discriminate against citizens of other states. France is therefore caught between its own Court's interpretations of its constitution and the EC's law.⁴⁵

A subcontract question that still needs to be addressed by the EC concerns short-term contracts, e.g., when workers cross the border for a few days or weeks.⁴⁶ A recent decision by the European Court of Justice touches upon this question. In the *Rush Portuguese* decision,⁴⁷ the Court ruled that a Portuguese company was entitled to move its own labor force, paid at Portuguese rates, to France (or any other member state) for the term of a construction or public works contract. The Court reasoned that, since the workers were only sent for a few months, this practice would not disrupt the French labor market. Countries such as France and West Germany, which pay high wages and benefits, view this decision unfavorably, because they would be required to pay Portuguese or any other workers employed within their countries at the French or German rate, whereas a Portuguese company can bring in Portuguese employees and pay them at the lower Portuguese rate.⁴⁸ The Court's decision, however, provides a means for the high-wage countries to impose equal wages and benefits for all workers working within their territory. To this end, the decision notes that EC law does not prevent a member state from extending its labor legislation or collective bargaining agreements to cover workers temporarily employed in its territory, irrespective of the country where the employer is established. It is unclear how this decision will influence the EC Commission's proposed cross-border subcontract directive.

The directives on cross-border employment also raise other important financial questions for countries such as France in which many non-EC citizens work.⁴⁹ In this regard, the EC Commission,

and to lesser extent, the Court of Justice, must decide whether the relevant directives apply to European citizens or to European workers. The answer to this question influences all of French social policy, because of the large number of North Africans residing in France. France is very favorable to EC action when the EC Commission talks about European citizens, but when the EC Commission talks about any worker in the EC, France is concerned about the financial expense.⁵⁰

Worker Information, Participation, and Consultation

As noted in the first followup report, the EC Commission has stated its intention to issue an "instrument" this year on the controversial subject of worker information, consultation, and participation. It is still uncertain whether this instrument will be in the form of a directive (the implementation of which would be obligatory upon the member states) or a nonbinding recommendation.⁵¹ Although the Vredeling proposal is still technically on the table, an EC Commission representative has indicated that it is not the Commission's purpose to reopen the Vredeling controversy.⁵² The outcome of the European Company Statute directive on worker participation and consultation will probably influence the social measure on worker consultation and participation, although the latter will be more broadly based.⁵³ As discussed in chapter 9 ("Competition and Corporate Structure") of this report, the European Company Statute is now under discussion in the EC Council.

Safety, Hygiene, and Health Agency

Another measure that the EC Commission is likely to present this year involves the establishment of an occupational safety and health agency.⁵⁴ The agency would fill the need to provide worker safety and health information and to follow up on implementation and enforcement of relevant directives.⁵⁵ Member states such as the United Kingdom, which already have strong worker safety and health programs, favor the creation of an EC-wide agency.⁵⁶ In their view, the establishment of such an agency puts somebody in charge of seeing what is really going on at the worksites in the various countries. It could monitor the behavior of the field inspectors in the different countries and see which countries actually enforce their occupational safety and health laws and take companies to court. It would work towards getting to common standards *as applied*.⁵⁷

⁴⁴ Ibid.

⁴⁵ USITC staff meeting with staff of French interministerial committee on EC affairs (SGCI), Paris, June 11, 1990 (SGCI meeting).

⁴⁶ Ibid.; DG-V meeting.

⁴⁷ Case No. C-113/89 (EC Court of Justice, Mar. 27, 1990). See *European Report*, No. 1576, Internal Market, p. 4 (Mar. 31, 1990).

⁴⁸ SGCI meeting.

⁴⁹ SGCI meeting.

⁵⁰ Ibid.

⁵¹ DG-V meeting.

⁵² EC Commission meeting.

⁵³ DG-V meeting; ETUC meeting.

⁵⁴ EC Commission meeting.

⁵⁵ Ibid.

⁵⁶ USITC staff meeting with British representative, London, May 31, 1990.

⁵⁷ Ibid.

In addition, an EC-wide agency would allow the packaging of the different skills that are prevalent in the various EC countries.⁵⁸ The United Kingdom is strong in risk assessment and exposure monitoring but relatively weak on access to medical advice for workers. France is strong in all of these factors but weak in the dissemination of information among the various bodies in charge of the individual subjects. West Germany has good technical engineers and chemists but has few actual industrial hygienists.⁵⁹

Worker Notification of Takeover

The EC Commission is also working on an amendment to another directive that falls outside the social dimension action program, but has implications for labor relations. Specifically, the EC Commission intends to expand the existing successor company directive,⁶⁰ which requires advance notice and certain other rights to workers affected by a takeover. The existing directive covers only the takeover of a company from one member state by another company of the same state. Michelin, a French company, took over a company in Belgium without affording the notice and other rights required by the directive. It successfully argued that its takeover was not covered by the directive since the company taken over was incorporated in a different member state. The EC Commission intends to close this loophole by expanding this directive to cover all takeovers by companies within the EC.⁶¹

The Social Dialog

As explained in Chapter 18 of the First Followup report, the "Social Dialogue" consists of institutionalized talks between management and labor at the Community level. To date, the talks have been aimed at adopting nonlegislative "joint options" that are presented and discussed with employers and workers in each member state.⁶²

The Social Dialogue Steering Committee, consisting of representatives from ETUC, UNICE, and CEEP, met in January and July of 1990.⁶³ At these meetings, the committee issued a joint option concerning vocational training. The option suggests that companies should be responsible for the funding of training programs. It also recognizes the rights of workers or their representatives to be informed and consulted on training programs.⁶⁴ The committee also progressed on finalization of a

joint option addressing the mobility within, and improved functioning of, the European job market.⁶⁵ Adoption of this option is subject to agreement of the signatory organizations.⁶⁶ A paper on flexibility and adaptability in the workplace has been on the table for some time, but it remains blocked by the ETUC at the insistence of two member unions (IGM and DGB).⁶⁷ The social dialog will be resumed in September 1990.

Currently, management and labor have different views as to the role of the social dialog.⁶⁸ Labor, as represented by ETUC believes labor regulation should be addressed by legislation or by binding agreements between employers and unions at the European level. In contrast, management's view, as expressed by UNICE, is that most labor matters should be negotiated through local collective bargaining agreements.⁶⁹

Consistent with their respective preferences, representatives of the two associations disagree as to the likelihood or effectiveness of EC-wide bargaining. Whereas ETUC representatives believe that the eventual emergence of such bargaining is inevitable,⁷⁰ representatives of UNICE and other employer organizations do not endorse negotiations at this level.⁷¹ Some industry representatives believe collective bargaining is so different between countries that it would be impossible to reach agreement.⁷² For example, companies in Italy employ centralized bargaining; whereas West German companies must deal individually with each region or lander; and, in the United Kingdom, there are few or no collective bargaining agreements because problems are dealt with at the enterprise level. There are also other differences among the countries that industry representatives say would make EC-wide collective bargaining difficult. For example, France has separate bargaining units for white collar and blue collar workers, whereas West Germany does not.⁷³

There are some instances of Europeanwide collective bargaining. The construction and auto industries currently have some such agreements, but they only discuss training matters.⁷⁴ Furthermore, the unions within an industry sector will often agree to sign the same agreement as that negotiated by another local union. A landmark negotiation of this sort took place this year in West Germany, when a local IG Metall union negotiated a reduced-working-time agreement. Other IG Metall unions of other lander then agreed to sign the same agreement, which now applies to the metal industry

⁵⁸ Ibid.; USITC staff telephone conversation with Representative of General Motors, May 24, 1990.

⁵⁹ Ibid.

⁶⁰ Council Directive 78/855 (Oct. 9, 1978).

⁶¹ DG-V meeting.

⁶² J.M. Didier, "Workers' Rights in the EC's Single Market," pt. 2, 1992—*The External Impact of European Unification*, Vol. 1, No. 20 (Jan. 26, 1990), p.13.

⁶³ EC Committee of the American Chamber of Commerce, *Business Guide to EC Initiatives*, p. 18.

⁶⁴ Ibid.

⁶⁵ Ibid.; *Europe*, No. 5203 (Feb. 28, 1990), p. 13.

⁶⁶ Ibid.

⁶⁷ Ibid.; UNICE comments.

⁶⁸ Ibid.; EC Commission meeting; DG-V meeting; ETUC meeting.

⁶⁹ Ibid.

⁷⁰ ETUC meeting.

⁷¹ UNICE comments; CNPF meeting.

⁷² Ibid.

⁷³ Ibid.

⁷⁴ Ibid.

throughout West Germany.⁷⁵ There is also an emerging tendency for cross-sector adoption of contract provisions.⁷⁶

The question of EC-wide bargaining is now linked to the reliance placed on the joint options reached by management and labor in the social dialog.⁷⁷ ETUC wants to give concrete value to these joint options, whereas UNICE does not want the options to interfere with the flexibility and adaptability of the collective bargaining process.⁷⁸ In the view of one EC Commission representative, the less productive the social dialog, the more pressure the ETUC will apply for use of the legislative approach.⁷⁹

Related to the employer-union debate over the appropriate use of collective bargaining is a question concerning implementation by Italy of existing labor-related directives.⁸⁰ The Italian Government believes some of the subjects legislated by the EC should be left to collective bargaining. The EC Commission has three times successfully brought Italy to court for failure to implement a measure requiring worker consultation prior to work reorganization.⁸¹ Nonetheless, Italy still has failed to implement the measure to the EC's satisfaction.⁸²

Court of Justice Decisions

During the period covered by this Report, there have been three significant decisions by the Court of Justice in the social dimension area. One of these decisions – *Rush Portuguesa* – was discussed above, in the section on cross-border subcontracts.

The other two cases involved sex discrimination. Article 119 of the EEC Treaty provides that men and women must receive equal pay for equal work. This provision, however, does not explicitly prohibit other forms of employment discrimination, such as discrimination in hiring and firing.⁸³ There are, however, EC directives forbidding these other forms of employment discrimination.⁸⁴

The distinction between the pay discrimination prohibited by the treaty and other forms of discrimination prohibited by EC directives is

important in determining what types of discrimination actions will be upheld.⁸⁵ In 1986, the Court of Justice ruled that a worker employed by a public authority can sue under the EC equal treatment directive, even if the member state has not yet implemented the directive; but, absent national legislation, a person employed in the private sector cannot sue.⁸⁶ In a recent decision, the court extended this rule to allow such suit against a public utility (British Gas).⁸⁷ While these proceedings were pending, the EC Commission successfully sued the United Kingdom for failure to implement the equal treatment directive.⁸⁸ The United Kingdom has since implemented the directive, and an employee of a private company could therefore now sue the company for failure to comply with national law.

In contrast to other discrimination issues, any worker can sue for equal-pay discrimination, because the right to equal pay is in the EEC Treaty and therefore applies to public and private firms alike.⁸⁹ Because of this distinction, the determination of what constitutes "pay" within the meaning of article 19 is important. Article 19 defines "pay" as "the ordinary basis or minimum wage or salary or any other consideration, whether in cash or kind, which the worker receives, directly or indirectly, in respect of his employment from his employer."

The Court of Justice recently determined that retirement benefits paid upon involuntary dismissal fall within the article 19 definition of "pay."⁹⁰ In the *Barber* case, a 52-year-old male employee who lost his job challenged his company's pension plan, under which he would not be entitled to benefits until age 55 whereas a female employee in the same position would have been entitled to benefits as of age 50. In its first decision finding pay discrimination against men, the Court held that the sex-based distinction in the plan was prohibited under the "equal pay" provision of article 19. Many EC firms, including U.S. companies doing business in the EC, are likely to be affected by this decision.⁹¹ Tax advisors are recommending that firms review provisions of their pension plans such as spousal benefits, early and late retirement provisions, and waiting periods.⁹²

⁷⁵ Ibid.

⁷⁶ UNICE comments.

⁷⁷ CNPF meeting.

⁷⁸ Ibid.

⁷⁹ EC Commission meeting.

⁸⁰ DG-V meeting.

⁸¹ Ibid.

⁸² Ibid.

⁸³ USITC staff meeting with Professor Trevor Hartley, London School of Economics, London, June 1, 1990 (Hartley meeting).

⁸⁴ E.g., Council Directive No. 76/207 on equal treatment of men and women at work.

⁸⁵ Hartley meeting.

⁸⁶ Ibid.; *Marshall v. Southampton and South West-Hampshire Area Health Authority*, ECR 723 (EC Court of Justice, 1986).

⁸⁷ *Foster and Others v. British Gas plc*, Case C-188/89 (EC Court of Justice, July 12, 1990).

⁸⁸ L. Kellaway, "Court Rules on EC Directives," *Financial Times*, July 13, 1990, p. 22.

⁸⁹ Hartley meeting.

⁹⁰ *Barber v. The Guardian Royal Exchange Assurance Group*, Case No. C-262/88 (EC Court of Justice, May, 17 1990).

⁹¹ 1992 – *The External Impact of European Unification*, vol. 2, No. 8 (July 13, 1990), p. 9.

⁹² Ibid.

CHAPTER 16
RESEARCH AND DEVELOPMENT

CONTENTS

	<i>Page</i>
Background	16-3
Research and development funding	16-3
European Community research and development policy	16-4
Cooperative research and development in Europe	16-4
EC Framework research and development programs	16-5
Legal basis for the Framework programs	16-5
Framework structure	16-6
The Framework programs	16-6
ESPRIT	16-8
RACE	16-8
BRITE/EURAM	16-8
Nuclear fusion	16-8
Support programs	16-9
Non-Framework programs	16-9
European Research Cooperation Agency (EUREKA)	16-9
European Space Agency (ESA)	16-10
European Science Foundation (ESF)	16-10
European Centre For Nuclear Research (CERN)	16-10
Cooperation on Science and Technology (COST)	16-11
Participation by non-EC members in EC research and development	16-11
Current agreements	16-11
Utilization and dissemination of results	16-12
Outlook	16-12
 Figures	
16-1. Second and third Framework program budgets	16-7
16-2. European Community research programs	16-14

CHAPTER 16 RESEARCH AND DEVELOPMENT

Background

In the 1980s, the European Community, once at the forefront of scientific and technological innovation, found itself falling behind the United States and Japan in key areas of economic importance, such as information technology and telecommunications; materials technology, especially superconductors; aeronautics; biotechnology; and energy. A study conducted by the EC to determine which countries were the leaders in science and technology identified 37 economically important technological sectors and concluded that 31 of these were dominated by the United States, 9 by Japan, and only 2 by European countries.¹

Further indications of the decline of European science and technology efforts were found in almost every measure of research and development (R&D). For example, in 1986, 4 out of 5 patent applications for new materials were filed either by U.S. or Japanese firms and, of the 10 leading computer firms, 7 were U.S., 2 were Japanese, and only 1 was European.² The United States also has the edge in total number of R&D workers, which was estimated at 825,000 in 1986 compared with 500,000 in the EC.³ The relative superiority of the United States in research and technology is reflected in technology input and output indicators, such as the number of researchers relative to total labor force, R&D share of sales, and patents issued per capita.⁴

The EC's decline in world stature in scientific and technological innovation was attributed to a number of factors that were primarily an outgrowth of the fragmentation of the R&D community in Europe.⁵ Division of research and development projects along national boundaries led to a reduction in the number and scope of projects because available resources in individual European

¹ Office for Official Publications of the European Communities, *Research and Technological Development Policy*, Luxembourg, 1988, (Periodical 2/1988,) p. 8. The individual figures do not add to totals because some sectors are dominated by two countries equally.

² Ibid.

³ Ibid.

⁴ Fabrizio Onida, "Technological Competition, Structural Change, and International Integration of European Single Market," conference paper prepared for the *American Enterprise Institute*, Washington, DC, Mar. 5-8, 1990, pp. 55 and 59. There were 69 R&D workers per 10,000 labor force in the United States in 1986 compared with 63.2 in Japan (1985), and less than 50 each in West Germany, France, and the United Kingdom (1984). Similarly, there were 157.88 patents issued per million population in the United States during 1980-85, compared with 78.98 in Japan and 51.15 in Western Europe.

⁵ "The E.C.'s Research and Technological Development," *Europe*, December 1988, pp. 28-30.

countries were much less than those in larger countries such as the United States. For example, total U.S. R&D expenditures were nearly 10 times those of the United Kingdom and 5 times those of West Germany.⁶ According to some reports, this fragmentation contributed to researchers' working in isolation and needlessly duplicating projects in individual national programs. As a result, some experts posited that European resources were not being used effectively.⁷

Research and Development Funding

In most countries, Government funds are a significant source of support for research and development efforts; however, there are differences in the purpose and direction of publicly funded R&D. In the United States, Government funding and the mission of the Government are closely related. As a result, more than 90 percent of public funds for R&D is allocated to defense, space, and energy projects.⁸ In the EC, government support of research and development is much more closely tied to economic development and improvement in industrial products and processes. Two of the principal reasons given for greater government support of economic development in the EC are that (1) this was necessary in order to rebuild industries after World War II and (2) smaller industries and markets, such as those found in European countries, need government assistance to survive.⁹

Between 1980 and 1989, Federal spending on R&D in the United States grew by an estimated 36 percent in real terms. The growth in total Federal spending was attributed entirely to defense-related R&D, primarily product development, which increased rapidly during 1980-89. In 1989, defense projects accounted for nearly two-thirds of Federal R&D spending, compared with 47 percent in 1980. During this time, spending on defense product development doubled, while funding of defense basic research increased 17 percent. However, basic research accounts for less than 3 percent of defense R&D. In contrast, total public spending on nondefense R&D decreased 3 percent during the period, even though spending on nondefense basic research increased by 51 percent. Private sector expenditures on R&D efforts mirrored defense Government spending, rising 40 percent between 1980 and 1989.¹⁰

Total defense and nondefense R&D expenditures of the members of the European Community lagged behind those of the United

⁶ Leonard L. Lederman, "Science and Technology Policies and Priorities: A Comparative Analysis," *Science*, vol. 237, September 1987, p. 1127.

⁷ "The E.C.'s Research and Technological Development," pp. 28-30.

⁸ National Science Board, *Science and Engineering Indicators-1989* (Washington, D.C., U.S. Government Printing Office, 1989), p. 91.

⁹ Lederman, "Science and Technology Policies and Priorities," p. 1125.

¹⁰ National Science Board, *Science and Engineering Indicators-1989*, pp. 91-94.

States¹¹ even though most of the EC nations showed growth in R&D spending during the 1980s. The exception to this trend was the United Kingdom, where the absolute funding level showed no significant change. The increase in West Germany's R&D came mainly from increased industrial spending; in France and Italy, gains were attributed mainly to increased Government spending. Government spending on defense-related research varied significantly from country to country; the United Kingdom spent 51 percent of its Government R&D budget on defense; France, 34 percent; and West Germany, 12.5 percent.¹² In terms of total expenditures, wide differences exist between the amounts spent by countries such as West Germany, the United Kingdom, and France, which together account for over three-fourths of R&D expenditures in the EC, and R&D funding levels in Spain, Portugal, and Greece, which spend very little on science and technology activities. Public funding is generally the most important source of R&D spending in the EC, and only in West Germany and Belgium are public expenditures less than those of industry.

European Community Research and Development Policy

Research programs sponsored and funded by the EC can be best described as either target-oriented basic research or precompetitive technological R&D. In either case, the projects are neither totally commercial nor totally academic in nature, but fall between these two extremes. Target-oriented research, unlike pure basic research, focuses on possible applications; precompetitive research is a stage in the technological process prior to that of commercial development. The three major R&D areas listed below and targeted under the Third Framework Program (1990-94), the EC's master plan for R&D, exemplify research topics that can be classified as either precompetitive R&D or target-oriented basic research.

- Diffusion of technologies in the fields of information, communication, and industrial and material management.
- Management of natural resources, such as environment, life sciences, and energy.
- Management of intellectual resources, such as human capital and mobility.

The EC R&D policy is designed to manage resources efficiently, avoid duplication of work between individual countries, improve

¹¹ Patrick Johnson, "Summary Report on the State of Science and Technology in Europe," *European Science Notes Information Bulletin*, Office of the Naval Research Office, Publication No. 90-02, p. 24. In 1985, total R&D spending in the United States was 75 percent higher than that of the EC. In terms of R&D expenditures measured as a percent of GDP, the United States' spending accounted for 2.8 percent of GDP and EC countries' totaled only 1.9 percent.

¹² *Ibid.*, p. 27.

productivity, and assist member states to compete effectively in the international market. The EC's R&D policy discourages individual members from directing their resources to create national advantages; instead, it encourages them to pool their resources to their advantage in international competition, especially in high technology areas where significant manpower and economic resources are needed. EC R&D policy gives priority to projects that strengthen the unity of the European market or the European scientific community and to those projects that fulfill certain public service obligations, such as infrastructure and the environment in the unified EC.¹³

National programs are financed principally by the respective governments and account for just over 95 percent of total Government R&D spending in the EC and include basic, precompetitive, and competitive research. The EC supports member-state aid that is intended to further certain industrial policy goals, such as promoting R&D in general and assisting the R&D efforts of small and medium-sized enterprises (SMEs). However, the EC generally does not support assistance that is targeted to specific commercial endeavors.¹⁴ However, many of the national governments actively participate in shaping their industrial policies through large government-support programs for R&D leading to standards development. These standards can be used as important competitive weapons to lock in customers and to lock out competitors.¹⁵

Cooperative Research and Development in Europe

The 1980s saw the emergence of a series of highly integrated, second-generation European R&D programs in major technological areas. The First Framework Program, an umbrella program implemented in 1984, set forth the Community's R&D policy, established research objectives, and listed research activities for the period 1984-87. The EC R&D efforts were formalized by the Community adoption of the Single European Act (SEA) in 1985, which defined the objectives and methods of implementation of cooperative R&D. The Second Framework Program, implemented in 1987, and the Third Framework Program, implemented in 1990, are the blueprints for Community R&D through 1994.

In addition to these EC-originated Framework programs, there are several other multinational R&D programs in which the EC and its members participate. The largest of these, EUREKA, was

¹³ EC Commission, *EC Research Funding*, January 1990.

¹⁴ USITC, *Foreign Industrial Targeting and its Effects on U.S. Industries, Phase II, The EC and Member States* (Investigation No. 332-162), USITC Publication 1517, April 1984, p. 16.

¹⁵ OECD, *Information Technology and New Growth Opportunities*, Paris, 1989.

established in 1985 to promote international cooperation in science and technology. Included among its members are the countries of the EC and the European Free Trade Association (EFTA)¹⁶ as well as Turkey. The EC and its members also participate in other international research organizations, such as the European Space Agency (ESA), the European Centre for Nuclear Research (CERN), and the European Science Foundation (ESF).

EC Framework Research and Development Programs

Legal Basis for the Framework Programs

When the SEA was implemented on July 1, 1987, it incorporated EC science and technology policy into the 1992 program. Article 24 of the SEA added title VI to the EEC Treaty¹⁷, which for the first time granted R&D policy an equal status with other areas, such as economic and social policy.¹⁸ Article 130 F of title VI states that its aim is to "strengthen the scientific and technological basis of European industry and to encourage it to become more competitive at [the] international level."¹⁹ As set forth in article 130 G, the EC is now officially responsible for the following:

- implementing research and technological development and demonstration of programs, including support for cooperation among firms, research centers, and universities;
- promoting cooperation with third countries and international organizations;
- disseminating and evaluating research results; and
- promoting training and the mobility of researchers in the Community.

¹⁶ The EFTA countries are Finland, Switzerland, Iceland, Norway, Austria, and Sweden.

¹⁷ Treaty establishing the European Economic Community, Rome, Mar. 25, 1957.

¹⁸ EC Commission, *EC Research Funding*.

¹⁹ Art. 130 F further states—

1. In order to achieve this, it shall encourage undertakings including small and medium-sized undertakings, research centers and universities in their research and technological development activities; it shall support their efforts to cooperate with one another, aiming, in particular, at enabling undertakings to exploit the Community's internal market potential to the full, in particular through the opening up of national public contracts, the definition of common standards and the removal of legal and fiscal barriers to that cooperation.

2. In the achievement of these aims, particular account shall be taken of the connection between the common research and technological development effort, the establishment of the internal market and the implementation of common policies, particularly as regards competition and trade.

Article 130 H grants the EC Commission responsibility for taking initiatives to promote the coordination of EC member-state policies and programs relating to cooperative research and development. Before the passage of the SEA, the EC played a role in formulating policy for cooperative R&D in the EC under the provisions of article 235 of the EEC Treaty. This provision was first employed in 1974 by a Council resolution to cover the coordination by the EC of member-state policies and research projects in science and technology.

The EC Commission plays two somewhat different roles in formulating EC R&D policies, that of directing EC-funded R&D projects and that of coordinating member-state programs relating to R&D. Title VI specifies that the Community is to carry out its responsibilities over R&D at the EC level by adopting a multiannual Framework program that lays out scientific and technical objectives, establishes priorities, and sets forth the principal program features. In addition it determines funding levels, member-state contributions to specific programs, and distribution of the funds among various research activities. The final Framework program must be unanimously adopted by the Council;²⁰ specific R&D programs need only be adopted by a qualified majority of the Council.²¹ For each program, the Council determines the scientific or technological content, the duration of the project, and an approximation of the level of funding necessary to complete the program.

When developing its framework program, the Community receives expert advice from three advisory committees whose members are drawn from industry, the scientific community, and government.²² These advisory committees are as follows:

- CREST (Scientific and Technical Research Committee), which coordinates research policies between the EC member countries and the EC;
- CODEST (Committee for the European Development of Science and Technology) which drafts proposals for new priority support areas and strategies and advises the Commission on the implementation of the SCIENCE²³ program; and
- IRDAC (Industrial Research and Development Advisory Committee), which provides recommendations on questions of industrial research and development.

²⁰ Art. 130 Q.

²¹ *Ibid.*

²² EC Commission, *EC Research Funding*, p. 7.

²³ Stimulation des Cooperations Internationales et des Echanges Necessaires aux Chercheurs en Europe (Stimulation of the International Cooperation and Interchange Need by European Research Scientists).

Framework Structure

The Community has three types of administrative and technical instruments available within the Framework structure for implementing its R&D activities. The bulk of Framework R&D is performed either in-house at the EC facilities of the Joint Research Center (JRC) or is contracted out to universities, research institutes, or industry and is generally financed on a shared-cost basis. In addition, a third form of R&D support consists of Community-level coordination of programs carried out at the member-state level for which the EC funds only the costs of meetings, communications among research groups, and other administrative tasks that promote international cooperation.²⁴

The JRC is composed of nine institutes²⁵ and has facilities located in Italy, Belgium, the Netherlands, and West Germany, with a combined staff of over 2,000. Initially, the JRC was created by the Euratom Treaty to perform nuclear research; subsequently, the JRC expanded its mission to other areas, such as safety, environmental protection, and satellite remote sensing. However, the JRC is no longer the dominant research tool of the EC, and its stature and funding is declining.²⁶ In the 1990s, JRC R&D will focus on the same areas as the other Framework Programs and will concentrate on developing closer cooperation with industry.

Contract research accounts for approximately 80 percent of Framework R&D funding and nearly all of the major EC R&D projects are funded in this manner. Generally, these are cost-sharing projects in which companies or institutes contribute half of the total expenditures. Noncommercial organizations, such as universities, that perform research activities within the Framework Programs may receive up to 100 percent of project costs from the EC.²⁷

The Framework Programs

The basic selection criteria for Framework projects were introduced in 1984 and applied for the first time in the Second Framework Program. These selection factors, called the Reisenhuber criteria, were promulgated by Dr. Heinz Reisenhuber, then the West German Research Minister. The Reisenhuber criteria are still central to the choice of EC research projects today and favor projects that —

- are too large or complex to be funded and staffed by individual countries;

²⁴ USITC, *Operation of the Trade Agreements Program*, USITC Publication 2208, July 1989, p. 83.

²⁵ The institutes include Prospective Technological Studies, Advanced Materials, Systems Engineering, Transuranium Elements, Remote Sensing Application, Environment, Safety Technology, Center for Information Technologies and Electronics, and Central Bureau for Nuclear Measurements.

²⁶ American Chemical Society, Government Relations Office, "The Effect of the European 1992 Plan on U.S. Science Policy and the Chemical Industry," by Anthony Boccanfuso, American Chemical Society Science Fellow.

²⁷ EC Commission, *EC Research Funding*, p. 15.

- will strengthen the unity of the European market or the scientific and technological community, such as research leading to the setting of pan-European standards;
- will be financially rewarding to all concerned; and
- will require coordinated efforts by many countries or in large geographical regions, such as environmental projects.²⁸

The First Framework Program (1984-87), approved by the Council in 1983, had EC funding of more than 3.7 billion ECU.²⁹ Its primary emphasis was on energy research, which received nearly half of the total funding. The seven sectors of the First Framework Program and their funding are shown in the following tabulation (in millions of ECU):³⁰

Sector	Funding
Energy research	1,770
Strengthening of industrial competitiveness	1,060
Quality of life and of the world of work	385
Horizontal activities ¹	175
Agriculture and fisheries	130
R&D for the developing countries	130
Raw materials	80
Total	3,730

¹ The horizontal activities (now called Supporting Measures) consisted of: forecasts and assessments (FAST); stimulation of transboundary European scientific cooperation; and information and documentation.

The Second Framework Program (1987-91) had a budget of 5.4 billion ECU and was divided into eight sectors (fig. 1). The importance of energy research within the Second Framework declined both in absolute and relative value. The largest increase was in the area of information and telecommunications technologies, which accounted for more than 40 percent of the total budget. Although the Second Framework was scheduled to continue through 1991, the EC felt that the speed with which technology was changing and the need to buttress international competitiveness warranted immediate increased spending and a reorganization of R&D priorities.³¹ As a result, the Third Framework Program (1990-94) was approved in April 1990, with total funding of 5.7 billion ECU.

The principal difference between the Second and Third Framework Programs was in the allocation of funds. Funding for information and communications technologies was reduced slightly

²⁸ Dr. Joseph Rembser, "Europe 1992: The Perspectives for International Scientific and Technological Cooperation," foreign science lecture, American Association for the Advancement of Science, Nov. 2, 1989.

²⁹ In 1989 1 ECU equaled \$1.10. The dollar equivalent of 1 ECU rose from \$.79 in 1984 to \$1.18 in 1988.

³⁰ Rembser lecture.

³¹ EC Commission, *Proposal for a Council Decision Concerning the Framework Programme of Community Activities in the Field of Research and Technological Development (1990-1994)*, Aug. 2, 1989.

Figure 16-1
Second and third Framework programme focal areas and budgets

Framework Programme 1987-1991			Framework Programme 1990-1994		
Focal areas	Sum in million ECU	Proportion of total budget (%)	Focal areas	Sum in million ECU	Proportion of total budget (%)
1. Quality of life	375	6.9	I. Enabling technologies		
1.1 Health	60		1 Information and communications technologies	2 221	38.9
1.2 Radiation protection	34		-- Information technologies	1 352	
1.3 Environment	261		-- Telecommunications	489	
2. Towards a large market and an information and communications society	2 275	42.3	-- Development of technological systems of general interest	380	
2.1 Information technologies	1 600		2 Industrial and materials technologies	888	15.6
2.2 Telecommunications	550		-- Industrial and materials technologies	748	
2.3 New services of common interest (including transport)	125		-- Measurement and testing	140	
3. Modernization of industrial sectors	645	15.6	II. Management of natural resources		
3.1 Science and technology for the manufacturing industry	400		3 Environment	518	9.1
3.2 Science and technology of advanced materials	220		-- Environment	414	
3.3 Raw materials and recycling	45		-- Marine science and technology	104	
3.4 Technical standards, measurement methods and reference materials	180		4. Life sciences and technologies	741	13.0
4. Exploitation and optimum use of biological resources	280	5.2	-- Biotechnology	164	
4.1 Biotechnology	120		-- Agricultural and agro-industrial research (incl. fisheries)	333	
4.2 Agro-industrial technologies	105		-- Biomedical and health research	133	
4.3 Competitiveness of agriculture and management of agricultural resources	55		-- Life sciences and technologies for developing countries	111	
5. Energy	1 173	21.7	5 Energy	814	14.3
5.1 Fission: nuclear safety	440		-- Non-nuclear energies	157	
5.2 Controlled thermonuclear fusion	611		-- Nuclear fusion safety	199	
5.3 Non-nuclear energies and rational use of energy	122		-- Controlled thermonuclear fusion	458	
6. Science and technology for development	60	1.5	III. Management of intellectual resources		
7. Exploitation of the sea bed and use of marine resources	80	1.5	6 Human capital and mobility	518	9.1
7.1 Marine science and technology	50		Total	5 769	100.0
7.2 Fisheries	30				
8. Improvement of European S/T cooperation	288	5.3			
8.1 Stimulation, enhancement and use of human resources	180				
8.2 Use of major installations	30				
8.3 Forecasting and assessment and other back-up measures (including statistics)	23				
8.4 Dissemination and utilization of S/T research results	55				
Total	5 366	100.0			

including 1 111 million for the centralized management of the dissemination and exploitation of research results, and 1 111 million for the Joint Research Centre (JRC).

Source: EC Commission, EC Research Funding, 1990.

and redirected from traditional to new areas, such as microelectronics and networks connecting information systems. In the Third Framework, the number of sectors was reduced from eight to three to promote greater cooperation and cross fertilization among existing programs; however, individual projects and programs were not directly affected by this change. In addition, emphasis on environmental protection and life science technologies increased and that of the energy sector diminished. The amount of funding devoted to management of intellectual resources, namely the mobility and training of research personnel, was more than twice that of the Second Framework.³²

The following is a discussion of the more important segments of Framework programs.

ESPRIT

The largest expenditure under both the Second and Third Framework Programs was for the European Strategic Program for Research and Development in Information Technology (ESPRIT), with a total budget of EC and matching funds of 3.2 billion ECU for the period 1988-92. The main objectives of the program are to provide European information industries with the technologies they need to be competitive with the United States and Japan in the 1990s, to promote industrial cooperation in information technologies in Europe, and to assist in the standardsmaking process.³³ The first phase of the ESPRIT program began in 1984, with funding of 1.5 billion ECU. ESPRIT I's research projects concentrated on microelectronics; information processing services, including software technology and advanced information processing; and information technology applications, especially computer-integrated manufacturing and office systems. It included over 200 projects, more than 450 participating organizations, and approximately 3,000 researchers.³⁴ ESPRIT II, the second phase of this program, is an expanded version of the first phase and will focus on the same areas. An effort has been made to include small and medium-sized enterprises (SME's) in ESPRIT II projects. Of the 158 projects selected, 148 have SMEs participating.³⁵

RACE

The objective of the Research and Development in Advanced Communication Technology for Europe (RACE) program is to enable the EC to develop an integrated broadband communications (IBC) system based on integrated services digital networks (ISDN). Such a system would provide

high-speed transmission capabilities, flexibility in the choice of services and equipment, and a homogenous network serving all EC countries.³⁶ The definition or planning phase of the RACE program, budgeted at 40 million ECU, ended in 1987, and the next phase, which extends through 1991, has total funding of 1.1 billion ECU. During this phase, the program is focusing on the integration of technologies and systems, the verification and testing of concepts and systems, and pilot applications of future IBC services in key industries.³⁷ Applications will be developed in banking and finance, media and publishing, manufacturing, transportation, distribution, and health care. To accomplish this, 48 RACE projects were begun in 1988 and 40 more were initiated in 1989. Another important function of the RACE program is its role in setting standards; its goal is to develop standards for a European IBC network that will become the basis for subsequent competitive product development in the European communications industry.³⁸

BRITE/EURAM

A major portion of the EC's R&D in industrial technologies is carried out by two programs with combined funding of 1 billion ECU for the period 1989-92. The first program is Basic Research in Industrial Technologies for Europe (BRITE), which is devoted to the application of advanced technologies such as lasers, computerized design, and mathematical modeling in manufacturing industries. The second program is European Research on Advanced Materials (EURAM) which covers the field of materials technology. EURAM's objective is to develop the technology of materials and the capability to perfect and produce new materials.³⁹ Since both programs are working on manufacturing applications, especially in the automotive, aeronautics, construction, textiles, and chemical industries,⁴⁰ they were recently combined to enhance research efforts in related areas.

Nuclear Fusion

European activities in the area of nuclear fusion energy research are conducted principally through work in the Joint European Torus (JET) and the Next European Torus (NET). The Community's ultimate nuclear fusion objective, with EC funding of more than 700 million ECU, is the joint construction of prototype nuclear reactors and their industrial production and marketing.⁴¹ Much of the research in fusion and plasma physics is being carried out at an experimental fusion facility in the United

³⁶ RACE Project Office, "Integrated Broadband Communications in Europe," October 1986.

³⁷ Andre, *Research and Technological Development Policy*.

³⁸ Ibid.

³⁹ Ibid.

⁴⁰ "The E.C.'s Research and Technological Development," pp. 28-30.

⁴¹ Ibid.

³² Ibid.

³³ EC Commission, Directorate General XIII, *The Review of ESPRIT 1984-88*, May 1989.

³⁴ Michel Andre, *Research and Technological Development Policy*, EC Commission, 1988.

³⁵ *European Report*, No. 1425 (July 29, 1988), Internal Market, p. 10.

Kingdom. Related technologies being studied at the JRC include superconducting magnets, reactor materials, and tritium recovery systems.⁴²

Support Programs

In addition to the Framework research initiatives are the programs supporting Framework research by providing education of current and future researchers, disseminating research results, and creating infrastructures that facilitate technology transfer and the application of research results.⁴³ The three principal educational programs are European Action Scheme for the Mobility of University Students (ERASMUS); Community Action Programme in Education and Training for Technology (COMETT); and LINGUA, a program for the promotion of foreign language knowledge in the European Community. These programs stress mobility of people and information throughout the EC and the development of engineers and scientists with "European attitudes"⁴⁴.

Other support programs, such as the Strategic Programme for Innovation and Technology Transfer (SPRINT), are designed to promote new technologies. SPRINT's mission is to integrate national and European research and development efforts, to promote demonstration projects, and to establish cross-border, technology-oriented organizations to assist in technology transfer. There are a number of other programs that facilitate the dissemination of information or that seek to improve information delivery systems. Among these programs are the Inter-Institutional Integrated Services Information System (INSIS), Information Market Policy Actions (IMPACT), and Science and Technology for Regional Innovation and Development in Europe (STRIDE).

A summary of R&D programs within the EC Framework Program is presented in figure 2 at the end of this chapter.

Non-Framework Programs

Outside the Framework programs there are other cooperative R&D programs sponsored by confederations of European countries. The EC as a group and some or all of its individual member states belong to these organizations and participate in their projects. These programs range from pure basic research to commercial development; they may be narrow in scope or as broad as the Framework program. The EC and its members participate in projects in areas of pure basic research under the auspices of institutions such as European

Center for Nuclear Research, European Science Foundation, European Space Agency, and the Cooperation on Science and Technology, or in projects that are much closer to the market, such as those sponsored by the European Research Cooperation Agency. These European-based R&D programs are described briefly below.

European Research Cooperation Agency (EUREKA)

EUREKA was launched in July 1985 at the European Technology Conference. Initiated by France, the program is designed to facilitate increased industrial, technological, and scientific cooperation with the aim of developing products, processes, and services with global market potential.⁴⁵ EUREKA has 19 members, including the countries of the EC, EFTA, and Turkey, and is by far the largest non-framework R&D program in Europe. Its goal is to stimulate cross-border cooperation in order to heighten Europe's productivity and competitiveness in the world market.⁴⁶ It interacts with companies and research institutions in member countries and provides coordination for their efforts in the development of leading-edge technology. Special emphasis is placed on projects in the field of energy, medical technology, biotechnology, communications, information technology, transport, new materials, robotics and production automation, lasers, and the environment.⁴⁷

Although EUREKA is not an EC-controlled research program, the EC Commission and its member states are participants in EUREKA projects, which are often closely related to EC Framework research. However, there are major differences between EUREKA and the Framework. The Framework programs are limited to basic and prenormative⁴⁸ or precompetitive research, whereas EUREKA projects are more applications oriented. Another major difference is that EUREKA projects arise spontaneously from all technology fields rather than in response to a detailed plan. Framework research areas are defined in advance by Council directives, but EUREKA may be described as a 'bottom-up' initiative.⁴⁹ The project partners themselves decide what topics they wish to investigate, which groups they wish to form for the purposes of cooperation, how they wish to assign the work involved in the project, the contractual regulations governing the individual projects, and ownership of the results they desire to obtain.

⁴² Andre, *Research and Technological Development Policy*.

⁴³ EC Commission, *EC Research Funding*, January 1990, p. 3.

⁴⁴ EC Commission, *Proposal for a Council Decision Concerning the Framework Programme of Community Activities in the Field of Research and Technological Development (1990-1994)*, Aug. 2, 1989.

⁴⁵ EUREKA Annual Project Report, 1989.

⁴⁶ EUREKA Secretariat, *Together for the Future*.

⁴⁷ Ibid.

⁴⁸ Prenormative research is generally considered to mean that research done before, and leading to, the setting of a standard. A number of EC documents mention prenormative research leading to the setting of pan-European standards.

⁴⁹ William Street, "EUREKA Catalyzes Many Projects, Transforms European Research," *Physics Today*, March 1990.

Between the first conference at the ministerial level at Hannover in November 1985 and the Rome conference in June 1990, a total of 388 projects were announced with overall funding of more than 7.4 billion ECU.⁵⁰ Approximately 2,000 organizations, about two-thirds of which were private companies, have participated in EUREKA projects to date and the bulk of the funding has been from the private sector; public funding for EUREKA projects accounts for less than 10 percent of the cost of the projects.⁵¹

Two of the more important EUREKA projects are EUREKA-95, the development of a European standard for high-definition television (HDTV), and Joint European Semiconductor Silicon Initiative (JESSI), the development of processes and equipment to achieve integrated circuits with submicron line widths. Success in JESSI is hoped to lead to technological parity with Japan in the production of integrated circuits.⁵² A third program, PROMETHEUS, seeks to develop modern automobile traffic systems. The goals of this program are to increase traffic safety, lessen the impact on the environment, and increase efficiency and economy by using modern information technology for road transport purposes.⁵³

The Community wishes to strengthen its ties with EUREKA in a number of ways. The EC desires to establish a stronger interrelationship between the basic and precompetitive research of the Framework programs and the market-oriented research of EUREKA. The EC is also considering financing precompetitive EUREKA projects, mobilizing private financing and providing risk insurance for other EUREKA projects, and developing new possibilities for direct participation in EUREKA projects. Finally, both the EC and EUREKA have expressed the belief that their R&D efforts will benefit from the complete economic integration of the European Community and a reduction of barriers between the EC and the EFTA.⁵⁴

European Space Agency (ESA)

European efforts to cooperate in science and technology have resulted in the creation of a number of different organizations. One of these is ESA, which was created in 1975 to replace the European Space Research Organization (ESRO) and the European Space Vehicle Development Organization (ELDO). The agency is composed of 13 member states—Austria, Belgium, Denmark, West Germany, France, Ireland, Italy, the Netherlands, Norway, Spain, Sweden, Switzerland, and the United Kingdom, with Canada and Finland

⁵⁰ Rembser lecture and "Presentation of New EUREKA Projects," *European Report*, No. 1592, supplement (June 7, 1990), p. 1.

⁵¹ American Chemical Society, "The Effect of the European 1992 Plan on U.S. Science Policy."

⁵² *Electronic Business*, Mar. 5, 1990, p. 43.

⁵³ EUREKA Secretariat, *1989 Project Progress Report*.

⁵⁴ *EUREKA Annual Project Report, 1989*.

as associates. In 1989, this agency had a budget of about \$2 billion and a staff of 1,800.⁵⁵

The long-term objectives of ESA are to intensify and develop scientific activities, especially in areas such as remote sensing, space telecommunications, microgravity research, and space technology. ESA also seeks to promote European participation in the United States International Space Station and the Hermes space vehicle for manned missions to the Columbus/space station. Other technologies that the ESA plans to develop include a data relay satellite system (DRS) and ground infrastructures, especially for launching, control, communications, and astronaut training facilities.⁵⁶

European Science Foundation (ESF)

The ESF has developed numerous information networks throughout Europe on subjects in science and the humanities, and its membership includes 27 European governments and scientific institutions as well as the EUREKA Secretariat. However, because the ESF has a budget of only \$2.5 million annually it is unable to fund research projects. The ESF's principal activities are the initiation and coordination of European R&D projects in a wide variety of fields.⁵⁷ By the end of 1988, ESF projects included subjects ranging from volcanology to financial markets.⁵⁸ One of the more notable projects sponsored by the ESA is the European Synchrotron Radiation Facility, which is under construction in France. The funding for this project is a cooperative effort of 10 of ESA's members.

European Centre for Nuclear Research (CERN)

CERN, the European high-energy physics laboratory, located in Geneva, is a joint European venture that has given Europe world-class status in the field of particle physics. It has a permanent staff of 3,500 plus an additional 5,000 researchers from abroad and a budget of SwF 800 million.⁵⁹ Established in 1953, CERN currently has 14 members, with membership for Finland pending. Scientific groups from 20 countries of the world and researchers from about 300 universities and institutes participate in collaborative research at CERN. Because CERN has a number of exchange and cooperation agreements with European countries and institutions, it attracts a higher percentage of world-class scientists engaged in

⁵⁶ Rembser lecture.

⁵⁷ *Ibid.*, p. 14.

⁵⁸ Dean L. Mitchell, "The Evolution of Europe 1992," *European Science Notes Information Bulletin*, Office of Naval Research European Office, Publication No. 90-02, p. 4.

⁵⁹ Rembser, lecture, p. 12. Other ESF areas include longitudinal studies on individual development, earth science study centers, European communications and transport activities research, polar science, the history of European expansion, crystallography of biological macromolecules, molecular neurobiology of mental illness, surface crystallography, neural mechanisms of learning and memory, nonlinear systems, and demography and social change.

⁶⁰ *Ibid.*, p. 9a.

elementary particle research than any other comparable facility.⁶⁰

Cooperation on Science and Technology (COST)

COST⁶¹ is a broad forum for European scientific and technical cooperation that has been operative since 1971. The COST organization includes the EC and EFTA countries, Yugoslavia, and Turkey and provides a framework for specific projects in which all member countries are free to participate. A minimum of three countries is normally required to launch a project, but others may join within 6 months. Each country funds that portion of the research carried out within its borders, and the EC absorbs the coordinating costs. Under the COST program, more than 60 projects have been undertaken in areas such as computing, medical research, and social sciences.⁶² The European Centre for Medium Range Weather Forecasting at Reading, in the United Kingdom, was founded by COST in 1973 and now operates independently. The best examples of COST cooperation are found in telecommunications, transport, and materials.

Participation by Non-EC Members in EC Research and Development

Current Agreements

No institutional framework for U.S. participation in EC R&D projects exists currently, although there are agreements between the United States and the EC as well as between the United States and individual EC member states. There are 10 agreements between the EC and the United States outlining bilateral cooperation in specific R&D areas. In addition, there were 126 bilateral science and technology agreements between the individual EC states and the United States in 1988; 110 of these agreements were with France, West Germany, the United Kingdom, Italy, and Spain.⁶³ All U.S. agreements with the EC are in energy-related fields; agreements with individual countries include areas as diverse as the environment, material sciences, and agricultural sciences. In addition, a high-technology working group consisting of U.S. and EC representatives was formed in 1983 to monitor current and future developments in high-technology areas and to review potential areas for joint cooperation.

⁶⁰ *Ibid.*, p. 11.

⁶¹ *Cooperation Europeenne dans le Domaine de la Recherche Scientifique et Technique.*

⁶² Office for Official Publications of the European Communities, "Research and Technological Development Policy," p. 59. Other subjects of COST projects include telecommunications, transport, oceanography, materials, environment, meteorology, agriculture, biotechnology, and food technology.

⁶³ American Chemical Society, "The Effect of the European 1992 Plan on U.S. Science Policy." According to the report, there were 126 agreements with the individual EC countries and another 13 multilateral with ESA and the EC.

The need for greater science and technology cooperation between the United States and the EC was the main theme of the speech given by Mr. Filippo Maria Pandolfi, Vice President of the EC, in Washington before the U.S. National Academy of Sciences Forum, on March 5, 1990. He proposed five priority areas of possible cooperation:

- biotechnology,
- information technology,
- energy and environment,
- R&D in Eastern Europe, and
- large-scale scientific projects such as research on the human genome,⁶⁴ nuclear fusion, space stations, and high-energy physics.

A number of U.S. companies do participate in the various EC programs. U.S. organizations with EC research facilities that participated in ESPRIT I include Analog Devices; AT&T, through its European telecommunications joint venture with Philips; the Battelle Institute; Digital Equipment Corp.; IBM; and Foxboro.⁶⁵ Some participation by organizations located outside the EC has been permitted in the form of contracts, but this has been a small portion of the overall ESPRIT program.⁶⁶ Certain U.S. firms with a presence in the EC have had the opportunity to participate in other cooperative R&D programs. IBM, for example, has been designated as a prime contractor in JESSI. However no U.S. company, including IBM, which has extensive research facilities in the EC, has been appointed to the program-selection boards, or to the program advisory committees that control the direction of the major projects.

In addition, the EC and several individual EC states have agreements with EFTA, Eastern European countries, the Soviet Union, and Canada. Entities established or resident in the EFTA countries are eligible to participate in most R&D programs under agreements, either specific or general, signed by EFTA governments with the EC. Certain EFTA countries are directly associated with specific Framework programs as a result of signing an agreement with the EC, and organizations from those EFTA countries may participate in these programs under the same conditions as entities from the EC. If the EFTA country has only entered into a general agreement with the EC covering scientific and technological cooperation, organizations from that EFTA country may

⁶⁴ One haploid set of chromosomes with the genes they contain.

⁶⁵ Kenneth Flamm, "Semiconductors," in Hufbauer, p. 282.

⁶⁶ "All of the EC teams participating in ESPRIT projects are connected to each other by means of a data network, and are intended to have full access to university and industry research in a variety of fields." Congressional Research Service, *Europe 1992*, p. 100.

participate if the EC makes a specific decision to permit such participation in the particular project.⁶⁷ On June 19, 1989, the EC Council adopted a Framework agreement for scientific and technological cooperation with Iceland and similar agreements were concluded with Finland and Norway regarding protection of the environment. In 1990, agreements were signed with Austria, Finland, Norway, Sweden, and Switzerland to stimulate the international cooperation and interchange of European research scientists.

The growing importance, particularly for West Germany, of politically formalized cooperation projects with the Council for Mutual Economic Assistance countries is reflected in the increasing number of bilateral agreements on scientific cooperation. West Germany currently has treaties and agreements on scientific and technological cooperation with Bulgaria, Czechoslovakia, East Germany, Poland, Romania, the Soviet Union, and Hungary. In addition, Italy and the Soviet Union recently entered into a scientific cooperation agreement by which the University of Genoa and the Soviet State Committee for Science and Technology have set up a joint center for advanced research in biotechnology and bioelectronics on the island of Elba. A second area of scientific cooperation between Italy and Soviet Union is a project in fine chemicals.⁶⁸

Utilization and Dissemination of Results

The respective rights and obligations of participants in research consortia are set forth in annex II of the EC's model contract. The provisions covering rights of ownership, exploitation, and dissemination of results are governed by the following four basic principles:

- all intellectual-property rights resulting from the work of the project belong to the contractors, who are obliged to exploit the results and to reach agreement among themselves on such exploitation;
- the contract should promote wide dissemination of the project results for the purposes of research and technological development;
- dissemination of results for the purposes of exploitation and commercialization should be limited; and
- the obligation to make available the results to partners in other EC programs is complemented by the entitlement to receive the results from other projects or programs.

⁶⁷ EC Commission, *EC Research Funding*.

⁶⁸ U.S. Department of State Telegram, "Italy Technology Round Up, February 1990," March 1990, Rome, Message Reference No. 05485.

Certain rules also apply to dissemination of project results for research purposes. First, each participant in a contract must grant free licenses to the other partners in the same project, if it can be demonstrated that such licenses are necessary for the project to be executed and the results exploited. The EC Commission itself also reserves the right to use results freely for its own research purposes, e.g., for research it undertakes in the JRC. Second, upon request licenses must be granted for a fee to participants in other EC-sponsored R&D projects and programs, if the requesting party can guarantee that the results will not be used for other purposes. Finally, other companies in the EC can, for a fee, obtain licenses for R&D results in fields related to their own, provided this is in the interests of the EC and certain conditions are fulfilled. These conditions are (1) that the license is not against the business interests of those who developed it, (2) that guarantees can be obtained that the results will not be used for purposes other than that for which they were supplied, and (3) that contractors have not yet taken steps to exploit the results commercially.

The contracts are not intended to affect existing intellectual property rights. However, if existing rights are the basis upon which the research work is carried out, or the basis for processing new information by other contractual partners, participants in other program projects could obtain limited licenses for those protective rights, provided that no objections have been raised to the transfer. All contractors participating in a particular project have equivalent rights to the results of the project and each receives a free license to those results. Project contractors are also responsible for commercializing the results of projects. If a contractor is not a commercial organization and therefore is not able to utilize the results itself, its rights to the results can be transferred to the other partners in the project for appropriate remuneration.⁶⁹

Outlook

EC officials have stressed the openness of their research system, stating that "conditions for participating in EC research programmes are completely transparent and nondiscriminatory with respect to Community-based organizations with foreign parentage."⁷⁰ The EC Commission has stated that "every natural or legal person under public or private law who is resident or established in an EC member state" is eligible to participate.⁷¹ If they can comply with the rules that say, in essence, that the work is to be done in the Community, by two or more member firms that are not established in the same member state and that the work is to be exploited in Europe, they are treated exactly as

⁶⁹ EC Commission, *EC Research Funding*.

⁷⁰ *Ibid.*

⁷¹ *Ibid.*

firms with Community ownership.⁷² Both the Framework programs and EUREKA require non-EC companies to have what is called an "integrated presence" in Europe, which has been interpreted to mean that the company wishing to participate must engage in production, marketing, and research operations in the EC.⁷³

U.S. firms, however, have complained that they are relegated to a second-class role with respect to participation in EC programs because no U.S. firm has been appointed to the program-selection boards or to the program advisory committees, which control the direction of the major projects.⁷⁴ In response to this, EC officials point out that foreign company access to U.S. Federally funded programs is limited. They specifically mention that all foreign-owned companies are excluded from the

⁷² Filippo Maria Pandolfi, Vice President of the EC Commission, "Science and Technology and European Market Integration," Speech at U.S. National Academy of Sciences Forum, Washington, DC, Mar. 5, 1990.

⁷³ Congress, House, Committee on Science, Space and Technology, Statement by Dr. John H. Moore, Deputy Director, National Science Foundation, and Dr. Richard E. Bradshaw, International Analyst, National Science Foundation, *Europe 1992 and its Effects on U.S. Science, Technology and Competitiveness*, 101st Cong., 1st sess., May 16 and 17, 1989, p. 173.

⁷⁴ National Association of Manufacturers, *Update on EC-92* (draft), March 1990, p. 38.

Federally funded Sematech project and that participation in many U.S. defense research projects is limited to U.S.-owned firms.⁷⁵ According to EC sources, participation in EC research programs by firms in the EC with U.S. ownership or control currently is 1.5 percent, compared with only 0.18 percent of U.S. publicly funded R&D that goes to U.S. firms with foreign ownership.⁷⁶

As cooperative research grows within the EC, there are those who believe that one of the outcomes of EC 92 will be a greater inward focus of EC R&D. There is concern in the United States that research relationships established with the individual countries of the EC will decline and that new opportunities for cooperative R&D will be more difficult to develop. The EC emphasis on self-sufficiency has caused a decline in the percentage of scientists and engineers that is trained outside the EC. If the trend in scientific education carries over into research as well, there is concern that U.S. researchers may find fewer and fewer opportunities to work with European partners.⁷⁷

⁷⁵ Pandolfi speech.

⁷⁶ Ibid.

⁷⁷ Eric Bloch, Director, National Science Foundation, "Implications for R&D Intensive Industries Europe 1992: A U.S. Perspective," National Research Council Academy Forum, Mar. 5, 1990.

Figure 16-2
European Community research programs

Agriculture (Competitiveness of Agriculture and Management of Agricultural Resources)

EC funding: 1989-93 55 million ECU

To help EC farmers adapt to overproduction and restrictive prices and markets policy, to improve farming conditions in slowly developing regions, to encourage environmental protection and land conservation, to develop agricultural information services, and to improve the dissemination of research results.

AIM (Advanced Informatics in Medicine)

EC funding: 1988-90 20 million ECU

To develop information technologies for improving health care services and minimizing costs and delays; to contribute to the creation of an integrated health environment at Community level.

BCR (Community Bureau of Reference)

EC funding: 1988-92 59.2 million ECU

To improve measurements, chemical analyses, and testing R&D in applied metrology and chemical analysis.

BRIDGE (Biotechnology Research for Innovation, Development, and Growth in Europe)

EC funding: 1990-94 100 million ECU

To promote cross-border research for the purpose of speeding up the production of biological data, materials, and processes necessary for the optimal use of natural organisms; to establish Community regulations for biotechnology.

BRITE/EURAM (Basic Research in Industrial Technologies for Europe/European Research on Advanced Materials)

EC funding: 1989-92 499.5 million ECU

To strengthen the competitiveness of the European manufacturing industry, including small and medium-sized enterprises (SMEs), in world markets; to establish the necessary technological base for the development of new products and processes.

Decommissioning of Nuclear Installations

EC funding: 1989-93 31.5 million ECU

To develop a management system for dismantled nuclear installations and their radioactive wastes.

DELTA (Development of European Learning through Technological Advance)

EC funding: 1988-90 20 million ECU

To support R&D for emerging technologies to benefit teaching and learning.

DOSES (Development of Statistical Expert Systems)

EC funding: 1989-93 4 million ECU

To promote the use of advanced techniques for processing statistical data; in particular, the application of an expert system for the whole chain of statistical data processing.

DRIVE (Dedicated Road Infrastructure for Vehicle Safety in Europe)

EC funding: 1988-91 60 million ECU

To develop information technology to improve road-transport efficiency and safety and lessen the impact on the environment.

ECLAIR (European Collaborative Linkage of Agriculture and Industry through Research)

EC funding: 1988-93 80 million ECU

To promote European application of recent developments in life sciences and biotechnology.

Figure 16-2—Continued
European Community research programs

ESPRIT (European Strategic Program for Research and Development in Information Technologies)
EC funding: 1987-92 1,600 million ECU

To help provide the European information technology (IT) industry with a technology base needed to meet upcoming competitive requirements, to promote European industrial cooperation in IT, and to contribute to the development of internationally accepted standards. Phase II centers on microelectronics and peripherals, information-processing systems, and IT application technologies, with new emphasis on strengthening European capabilities in the areas of application-specific integrated circuits, high-performance parallel processing computers, new office work stations, and basic research actions.

EURET (Recherche dans le Transport en Europe)

EC funding: 1990-93 25 million ECU

To develop a Community transport system capable of responding to the increase in demand for all types of transport—both quantitatively and qualitatively—resulting from the completion of the internal market.

EUROTRA (European Translation Program)

EC funding: 1989-90 12.5 million ECU

To develop a machine translation system of advanced design capable of dealing with all official languages of the Community.

FAR (Fisheries and Aquaculture Research)

EC funding: 1988-92 30 million ECU

To promote interdisciplinary initiatives for rational and scientific research on resources; to develop aquaculture and new types of methods and procedures for exploiting little-researched resources.

FLAIR (Food Linked Agro-Industrial Research)

EC funding: 1989-93 25 million ECU

To contribute to Europe's competitiveness in the food industry, to the improvement of food safety and quality for the consumer, and to the strengthening of food science and technology.

Human Genome Analysis

EC funding: 1989-91 15 million ECU

To encourage development of advanced genetic technologies for human genome study, improving resolution of the human genetic map, and establishment of ordered clone libraries of human DNA.

JOULE (Joint Opportunities for Unconventional or Long-term Energy Supply)

EC funding: 1989-92 122 million ECU

To develop energy technologies that take account of new and renewable energy sources; to increase security of supply and reduce energy imports; to contribute to environmental protection.

Large-Scale Scientific Facilities

EC funding: 1989-92 30 million ECU

To optimize the use of large-scale scientific facilities and installations; to provide access to researchers who would not normally have such access.

MAST (Marine Science and Technology)

EC funding: 1987-92 50 million ECU

To improve knowledge of the marine environment; to promote new exploration technologies for the protection and exploitation of marine resources; to coordinate national R&D programs.

Figure 16-2—Continued
European Community research programs

Medical and Health Research

EC funding: 1987-91 65 million ECU

To increase the scientific and economic efficiency of medical research efforts through gradual coordination at the Community level and to optimize capacity and economic efficiency of health care efforts Communitywide.

MONITOR (Forecasting, Strategic Analysis, and Evaluation)

EC funding: 1989-93 22 million ECU

To help identify new directions and priorities in common research and technological development, to clarify relationships between R&D and other common policies, and for the improvement of R&D program evaluation. It comprises activities under SAST (Strategic Analysis in Science and Technology), FAST (Forecasting and Assessment in Science and Technology), and SPEAR (Support Program for Evaluation Activities in Research).

Nuclear Fusion

EC funding: 1988-92 551 million ECU

To establish the physical and technological bases necessary for the detailed planning of Next European Torus; in the field of physics and plasma engineering, this implies the full exploitation of Joint European Torus and several experimental fusion machines; to embark on the detailed design to NET.

RACE (Research and Development in Advanced Communication in Europe)

EC funding: 1987-92 550 million ECU

To develop the future communications infrastructure by combining the expertise of telecommunications researchers, manufacturers, administrations, and broadcasting stations across Europe.

Radiation Protection

EC funding: 1985-89 68 million ECU

To improve knowledge of human exposure to radiation and the effects of ionizing radiation on human beings and their environment; to develop countermeasures to master and reduce the risks; to provide a scientific basis for continued updating of the Basic Safety Standards for the health protection of the general public and workers against the dangers of ionizing radiation.

Radioactive Waste

EC funding: 1990-94 79.6 million ECU

To perfect and demonstrate the management and storage of radioactive waste, a system that will ensure the best possible protection of human beings and the environment.

Raw Materials and Recycling

EC funding: 1990-92 45 million ECU

To enhance the international competitive position of industries involved with raw materials and recycling, including primary raw materials, the recycling of nonferrous and strategic metals, forestry and wood products (FOREST), and the recycling of waste (REWARD).

SCIENCE (Stimulation des Cooperations Internationales et des Echanges Necessaires aux Chercheurs en Europe)

EC funding: 1988-92 167 million ECU

To improve the general quality of scientific and technical research and development; to promote training through research; to improve the mobility of researchers in Europe; to develop intra-European scientific and technical cooperation on high-quality projects; to promote the setting up of scientific cooperation networks.

SPES (Stimulation Plan for Economic Science)

EC funding: 1989-92 6 million ECU

To establish a cooperation and interchange network between top-level economists.

Figure 16-2—Continued
European Community research programs

STD (Science and Technology for Development)

EC funding: 1987-91 80 million ECU

The promotion of increased cooperation between the EC and developing countries to their mutual benefit, principally through tropical and subtropical agricultural programs, and the areas of medicine, health, and nutrition in tropical and subtropical areas.

STEP EPOCH (Science and Technology for Environmental Protection and European Programme on Climatology and Natural Hazards)

EC funding: 1989-92 75 million ECU (STEP), 40 million ECU (EPOCH)

To provide scientific and technical support for the environmental policy of the Community; to improve the productivity of the overall research effort in the Community by coordinating national programs in the field of environmental research; to promote the scientific and technical quality of environmental research.

TELEMAN (Remote Handling in Hazardous or Disordered Nuclear Environments)

EC funding: 1989-93 19 million ECU

To develop advanced remote-operated equipment for the nuclear industry; to establish a scientific and technological basis for the development of remote operating systems in all areas of the nuclear industry (mining, reactor operation, reprocessing, and decommissioning); to increase the safety of humans and installations; to improve waste management in environments that have changed unpredictably.

VALUE (Valorisation and Utilisation for Europe)

EC funding: 1989-93 38 million ECU

To ease and accelerate the circulation of information related to scientific and technical research to increase the efficiency of the research itself and to stimulate the process of innovation and industrial exploitation in Europe.

Source: EC Commission, *EC Research Funding*, January 1990, and EC Commission, *European Community Research Programmes*, December 1989.

CHAPTER 17
RECIPROCITY

CONTENTS

	<i>Page</i>
Developments covered in the previous reports	17-3
Background and anticipated changes	17-3
Possible effects	17-3
Developments covered in this report	17-4

CHAPTER 17 RECIPROCITY

The European Community's reciprocity policy has raised concerns that access to the single market could be unduly restricted in certain sectors for third-country firms. Reciprocity provisions have been incorporated in various 1992 measures, including directives that cover financial services, testing and certification, government procurement, merger control, and intellectual property. In general, reciprocity provisions effectively provide for conditional national treatment, making nondiscriminatory market access contingent upon how EC firms are treated in the third country concerned. The United States has continuing concerns about the European Community's reciprocity policy and is monitoring its interpretation and implementation.

Developments Covered in the Previous Reports

Background and Anticipated Changes

The EC's reciprocity policy was developed in the banking area and then extended to cover securities and insurance. It also has been incorporated in varying forms in other directives that deal with a range of subjects and it may be extended to cover additional areas. Depending on the particular context, the reciprocity policy criteria may preclude market access and national treatment altogether, or they may operate as a mechanism that would trigger negotiations with the third country concerned.

In the financial services sector, the policy has evolved from one based on "reciprocal treatment" to one based on "national treatment and effective market access." The original proposal for a Second Banking Directive, which was issued in February 1988, contained a reciprocity provision that would have made the market access of third-country banks to the single market dependent upon whether all EC banks received "reciprocal treatment" (however defined) in the third country concerned.

One of the basic difficulties was that it was not at all clear what the EC meant by "reciprocal treatment." Reciprocity could be interpreted in many ways, and it could have different meanings and implications depending on the specific context. The most restrictive form of reciprocity is mirror-image reciprocity, which could require identical treatment in the third country. Under this interpretation, the EC might expect to receive better than national treatment in a third country. Other formulations of reciprocity include sectoral reciprocity, overall reciprocity (which is a standard that appears in the GATT), or reciprocal national treatment.

The United States was concerned about the original banking proposal because the EC might have determined that EC banks do not receive "reciprocal treatment" in the United States due to the fact that the United States legally separates commercial and investment banking and legally restricts interstate banking, whereas the 1992 program allows universal and interstate banking. Therefore, U.S. firms could be restricted from competing on an equal and nondiscriminatory basis in the single market, even though the United States generally offers unconditional national treatment.

In addition, concerns arose that, notwithstanding the rights conferred by article 58 of the Treaty of Rome, reciprocity may be applied to restrict U.S. subsidiaries that are already authorized and operating in the EC market, and, moreover, that it may be applied when such subsidiaries undertake a corporate restructuring, engage in new activities, or make an acquisition. U.S. firms were also concerned that reciprocity might be applied retroactively.

Most of these concerns were largely resolved with the adoption of the Second Banking Directive in December 1989. The approach taken in the final directive as adopted is that access to the single market will be contingent on whether EC banks receive "national treatment and effective market access" in the third country concerned. Under this policy, the EC will be looking to see that EC banks receive genuine national treatment that really works in practice (i.e., *de jure* and *de facto* national treatment). If the EC determines that the third country does not provide genuine national treatment to EC banks, then requests for banking licenses from banks of the third country would be suspended pending negotiations. Since the United States provides genuine, unconditional national treatment to EC banks in the United States (although some State banking laws may adversely affect foreign banks), it is not likely that U.S. banks would be subject to the suspension procedure.

However, even if a third country is found to provide genuine national treatment, the EC may seek negotiations in order to obtain treatment for EC banks in the third country "comparable to that granted by the Community to credit institutions from that third country." It is under this latter procedure that the EC could seek to negotiate with the United States. The negotiations would seek to obtain "comparable competitive opportunities" (however defined) for EC banks in the United States, which could include the right to sell a wide range of banking services throughout the United States on the basis of a single authorization. Such negotiations may be difficult because U.S. banking laws generally limit interstate banking and separate commercial and investment banking.

Possible Effects

The United States maintains that the Community's reciprocity policy is inconsistent with

the Community's international obligations and may undermine multilateral trade liberalization. The EC reciprocity policy makes market access and national treatment in the single market conditional on the treatment of EC firms in the United States. In each area where a 1992 directive contains a reciprocity provision, there is a potential risk that U.S. firms will not benefit from unconditional national treatment and will not be able to compete on an equal and nondiscriminatory basis.

Developments Covered in This Report

Any new development regarding the Community's reciprocity policy in a particular area is examined in the chapter of this report in which the underlying directive is examined.

CHAPTER 18
RULES OF ORIGIN AND LOCAL-CONTENT REQUIREMENTS

CONTENTS

	<i>Page</i>
Developments covered in previous reports	18-3
Background	18-3
Anticipated changes	18-3
Possible effects	18-3
Developments since the first followup report	18-3
Background and anticipated changes	18-3
Possible effects	18-4

CHAPTER 18

RULES OF ORIGIN AND LOCAL-CONTENT REQUIREMENTS

Rules of origin, and the supplementary local-content rules the EC often utilizes, were not included in the many directives designed to complete the single market. However, because their terms and interpretation affect the application of many measures relating to international trade, origin standards have frequently been involved in analyses of post-1992 prospects for U.S. business in and exports to the EC.

Developments Covered in Previous Reports

Rules of origin are employed to determine the source of goods that are not wholly grown, produced, or manufactured in one country (from components or materials of that country). Such a finding is needed for several purposes—the assessment of the correct duty rate, the administration of country-specific measures, the enforcement of “buy national” restrictions, and the accumulation of accurate statistics. It is often in the second of these areas that U.S. and other third-country exporters have alleged EC discrimination against foreign goods. In addition, foreign exporters have asserted that EC measures are intended to compel investment or sourcing within the EC, to the disadvantage of foreign producers and even of their EC-based affiliates.

Background

The EC's nonpreferential origin rule, set forth in a 1968 regulation, may be described as assigning origin to the country of “last substantial, economically justified processing.” For purposes of implementing preferential agreements and of applying antidumping duties, quantitative restrictions, or other measures, separate regulations have been adopted to cover individual countries or products. When a regulation sets the basis for determining the origin of a product category, to prevent circumvention of antidumping orders or for another single or country-specific purpose, the measure becomes the customs rule of origin for these goods and controls the treatment of such goods from all sources. Other supplementary measures, relying on specific content criteria or the change-of-tariff-heading principle, have been adopted to ensure uniform origin treatment when the basic origin rule is deemed insufficient.

Anticipated Changes

At present, no substantive changes in the EC's origin rules or local-content standards have been

proposed. Existing anticircumvention provisions seem likely to continue in force, despite the recent decision by a GATT panel in a case brought by Japan in 1988 (discussed below).

Possible Effects

Because origin rules are arcane and often complex, and because they are included in or used to give effect to many trade policy measures, it can be difficult to identify their impact on trade and investment. Recent EC actions have also given rise to the belief that the principle of “most substantial processing” is replacing “last substantial processing” as the basis for some origin findings. The confusion is exacerbated by the lack of transparency in the development of the rules, and by the use of supplemental standards such as “negative rules” and content minimums or maximums.

In addition, as noted above, implicit or formal origin criteria may be contained in anticircumvention measures in dumping cases and in unpublished undertakings between the EC and target countries. When an anticircumvention action by the EC results in a regulation on the origin of the class of merchandise covered by a dumping finding, that origin standard becomes the basic customs rule of origin for such merchandise and controls in all other areas where origin is relevant (such as government procurement). Firms and governments outside the EC have frequently asserted that such rules are intended to compel investment in EC productive capacity or sourcing from EC producers, thereby displacing foreign production of components or finished goods. Foreign firms (especially Japanese companies) have been relocating to the EC to ensure that their output is deemed to have “EC origin.” The U.S. Government has on several occasions indicated its concern about procedures for adopting and administering the EC rules and their effect on investment decisions.

Developments Since the First Followup Report

Background and Anticipated Changes

There have been two notable developments relating to origin rules during the last few months. In addition, it is reported that some changes in the application of previous undertakings have occurred, apparently designed to avoid some adverse effects on U.S.-based components suppliers (although all of the problems faced by U.S. producers of some goods, such as printed circuit board assemblies, have not yet been remedied).¹

¹ These changes reportedly involve the method of computing value content for purposes of achieving the required level of nontargeted value in goods subject to antidumping orders—largely to avoid a “loss of origin” for certain components and assemblies supplied by U.S. firms.

The first development was the issuance of the EC Commission's proposed Common Customs Code for the Community, discussed in more detail in chapter 7 of this report. If adopted, the code will restate previously adopted legal principles for determining origin for nonpreferential purposes and, in general terms only, for preferential arrangements negotiated by the EC. Article 23 of the draft code would assign origin of goods wholly obtained or produced in one country to that country. It would also provide that—

Goods whose production involved more than one country shall be deemed to originate in the country where they underwent their last, substantial, economically justified processing or working in an undertaking equipped for that purpose and resulting in the manufacture of a new product or representing an important state of manufacture.

Concerning circumvention of any trade-related policy, article 25 would provide that—

Any processing or working in respect of which it is established, or in respect of which the facts as ascertained justify the presumption, that its sole object was to circumvent the provisions applicable in the Community or the Member States to goods from specific countries shall under no circumstances be deemed to confer on the goods thus produced the origin of the country where it is carried out within the meaning of Article 23(2) [set forth above].

The code would neither contain nor preclude additional regulations specifying how individual classes or kinds of merchandise are to be treated for origin purposes. It would appear, therefore, that outstanding and future measures on specific products are permissible under the above language.

The second development occurred subsequent to the drafting of the code and may eventually require revision of its provisions. The EC decided to allow adoption of the report of the GATT panel in the case brought by Japan challenging current anticircumvention measures. Information made available to date about the yet-to-be-published report indicates that the panel found certain rules applied by the EC against Japan invalid under the terms of article III (national treatment) and outside the exception provided for in article XX(d) (customs enforcement measures, etc.). No action to change existing regulations (or undertakings with targeted exporting countries that were reached to resolve prior complaints of circumvention) has yet been

taken or proposed by the EC, and to date the implications of the ruling are unclear.

Assuming successful conclusion of current negotiations in the Uruguay Round of multilateral talks, EC measures—and those of many countries—would need to be reviewed or redrafted with a view toward internationally agreed principles and procedures governing origin rules. Without a further agreement on a harmonized rule of origin, however, exporters to the EC are still faced with difficulties in challenging origin determinations asserted to have discriminatory effects.

Possible Effects

Because of the recent panel ruling, and with the Uruguay Round talks not yet concluded, it seems premature to predict any effects on U.S. exports to or U.S. business operating conditions in the EC.² If recent trends continue, one result may be a loss of U.S. jobs as production for the EC market is moved from this country to the EC. Another may be a loss of competitive position for firms that continue to produce domestically those goods they wish to sell in the EC or to third-country suppliers to the EC. The U.S. Government has repeatedly expressed its concerns and those of U.S. manufacturers, but the EC has not yet implemented changes to substantiate official EC statements that no policy of compelled EC-based production exists.

² For example, the broadcast directive (discussed in ch. 21 of this report and in U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States—First Follow-up Report* (Investigation No. 332-267), USITC Publication 2268, March 1990, ch. 6) has given rise to considerable opposition and to concerns about its legality under the GATT. The directive would require a majority of broadcast programming to be of European origin, would regulate advertising and sponsorship, and would attempt to achieve further protection of minors. Although the U.S. Government, the motion picture and television industries, and private organizations have criticized the proposal (with the official position that the measure would be a damaging precedent and represents GATT-illegal protectionism in the form of a local-content criterion), the EC response has been that (1) GATT regulates goods, not services such as broadcasting, and (2) the U.S. industry, which is protected from foreign competition by law and other means, would actually obtain greater opportunities to market their products (because the directive would raise the current "quota" of 14 percent on U.S. broadcast television in the United Kingdom and the EC-wide limit of 23 percent on all non-European programming). For a discussion suggesting that the end result may actually be higher U.S. exports to the EC, see Fred H. Cate, "The First Amendment and the International 'Free Flow' of Information," *Virginia J. of Int. Law* vol. 30 (1990), p. 371 (discussion of directive begins at p. 402). The author notes that in this country foreign ownership of broadcast outlets is prohibited, imports amount to less than 2 percent of programming, and certain advertising is regulated or barred.

PART V
ANTICIPATED CHANGES IN THE EC AND
POTENTIAL EFFECTS ON CERTAIN U.S. INDUSTRIES

CHAPTER 19
INDUSTRY AND COMPANY ACTION AND REACTION

CONTENTS

	<i>Page</i>
Introduction	19-3
Industry and company response	19-3
Historical patterns of EC involvement	19-3
Relative importance of the EC market	19-4
Scale economies	19-4
Existence of market niches	19-4
Automobiles	19-4
Chemicals and pharmaceuticals	19-4
Telecommunications	19-5
Other sectors	19-5
Large vs. small company response	19-5
Small and medium-sized enterprises in the United States	19-6
Small and medium-sized enterprises in the EC	19-6
Government policy in the United States and the EC	19-7
SME involvement in international markets	19-8
Small business economics	19-9
Impact of EC 92 on large and small companies	19-10
 Tables	
19-1. Relative activity of small firms in the most innovative U.S. industries, 1982	19-7
19-2. Small and medium-sized firms' share of value of exports to Western Europe, by industry, 1985, in percent	19-9

CHAPTER 19

INDUSTRY AND COMPANY ACTION AND REACTION

Introduction

The performance of a particular industry in gearing up for 1992 is usually measured in terms of the strategies undertaken by a relatively small number of large U.S. companies. The substantial resources of these multinational firms and their long-standing commitment to a European market presence—in some instances predating the signing of the Treaty of Rome in 1957—frequently allow them to implement a pan-European corporate strategy designed to ensure strong sales and earnings in an integrated EC market. Even among U.S.-based multinationals, however, the road to market success in the EC has not always been an easy one. Resurgent European demand and regulatory harmonization do not in themselves ensure success for leading U.S. companies.

Small and medium-sized enterprises (SMEs), which employ fewer than 500 people,¹ confront additional size-related problems that can hinder the ability of U.S. firms to monitor the EC 92 program and take the strategic steps necessary to gain or maintain a foothold in the European market. Although new ideas concerning the impact of firm size on international competitiveness have prompted many smaller U.S. firms to reevaluate their prospects for success in overseas markets, small size and limited company resources have usually restricted the range of options open to these firms.

While the issue of small business participation in the integrated EC market may at first glance appear to be of secondary importance given the historic predominance of U.S. multinationals in the Community, the large number of small and medium-sized firms in the United States and the growing impact that these companies have had in the area of new job creation over the past decade suggest otherwise. Especially in advanced technology sectors like computer software and biotechnology, younger and smaller firms have shown considerable skill in boosting EC sales—either through exports, joint ventures, or manufacturing independently in the Community.

It is the purpose of this chapter to address the related questions of intraindustry variation in response to EC 92 and the role of firm size in determining company action and competitiveness.

Industry And Company Response

In each of the three sectors analyzed in the subsequent chapters—automobiles, chemicals/

¹ Unless otherwise noted, SMEs will be defined throughout this chapter as firms employing fewer than 500 people.

pharmaceuticals, and telecommunications— involvement by U.S.-based firms in the EC market is restricted almost entirely to a small number of relatively large firms. Productive efficiency in auto and chemical production, as well as the provision of telecommunications services, is still determined to a large extent by the existence of economies of scale. This fact has limited the number of market participants.

However, it is clear that even in the industries where large firms are dominant, large size alone is not sufficient to guarantee an EC presence. Market power in the United States does not translate automatically into European success. Large firms such as Chrysler, which failed to make the commitment to Europe that its U.S. rivals did, and AT&T, which has run up against sizable barriers in competing for EC business, have experienced difficulties in Europe highlighting the problems associated with the assumption that large, well-known U.S. corporations are destined to succeed in the EC single market.

The pattern of company response within an industry to the opportunities presented by the EC single market depends heavily on the dynamics of the industry that is being analyzed. First, in industries where large companies predominate, historical patterns of company involvement in Europe and the presence of scale economies are critical in determining company response. Second, in those sectors where barriers to entry are low and where niche marketing opportunities exist (many of the advanced technology sectors), small and middle-market firms can compete more effectively. The distinction between these two types of industries should be kept in mind when examining the degree of variation in company response within a particular sector. Listed below are some of the factors that determine the level of intraindustry variation in company response to EC 92.

Historical Patterns of EC Involvement

Many U.S. multinationals began to set their sights on the European Community and the potential benefits of a unified market as early as the late 1950s after the signing of the Treaty of Rome.² While lingering nontariff barriers to trade kept these firms from reaping the rewards that they originally envisioned, early entry into the EC goes a long way toward explaining why companies like Ford and IBM continue to prosper in Europe today. One should not assume, however, that long-standing commitments to the European market put U.S. multinationals in a position to move toward a truly pan-European strategy without complications. As a general rule, large U.S. companies have kept national subsidiaries within the EC autonomous—regarding Europe as twelve separate markets. Major corporations like

² John F. Magee, "1992: Moves Americans Must Make," *Harvard Business Review*, May/June 1989, vol. 67, No. 3, p. 81. Magee focuses on the problems faced by U.S.-based multinationals in preparing for the single market.

Coca-Cola and Colgate-Palmolive have only recently established integrated EC management organizations to coordinate pan-European operations.³

Relative Importance of the EC Market

The existence of a strong and growing European market has served as a magnet for many large firms possessing the resources to undertake multinational production and marketing. This is particularly true in the current context, with the EC capital investment boom sparked by the single-market initiative well underway.⁴ Even within the large U.S. market, big firms may find their sales reaching a theoretical ceiling. For small and medium-sized firms, however, this point may be much more difficult to determine, and the urge to produce only for the domestic market may prove too powerful to resist.⁵

Scale Economies

In order to exploit economies of scale in industries like automobile and chemical production, huge capital investments are required to set up manufacturing and distribution facilities. This sharply limits the ability of newcomers to challenge leading market players. For companies seeking quick entry in scale-sensitive industries, mergers and acquisitions often become the preferred investment vehicle. Smithkline Beckman's merger with Beecham of the United Kingdom in pharmaceuticals reflects this strategy.

Existence of Market Niches

Opportunities for up-and-coming small and medium-sized firms producing customized goods and services exist in many emerging technology sectors. In these areas established market power may prove to be more of a liability than an asset. Quick response to changing market conditions or EC regulations may allow new players to challenge the established large companies.⁶

Patterns of company response and intraindustry variation for particular sectors are outlined in the following paragraphs.

³ Booz-Allen and Hamilton, Inc., *Europe 1992: Threat or Opportunity?*, special report, 1989. This report points out the slowness with which some large U.S. firms have responded to EC 92. Only 30 percent of Fortune 500 executives interviewed said their firms had implemented a full-fledged European business plan at the time of the survey.

⁴ Stephen Cooney, "Europe 1992: The Opportunity and the Challenge for U.S. Economic Interests," *SAIS Review*, Winter/Spring 1990, p. 78. Cooney points out the impact that the capital goods investment boom will have on U.S. manufacturers.

⁵ Congress, House Committee on Small Business, *Small Business and International Trade*, testimony of John C. Rennie, President, Pacer Systems, Inc., Sept. 21, 1988, p. 2.

⁶ Tom Peters, "New Products, New Markets, New Competition, New Thinking," *Economist*, Mar. 4, 1989, p. 21.

Automobiles

Among the big three U.S. auto producers, both Ford and General Motors have capitalized on well-established manufacturing and distribution networks in Western Europe to capture substantial shares of the EC market. With 22 manufacturing facilities in Europe, Ford presently controls about 12 percent of the EC passenger car market. GM, which has invested in 25 European assembly and parts plants, follows closely with an 11-percent share.⁷

Both firms have posted strong earnings performances in Europe over the past few years, offsetting declining U.S. sales. While Ford and GM have demonstrated a long-standing commitment to EC production and the self-sufficiency of their European subsidiaries, Chrysler has continued to concentrate on the U.S. market at the expense of European operations.

Chemicals and Pharmaceuticals

The EC has traditionally been a major source of revenue—both through exports and European operations—for the largest U.S. chemicals and pharmaceuticals producers. Total chemical exports from the United States topped \$36 billion in 1989, representing almost 16 percent of total industry shipments.⁸ Exports to EC markets amounted to over \$9.7 billion—more than 10 percent of all U.S. exports to the Community.⁹ The high degree of dependence on exports to the EC has prompted major U.S. producers to weigh the effects of the single-market program carefully. At the present time, a relatively small group of companies—led by Du Pont, Dow, and Exxon—expect to benefit from standards harmonization, rationalization of marketing and opportunities for greater capital investment in the EC. Given the long-standing importance of the European chemicals market, the chances of a major U.S. producer being left behind in responding to EC 92 would appear slim.

Similarly, U.S. production of pharmaceuticals for the EC market tends to be dominated by a relatively small number of well-capitalized firms, such as Merck and Bristol-Myers Squibb. These firms are capable of sustaining large R&D budgets. A wave of mergers in recent years has accelerated the trend toward industry concentration.¹⁰ Among the major U.S. pharmaceutical producers, many have taken steps toward greater investment in the EC, or have linked up with European partners—as Smithkline Beckman has done with Beecham of the United Kingdom. Direct investment by U.S. pharmaceutical firms in the EC totaled \$14 billion in 1986.¹¹

⁷ EC Commission, "Panorama of EC Industry," p. 14-5.

⁸ Compiled from official statistics of the U.S. Department of Commerce. For more details, see the chapter entitled "Chemicals and Pharmaceuticals Sector" in this report.

⁹ *Ibid.*

¹⁰ Jane Docherty and Katrina Labaere, "The Pharmaceutical Industry: Preparing for the Nineties," *EC Bulletin*, No. 84, September/October 1989, p. 13.

¹¹ U.S. Department of Commerce, Bureau of Economic Analysis, *U.S. Direct Investment Abroad*, June 1988.

Telecommunications

Although the telecommunications equipment industry does not exhibit the same degree of concentration as the automobile sector, a relatively small number of companies dominate both the U.S. and EC markets. Among the more than 2,000 U.S. producers of telecommunications equipment, sales by the 37 leading firms reached \$159 billion in 1989—accounting for approximately 80 percent of the U.S. market.¹²

Unlike U.S. automobile and chemical producers, telecommunications firms are only beginning to participate in overseas markets, due in large part to the arcane character of government procurement practices and the historic predominance of national telephone monopolies. Within the EC, this phenomenon has been especially troublesome for U.S. firms, which seek to gain ground in a European market expected to grow rapidly in the coming years. The EC represents the largest overseas market for U.S.-produced telecommunications equipment. U.S. company receipts for international telecommunications services amounted to only about \$3 billion in 1989, compared with domestic services revenues of about \$168 billion.

Other Sectors

In many of the nontelecommunications services and high-technology sectors, barriers to entry into the EC market associated with the need for large-scale production and distribution are much less imposing than in the three manufacturing sectors studied in this report. Indeed, while large U.S. multinationals in areas like banking and insurance will undoubtedly lead the way in developing an EC-wide presence, small and middle-market players cannot be ignored entirely in less scale-sensitive sectors like accounting, management consulting, and architectural services.¹³

In advanced technology sectors like biotechnology, optics, advanced materials, and scientific instruments, market power in the EC is much more diffuse. A significant trend in these industries has been the tendency for younger, smaller firms to begin exporting and setting up international distribution through joint ventures very early in the product life cycle. In this way, competitiveness can be established quickly on an international scale. The existence of market segments that large companies are simply not willing to exploit allows younger firms to boost international sales. As officials of a New England-based manufacturer of biodetection systems pointed out in conversations with USITC staff, opportunities for entry into the EC through

niche product marketing became evident soon after the company was founded in the mid-1980s.¹⁴

A recent survey of young high-technology firms conducted by the Bank of Boston reflects the strong inclination of these companies to sell their products overseas. Fully 82 percent of scientific testing and measurement equipment firms started since 1979, for example, were exporting their product by 1988. At the same time, 86 percent of optics equipment manufacturers were selling overseas—strong evidence of the leading role that technology, rather than market power, plays in the more dynamic emerging technology sectors.¹⁵

Large vs. Small Company Response

Opportunities for competitive success in the European Community on the part of small and medium-size enterprises (SMEs) exist and, in certain sectors, are expanding. Whether through the traditional method of exports, or through increasingly popular joint ventures, cross-licensing arrangements, or independent manufacturing in the EC, even the smallest U.S. firms can find a suitable way of breaking into the European market. On the surface at least, the most critical barriers to greater SME involvement in the EC and other international markets would appear to be psychological.¹⁶ SMEs in the United States have frequently expressed skepticism about venturing into new markets thousands of miles away when the U.S. market provides ample opportunity for growth.

In addition to the psychological obstacles, a number of size-related problems continue to hamper smaller firms in their effort to tackle international markets. A lack of good market information, doubts about the reliability of agents overseas, and an inadequate access to risk capital or trade financing all contribute to the small business owner's sense of apprehension concerning expansion overseas.¹⁷

Large firms possess a clear advantage in monitoring the EC 92 initiative and preparing for the single market. Despite the availability of numerous government and private reports on EC 92, and the existence of special U.S. Government programs to put smaller U.S. firms in touch with distributors and possible joint venture partners in the EC, SMEs often find it difficult to get precise information about how the single-market program will affect the marketing of their product.

¹⁴ Interview with USITC staff, May 1990.

¹⁵ Congress, House Committee on Small Business, *Small Business and International Trade*, testimony of James M. Howell, Chief Economist, Bank of Boston, Sept. 19, 1988, p. 12.

¹⁶ Congress, House Committee on Small Business, Subcommittee on Exports, testimony of Susan Engeleiter, Administrator, U.S. Small Business Administration, Sept. 12, 1989, p. 11.

¹⁷ For a discussion of this issue, see the section entitled "SME Involvement in International Markets," in this chapter of the report.

¹² "U.S. Companies Ranked by Industry," *Business Week*, Apr. 13, 1990, p. 242. Detailed industry statistics are provided in the chapter entitled "Telecommunications" in this report.

¹³ Magee, "1992: Moves Americans Must Make," p. 80.

Multinational corporations, on the other hand, are able to monitor the single-market initiative on a daily basis, making measured judgments about the impact of economic integration on the manufacturing and marketing of their product line.

However, psychological and structural barriers related to size cannot in themselves negate the effects that technology and a reexamination of the relationship between firm size and efficiency have had on SME involvement in the world economy. The share of jobs created by SMEs in the United States and in the EC is large and growing. In short, many of the old ideas regarding firm size and competitiveness – namely, the notion that “bigger is better” – have been discarded as irrelevant in the present context. U.S. Government policy, moreover, has been aimed at the expansion of SMEs’ role in overseas markets. Together, these factors help explain the need for a closer examination of the effects of European economic integration on small and medium-sized enterprises in the United States.

Small and Medium-Sized Enterprises in the United States

Of the approximately 4 million registered companies in the United States with more than one employee, all but about 10,000 (or 99.75 percent) employ fewer than 500 people, and therefore fall within the official U.S. Government definition of a small business.¹⁸ Although precise figures are not available, these firms have reportedly provided jobs for about half of the U.S. workforce in recent years, and their share of the U.S. GNP approaches one-third.¹⁹

SMEs have clearly played a leading role in creating new jobs over the past decade. According to a recently completed study comparing the impact of SMEs in the United States and West Germany on new job creation, 65.4 percent of new jobs created in the U.S. economy between 1976 and 1982 came from firms employing fewer than 500 people.²⁰ The lion’s share of new jobs created by small firms in recent years appears to be concentrated in the manufacturing sector. During the 1976-82 period, 95.3 percent of all new jobs in manufacturing were added by SMEs.²¹

According to a recent U.S. Small Business Administration (SBA) study, small firms in the U.S. manufacturing sector were responsible for creating

¹⁸ Criteria for defining a small business in the United States are outlined in the *Small Business Act* (July 18, 1958), 15 U.S.C. 632, Public Law 85-536, 72 Stat. 384, as amended.

¹⁹ William A. Brock and David S. Evans, “Small Business Economics,” *Small Business Economics*, vol. 1, January 1989, p. 7. In 1984, firms employing 500 people or fewer accounted for 52.9 percent of total U.S. employment. Companies employing less than 100 workers contributed 38.9 percent of U.S. jobs.

²⁰ Zoltan J. Acs and David B. Audretsch, “Job Creation and Firm Size in the U.S. and West Germany,” *International Small Business Journal*, vol. 7, No. 4, Fall 1988, p. 11. The data also showed that firms employing fewer than 100 accounted for 48.18 percent of new jobs created in the period.

²¹ *Ibid.*, p. 12.

1.2 million jobs between 1976 and 1984.²² During the same period, approximately 300,000 jobs were lost in large manufacturing firms. In the view of SBA economists, this surge in small business job creation was due in large part to the availability of new technology in manufacturing. Recent evidence also suggests that small manufacturers are showing much greater durability in the first years of their existence. New estimates of small firm failure rates among recently founded companies indicate that only three out of five firms – compared with four out of five in many earlier surveys – fail in the first 5 years of existence.²³

With regard to innovation, SMEs in the United States appear to be making their mark in key high-technology industries. Figures compiled in the early 1980s indicate that within emerging technology sectors where the number of innovations per employee is highest, small firms tend to contribute significantly to overall employment – an indication of the innovative capacity of SMEs (see table 19-1).²⁴

The large contribution of SMEs to overall employment in such innovative sectors as process control instruments, engineering/scientific equipment, and surface active agents is a clear indication of the leading role that smaller firms are playing in some of the most competitive advanced technology sectors.

Small and Medium-Sized Enterprises in the EC

It is significant to note that SMEs make up more than 90 percent of all businesses in the European Community, bearing in mind the more restrictive official EC definition of an SME (i.e. – a firm with fewer than 100 employees).²⁵ The share of total employment contributed by SMEs varies widely between the EC member states. While SME employment as a percentage of overall employment lies at or below 20 percent in West Germany, Luxembourg, and the United Kingdom, the figure falls between 30 and 45 percent for Belgium, the Netherlands, Denmark, Spain, Portugal, Ireland, and France; the share tops 50 percent in Greece and Italy.²⁶

²² Edward Starr, “The Growth of Small Manufacturers: 1976-84,” *Business America*, April 1988, p. 41.

²³ Bruce D. Phillips and Bruce A. Kirchhoff, “Formation, Growth and Survival: Small Firm Dynamics in the U.S. Economy,” *Small Business Economics*, vol. 1, Jan. 1989, p. 65.

²⁴ Acs and Audretsch, “Job Creation and Firm Size in the United States and West Germany,” p. 16. Also see Zoltan J. Acs and David B. Audretsch, “Innovation in Large and Small Firms: An Empirical Analysis,” *American Economic Review*, September 1988.

²⁵ *Official Journal of the European Communities (OJ)*, No. C 56 (Mar. 7, 1990), p. 65.

²⁶ *Employment in Europe, 1989*, EC Directorate General for Employment, Industrial Relations and Social Affairs, Com (89) 399, 1989, p. 81.

Table 19-1

Relative activity of small firms in the most innovative U.S. industries, 1982

employment, Industry	Innovations per thousand	SME share of industry
	employees	In percent
Process control instruments	3,548	46.5
Scales and balances	3,521	61.9
Engineering and scientific equipment	2,979	53.0
Medicinals and botanicals	2,222	8.9
Electronic computers	2,050	3.7
Surface active agents	1,818	66.2
Office machines	1,816	10.3
Measuring and controlling devices	1,610	39.1
Agricultural chemicals	1,600	33.0
Surgical and medical instruments	1,528	29.9

Source: Acs and Audretsch, "Job Creation and Firm Size in the U.S. and West Germany", *International Small Business Journal*, vol. 7, No. 4, 1988, p. 16. SMEs are defined here as firms employing fewer than 500 people.

The share of SME employment is growing in all member states except the Netherlands, where the figure has been essentially constant in recent years, and in Greece, where small business employment is actually declining in relative terms.²⁷ The role of smaller firms is greater in the service economy than in manufacturing. With the exception of the United Kingdom, no EC country has seen substantial growth in the contribution of SMEs to manufacturing employment.²⁸ Overall, SMEs provide about half of all jobs in the EC services sector.

As in the United States, SMEs in the European Community have been creating jobs at the expense of employment in larger firms.²⁹ In recent years, job creation has been concentrated in firms with fewer than 20 employees—particularly in the United Kingdom, France, and West Germany.

Government Policy in the United States and the EC

U.S. Government policies to help SMEs develop a European market strategy have been coordinated by the U.S. Department of Commerce (Commerce) and the SBA. In recent congressional testimony, Deputy Assistant Secretary of Commerce Franklin Vargo described a three-tiered U.S. Government plan to help smaller firms gear up for 1992.³¹ First, by keeping small companies informed about the changes taking place in Europe, U.S. officials hope to spur interest in developing a European strategy. Second, through special problem-solving services, specific issues of concern such as standards and testing requirements can be raised with EC officials. Third, through an elaborate marketing program, U.S. companies can learn more about potential

partners who can help sell their products in Europe. With regard to the last goal, Commerce is encouraging SMEs to use its Agent/Distributor Program to get in touch with would-be partners. Furthermore, special "matchmaker" programs and trade fairs have been organized to stimulate small business interest in the EC market.

For its part, the SBA helps conduct the "matchmaker" programs with Commerce to facilitate cooperation between U.S. and EC firms. The SBA is authorized to help refund part of the costs that small firms incur in attending overseas events of this kind. For small business exporters, the SBA set up the Export Revolving Line of Credit program in 1982. This program allows exporters to make use of a line of credit for up to 18 months. Small firms can borrow up to \$750,000.³¹ According to SBA officials, the principal problem with the program has been underutilization.³² Through mid-1989, only \$42.5 million had been borrowed by SMEs under the SBA program.

In terms of policy considerations, U.S. officials have focused their attention on the EC standards-adoption process and the importance of U.S. participation to ensure that discriminatory technical barriers are not erected. Particularly for smaller businesses with a limited range of products, the perils of a closed standards-setting process in the EC are obvious. Establishment of EC local content requirements and rules of origin also threaten small business interests directly. For those firms unable to contemplate a direct manufacturing presence in the EC, distorting content rules may effectively exclude U.S.-manufactured products from the EC altogether. Moreover, given the large proportion of component parts in U.S. exports of manufactured goods to Europe, the ramifications of discriminatory local content requirements are potentially

²⁷ Ibid.

²⁸ Ibid.

²⁹ Ibid.

³⁰ Congress, House Committee on Small Business, Subcommittee on Exports, testimony of Franklin J. Vargo, Deputy Assistant Secretary of Commerce for Europe and testimony of Susan Engeleiter, Administrator, U.S. Small Business Administration, Sept. 12, 1989.

³¹ U.S. Department of Commerce, *Europe Now: A Report*, Summer 1989, p. 3.

³² Congress, House Committee on Small Business, Subcommittee on Exports, testimony of Susan Engeleiter, Administrator, U.S. Small Business Administration, Sept. 12, 1989.

enormous.³³ Since many small companies ship component parts to EC subsidiaries of U.S. multinationals, SME interests will continue to be a major concern of U.S. policymakers. The Commerce Department sees the defense of small business interests as one of its primary goals in monitoring EC 92.

In the European Community, considerable evidence suggests that policymakers, both on the member-state and Communitywide level, have made the question of small business competitiveness a top priority in preparing for the single market. The EC Commission has encouraged the creation of special loan facilities and strategic advisory services to prepare SMEs in the EC for the challenges of an integrated market. The EC Directorate of Enterprise Policy has started a special program to help SMEs get in touch with possible joint-venture partners.³⁴ In addition, the EC has put together a large data base listing companies that are searching for partners. The EC Commission has also been active in organizing trade fairs to help SMEs meet potential partners from outside the Community. Many member-state governments have also introduced programs to keep SMEs in their countries informed about EC 92 through publicity campaigns and hot lines. Finally, the EC Commission is providing seed capital for startup companies that have failed to attract financing from other sources. Through the so-called Business Innovation Centers (BICs), the EC has committed itself to providing up to half of the capital required to start these businesses.³⁵

Five specific reasons have been cited by the EC in advancing its SME policy for 1992.³⁶ First, the tremendous economic impact that SMEs have in terms of jobs and output. Secondly, the wave of mergers and acquisitions inspired by EC 92 has pointed out the need to preserve smaller enterprises and avoid overconcentration in EC industry. Third, the EC seeks to resolve many of the structural problems that smaller firms face—restricted access to financing, inadequacy of training and limited knowledge of export markets to name a few. Fourth, the EC Commission recognizes the role that SME policy can play in promoting regional development programs, particularly in the Mediterranean countries, where smaller firms contribute so much to employment. Finally, on social policy grounds, the EC understands the contribution that smaller firms can make to better relations between management and labor.

Joint efforts to promote cooperation between U.S. and EC firms have also been undertaken. One

³³ Cooney, "Europe 1992: The Opportunity and the Challenge for U.S. Economic Interests," p. 81. Cooney estimates that about 34 percent of all U.S. exports to the EC are shipped as component parts to affiliates of U.S. firms in Europe.

³⁴ Sean Milmo, "EC Launches Small Business Back-Up Plan," *Business Marketing*, May 1989, p. 34.

³⁵ *Ibid.*

³⁶ *OJ No. C 56*, (Mar. 7, 1990), p. 65.

such program was the "Export '89 American-European Small Business Trade Congress and Symposium" in West Germany, sponsored by Commerce, the EC Commission and the German Federation of Independent Businesses. Organization of U.S.-European events of this kind is a priority for policymakers on both sides of the Atlantic.

SME Involvement in International Markets

Export marketing has historically been the vehicle through which smaller firms in the United States enter overseas markets. Still, the SME share of total U.S. exports remains quite small. In a 1988 survey of 5,000 U.S. companies, Dun & Bradstreet found that 8 percent of the firms with fewer than 100 employees in the survey exported their products.³⁷ However, the experience of those small firms that export actively appears to be positive. Fifty-six percent of exporting firms in the Dun's survey said their export volume had grown over the preceding year, while 23 percent said exports had increased by between 20 and 49 percent compared to the year before.³⁸ The Dun's survey concluded that almost 85 percent of all firms in the United States employ fewer than 20 people. Accordingly, even a small improvement in export volume among these firms could have a dramatic effect on the U.S. trade balance.

A recent study commissioned by the SBA provides additional insight into small-business exporting patterns. Based on data covering direct exports of manufactured products transported by ocean vessel, the SBA report found that SMEs accounted for 12.2 percent of the value of all shipments.³⁹ Firms with fewer than 100 employees accounted for 4.4 percent of total export value. Medium-sized firms⁴⁰ contributed 7.8 percent. When traffic handled by brokers and wholesalers is factored in, the study estimates the SME share of total export value rises to approximately 21 percent.

Based on the SBA numbers, an estimate of SME export activity by sector has also been completed. In table 19-2, the contribution of small and medium-sized firms to the value of U.S. exports to Western Europe in 18 manufacturing industries is listed.⁴¹

³⁷ Dun & Bradstreet Corp., Economic Analysis Dept., *The Dun's 5,000 Survey*, 1989, p. 1.

³⁸ *Ibid.*, p. 3.

³⁹ Jack Faucett, *Small Business Exports of Manufactured Products*, 1985, Washington, DC, U.S. Small Business Administration, Office of Advocacy, 1988, p. E8-1. Data for the survey were taken from the PIERS (Port Import Export Reporting System) data base, maintained by the *Journal of Commerce*. Shipments of goods through brokers and wholesalers are excluded. Vessel exports alone account for only about 38 percent of all outbound traffic.

⁴⁰ Defined here as those firms employing between 100 and 500 people.

⁴¹ Figures are compiled from the 1988 SBA export survey. Industries are broken down according to two-digit SIC codes.

Table 19-2

Small and medium-sized firms' share of value of exports to Western Europe, by Industry, 1985, in percent

Industry	Small firms' share of total exports	Medium-sized firms' share of total exports
Food and kindred products	5.7	12.6
Textile mill products	10.7	13.8
Apparel and fabric	4.2	13.6
Lumber and wood products	11.9	9.8
Furniture and fixtures	14.3	20.3
Paper and allied products2	0.6
Printing and publishing	3.3	31.4
Chemicals and allied products	1.7	8.4
Rubber and plastic products	4.8	9.7
Leather and leather products	4.9	57.5
Stone, clay, glass and concrete	4.9	4.9
Primary metal industries	3.1	4.5
Fabricated metal products	8.8	19.2
Machinery (except electrical)	3.5	6.3
Electrical and electronic equipment	2.2	7.8
Transportation equipment	2.4	1.1
Photo and medical instruments	3.8	18.9
Misc. manufactures	18.9	26.0
Total of Manufactured Goods	3.2	7.4

Source: Jack Faucett, *Small Business Exports of Manufactured Products, 1985*, U.S. Small Business Administration, 1988. Small firms are defined here as having fewer than 100 employees. Medium-sized firms: 100-500 employees.

Export marketing, however, is only one of the many options open to SMEs when deciding upon a strategy for expanding international business. Increasingly, smaller firms with the patience and savvy to make long-term commitments to the marketing of their products overseas are exploring joint ventures and strategic alliances with like-minded foreign companies as an attractive alternative to exporting. Particularly with respect to the EC, where regulatory and procedural changes are likely to require almost continuous monitoring on the part of U.S. firms, strategic allies can give SMEs a better chance to remain competitive in the single market. A number of small companies in the United States have pointed out the advantages of relying on European partners to supervise distribution and marketing in the EC, leaving more time for the U.S. firm to concentrate on production and compliance with European specifications.⁴²

Distribution appears to be one of the most daunting obstacles for smaller firms trying to stay competitive in Europe. Generally, setting up a multinational distribution network without forming partnerships is too costly for SMEs. The owner of a small business in the United States, without the luxury of time to shuttle back and forth across the Atlantic, is often forced to enlist the services of an agent or distributor with limited knowledge of his product line.⁴³ If a special

⁴² Paul Munier Lee, "Over There: The Exporting Challenge," *Small Business Reporter*, January 1990, p. 40.

⁴³ Small business concerns about agents are expressed in Alex F. De Noble, and others., "Export Intermediaries: Small Business Perceptions of Services and Performance," *Journal of Small Business Management*, April 1989, p. 33.

relationship with a European firm does not exist, smaller firms are usually forced to rely on trade shows and government-sponsored marketing programs to find an ally. Once the partner is identified, though, many small U.S. firms find themselves in a much better position to tackle the complexities of the single-market program.

Specifically with respect to the EC 92 program, big firms have demonstrated a clear advantage in mustering the resources to monitor the EC policy-making process, conducting sophisticated market research and, if necessary, finding the appropriate European partner. However, as more attention is focused on the needs of SMEs, the prospects for greater small firm involvement in the EC—above and beyond a strict reliance on exports from a U.S. base of operations—appear bright.

Small Business Economics

Several sets of reasons have been advanced to explain the recent growth of the U.S. small business sector. In the first issue of the journal *Small Business Economics*, William Brock and David Evans pointed out six factors influencing the expansion of SME activity:⁴⁴ first, the leading role that small firms play in high-growth infant industries where new technologies are employed extensively; second, the reduced cost of high-technology products and improved access to computers have lowered barriers to entry for young firms; third, stiffer international competition and uncertainty related to exchange rates have led firms to value flexibility

⁴⁴ William A. Brock and David S. Evans, "Small Business Economics," *Small Business Economics*, vol. 1, January 1989, p. 9.

over size;⁴⁵ fourth, the entry of women and baby boomers into the U.S. workforce has made it easier for small firms to hire well-trained people; fifth, distinct changes in consumer tastes have placed a premium on customized goods over mass-produced items; finally, deregulation of some U.S. industries is identified as a force behind the decision by many SMEs to enter the market.

In addition, many analysts have pointed to the availability of risk capital for small firms in the United States and the willingness of scientists and managers to start their own firms as critical factors influencing small business growth.⁴⁶ In Europe, on the other hand, economists see the residual power of industrial monopolies and the high cost of capital as factors having a negative impact on small business development.⁴⁷

In recent years, economists have spent a great deal of time analyzing the traditional argument that, in deciding upon the appropriate size of a firm, "bigger is better."⁴⁸ By increasing scale, the traditional argument goes, big firms could spread fixed costs over a larger production line, thereby lowering unit costs. Big companies, moreover, could shelter themselves from the risks associated with huge fluctuations in production and prices while small firms felt the sting of the business cycle. Most importantly, perhaps, large firms could invest huge sums of money into research and development, taking advantage of the latest technological innovations to improve efficiency and introduce high-quality, mass-produced goods.

The experience of large corporations created in this mold, however, has not always been happy. Particularly in the European Community, disastrous performances by "national champions" in such industries as automobiles and steel led policymakers to conclude that large companies were actually facing higher costs because of bureaucratic inefficiency.⁴⁹ The failure of mergers to stave off inefficiency and losses in the British auto industry during the 1960s and 1970s is perhaps the most notorious case reflecting the shortcomings of a "bigger is better" policy in Europe. Based on these observations and the trend toward greater involvement by SMEs in both the U.S. and EC economies, two analysts have recently noted that

⁴⁵ This idea has also been put forward by Z. Acs, D. Audretsch and B. Carlsson, "Flexible Technology and Firm Size," *RPIE Working Paper*, Cleveland, OH, Case Western Reserve University, 1988.

⁴⁶ Felix R. FitzRoy, "Employment, Entrepreneurship and 1992: Microeconomic Policy and European Problems," *Small Business Economics*, vol. 2, January 1990, p. 18.

⁴⁷ *Ibid.*

⁴⁸ During the 1960s, a number of analysts concluded that the only way for European firms to survive competition from their large corporate rivals in the United States was to favor the creation of huge corporations capable of realizing economies of scale. See, for example, J. Servan-Schreiber, *The American Challenge*, (New York: n.p., 1968).

⁴⁹ See Jacquemin and de Lichtbuer, "Size, Structure, Stability and Performance of the Largest British and EEC Firms," *European Economic Review*, vol. 4 (1973), p. 393.

"merger-induced corporate giantism" is no longer a decisive factor in determining international competitiveness.⁵⁰

Economists and policymakers have begun to question whether traditional notions of economies of scale should still be viewed as "articles of faith." New attention has centered on two trends in manufacturing that enhance the competitiveness of small and medium-sized enterprises.⁵¹ First, shifts in consumer tastes away from identical mass-produced items have made it easier for SMEs to target customers interested in customized niche products.⁵² Secondly, on the shop floor, the application of computers and automation technology has made it possible for small firms to employ flexible manufacturing and just-in-time production techniques to cut down on handling costs and make more productive use of a limited workforce.⁵³

Impact of EC 92 on Large and Small Companies

If the problems related to product standards, testing, certification and rules of origin are resolved satisfactorily, the opportunities for smaller U.S. companies created by the dismantling of residual trade barriers in Western Europe are substantial. Instead of concentrating on one or two key national markets, SMEs will be able to contemplate the marketing and distribution of a truly pan-European product. With the elimination of differences in technical standards among the 12 EC member states and the reduction of costs associated with border controls, smaller firms should be in a position to approach the EC as a single economic unit rather than 12 separate markets.⁵⁴ Still, differences in consumer tastes between EC countries are not likely to disappear anytime soon, and the establishment of new rules related to standards, testing, and certification of products may well present unforeseen problems. U.S. Government officials have recently pointed to the impact that EC-wide standards adoption and harmonized testing and certification procedures may have on small manufacturers, who often find it difficult to

⁵⁰ W. Adams and J.W. Brock, "The Bigness Mystique and the Merger Policy Debate: An International Comparison," *Northwestern Journal of International Law and Business*, vol. 9 (1988), p. 46. The evidence cited by Adams and Brock has been applied to the argument that "diseconomies of scale" actually exist in many industries.

⁵¹ FitzRoy, "Employment, Entrepreneurship and 1992: Microeconomic Policy and European Problems," p. 11.

⁵² Ralph M. Bradburd and David R. Ross, "Can Small Firms Find and Defend Strategic Niches?: A Test of the Porter Hypothesis," *Review of Economics and Statistics*, May 1989. The article examines many of the ideas advanced in Michael E. Porter, *Competitive Strategy* (New York: Free Press, 1980), pp. 145-148.

⁵³ G.H. Manoochehri, "JIT for Small Manufacturers," *Journal of Small Business Management*, October 1988, p. 27.

⁵⁴ Some estimates have placed border-control costs for U.S. firms operating in Europe as high as 5 percent of total European sales. See Seth J. Margolis, "Saddling Up, EC Style," *World*, KPMG Peat Marwick, 1989, p. 38.

meet two different sets of specifications in the United States and Europe.⁵⁵

Deciding upon the proper distribution channel, moreover, can be a difficult matter for smaller firms. If a European sales office or manufacturing facility is prohibited by cost, locating an agent or distributor with knowledge of the U.S. firm's products appears to be essential. Many small-company executives in the United States testify to the benefits of strategic alliances with EC firms that manufacture similar products but are willing to exchange EC marketing knowledge for technology or access to the U.S. market. In the words of a manufacturing company executive in Maine, "I think strategic alliances are the answer for smaller companies that depend on broad territorial coverage of a market like the EC. We do the same thing in the United States—it's impossible to cover California from Maine without an alliance of some kind."⁵⁶

The critical point for SMEs to bear in mind is the need to act early in preparing for the single market. A number of commentators and U.S. officials have stressed the fact that EC 92 is an ongoing process rather than a specific date. U.S. firms that wait for integration to be completed may lose a prime opportunity for success in Europe. Taking steps

⁵⁵ *Ibid.*, p. 38. For additional perspective on the standards, testing and certification issues and their implications for small firms, see Congress, House Committee on Small Business, Subcommittee on Exports, testimony of Mark Z. Orr, Deputy Assistant United States Trade Representative for Europe and the Mediterranean, Apr. 30, 1990.

⁵⁶ Interview by USITC staff, May 1990.

early to work with U.S. Government officials in monitoring EC 92 and in locating potential partners in Europe could save small firm owners from frustration later.

Large U.S. companies, too, stand to benefit greatly from EC 92 if the proper steps are taken early. A prominent management consultant in Europe has listed three areas where multinationals can take full advantage of the opportunities created by EC 92.⁵⁷ First, big firms should exploit opportunities for greater productive efficiency by streamlining organizations and rationalizing distribution. Second, these companies must concentrate more on meeting the challenge of competition from European conglomerates, which may be moving into new markets within the Community. Finally, large firms should prepare for a shakeup of their customer base brought on by reorganization of both the retail and manufacturing sectors. Regulatory harmonization and a reduction of obstacles to the physical movement of goods will presumably allow U.S. multinationals to regard the EC market in much the same way that they see the United States.

For large and small companies alike, however, heightened competition in the EC and in other international markets is almost certain to appear as an outgrowth of the single-market initiative. This fact alone should prompt U.S. companies to think hard about the impact of EC 92 on their ability to compete internationally.

⁵⁷ Magee, "1992: Moves Americans Must Make," pp. 79-80.

CHAPTER 20
AUTOMOTIVE SECTOR

CONTENTS

	<i>Page</i>
The automobile industry in the United States	20-3
Industry profile	20-3
Production and concentration	20-3
Investment and employment	20-3
Exports	20-4
Imports	20-5
The automobile industry in the EC	20-5
Industry profile	20-5
Japanese manufacturing in the EC	20-6
U.S. manufacturing in the EC	20-6
Nature of changes as a result of EC 92	20-7
Standards	20-7
VAT, indirect taxes	20-7
State aid to the auto industry	20-8
Research and development and technology	20-8
Social dimension	20-8
Quantitative restrictions	20-9
Anticipated industry response	20-10
Harmonization of standards, emissions, and taxes	20-10
Quantitative restrictions	20-11
Increased competition and industrial restructuring	20-12
EC investment in the Eastern Europe auto industry	20-13
Outlook	20-14
 Tables	
20-1 Automobiles: U.S. industry production, 1985-89	20-3
20-2 Size distribution of U.S. automobile companies and transplants, 1989	20-3
20-3 Automobiles: Industry employment, 1985-89	20-4
20-4 Automobiles: U.S. exports to the EC and all other markets, 1985-89	20-4
20-5 Automobiles: U.S. imports, from EC and all other sources, 1985-89	20-5

CHAPTER 20 AUTOMOTIVE SECTOR

The Automobile Industry in the United States

Industry profile

Production and Concentration

The United States is the world's second-largest producer of automobiles after Japan. U.S. production is accounted for by assembly plants owned by the Big Three—General Motors (GM), Ford, and Chrysler—and seven Japanese auto companies that either own or have significant interest in eight assembly plants in the United States. U.S. production rose during the 1980s. In 1985, it reached 8 million units (table 1), followed by production declines during 1986–87. During 1988–89, production fell by over 9 percent, to just under 7 million units as a result of declines in retail sales in the United States and Canada.¹ U.S. auto production during the first 2 months of 1990 totaled 854,000 units, or 42 percent less than production during the same period of 1989.² U.S. sales of domestic and imported automobiles totaled 10 million units in 1989 and are forecasted to decline in 1990 to just above 9 million units,³ likely leading to further declines in production.

Table 20-1
Automobiles: U.S. Industry production, 1985–89

Year	Units
1985	8,051,000
1986	7,734,000
1987	7,312,000
1988	7,720,000
1989	6,994,000

Source: U.S. International Trade Commission, *The U.S. Automobile Industry: Monthly Report on Selected Economic Indicators*, USITC Publications 2252, 2151, and 1941.

The U.S. auto industry is dominated by GM and Ford, which produced 3.1 million and 1.7 million autos, respectively, in 1989 (table 2). Chrysler is the third largest U.S. auto producer, with 1989 production of 914,000 autos, followed by Honda with 362,000, Mazda with 205,000, and 5 additional Japanese auto producers.⁴ In 1989, GM held 35 percent of the U.S. market, and Chrysler and Ford held 22 and 10 percent, respectively. In 1989,

¹ Motor Vehicle Manufacturers Association of the United States, Inc., *Economic Indicators: The Motor Vehicle's Role in the U.S. Economy*, 1st quarter 1990, p. 7.

² U.S. International Trade Commission, *The U.S. Automobile Industry: Monthly Report on Selected Economic Indicators*, February 1990 and March 1990, USITC Publications 2259 and 2267.

³ *Economic Indicators: The Motor Vehicle's Role in the U.S. Economy*, 1st quarter 1990, pp. 8–9.

⁴ *Automotive News*, Dec. 25, 1989, p. 33.

Japanese-owned producers with production plants in the United States accounted for nearly 26 percent of the U.S. market (including imports and U.S. production), whereas Western European producers had about 5 percent of the market.⁵ Industry analysts generally believe that U.S. and Western European automakers will gradually lose market share, at least through the mid-1990s, to Japanese automakers.⁶ U.S. auto sales in 1990, through August, support this prediction, with both Ford and Chrysler losing nearly 2 percent of their 1989 market share. GM's market share has remained fairly stable through August 1990. Toyota, Honda, and Mazda have all made relatively strong gains in market share during 1990, approximately equal to U.S. company losses.⁷

Table 20-2
Size distribution of U.S. automobile companies
and transplants, 1989

Company	U.S. production
General Motors	3,102,478
Ford	1,677,681
Chrysler	914,606
Honda	362,375
Mazda	205,294
NUMMI	192,716
Toyota	151,129
Nissan	115,565
Diamond Star	93,395
Subaru-Isuzu	6,317

Source: Derived from *Automotive News*, Dec. 25, 1989.

Investment and Employment

The Big Three automakers earned approximately \$8.4 billion in 1989, down \$2.8 billion from 1988 earnings of \$11.2 billion,⁸ earning approximately 3 percent profit on sales. U.S. investment by motor vehicle and equipment manufacturers totaled approximately \$12 billion annually during 1987–89 and is expected to remain stable in 1990.⁹ Motor-vehicle industry investment in new plants and equipment as a percentage of total manufacturing investment in new plants and equipment has gradually declined, from 8 percent in 1980 to less than 7 percent in 1989. Investment by Japanese-owned firms represents a limited portion of this investment. By 1990, capital investment by Japanese companies in U.S. automobile production operations will amount to approximately \$5.5 billion, with an additional \$1.0 billion projected by 1991.¹⁰ Since 1987, Japanese-owned automakers

⁵ Edward K. Miller, "The Transplants: State of the Industry '90," *Ward's Auto World*, January 1990, p. 23; Jesse Snyder, "Analyst Sees Japan Taking 7 Points of Big Three Market by '94," *Automotive News*, Sept. 4, 1989, p. 37.

⁶ Miller, "The Transplants: State of the Industry '90."

⁷ *Wall Street Journal*, Auto Sales Data, Sept. 6, 1990, p. A9.

⁸ *Economic Indicators: The Motor Vehicle's Role in the U.S. Economy*, 1st quarter 1990, p. 20-1.

⁹ *Economic Indicators*, p. 22.

¹⁰ Temple, Barker and Sloane, Inc., *The International Automobile Industry in America*, 1989, p. 13.

have substantially increased their investment in auto assembly operations in the United States, with previously established companies expanding their existing capacity, and several other companies (Mazda, Subaru/Isuzu, and Mitsubishi) starting production operations for the first time. Current annual output of these plants is approximately 850,000 units, and production is expected to top 1 million units in 1991.¹¹ In September 1990, Toyota announced plans to open a new U.S. assembly plant in an unspecified location, and Nissan is currently expanding production capacity at its U.S. assembly plant.¹²

U.S. automakers employed approximately 355,000 workers in 1989 (table 3). Employment in the industry has declined by over 53,000 workers since 1985, primarily as a result of production decreases.¹³

¹¹ *Japan Economic Journal*, "Japan's Automakers Ask U.S.: Why Are We Still Criticized?" (Mar. 17, 1990), p. 1.
¹² Paul Ingrassia, "Toyota To Build Plant in U.S., Reflecting Gains," *Wall Street Journal*, Sept. 10, 1990, p. A3.
¹³ *Economic Indicators*, p. 20.

Table 20-3
Automobiles: Industry employment, 1985-89
(In thousands)

Year	Number of workers
1985	408.5
1986	400.0
1987	381.4
1988	356.8
1989	354.8

Source: *Economic Indicators: The Motor Vehicle's Role in the U.S. Economy*, 1st quarter, 1990, Motor Vehicle Manufacturers Association, May 18, 1990.

Exports

In 1989, U.S. exports of autos to the EC totaled \$609 million (46,910 units), the majority of which were shipped to West Germany and France (table 4).¹⁴ U.S. exports of autos to the EC have increased substantially since 1985, as U.S. automakers have taken advantage of 5 consecutive years of record-level auto sales in Western Europe that have continued into the first quarter of 1990.¹⁵ While U.S. exports of autos to the EC increased elevenfold in value during 1985-89, the EC remains a relatively unimportant export market for U.S. producers,

¹⁴ Kevin Done, "Strong Car Sales in Western Europe Defy Forecasts," *Financial Times*, Apr. 20, 1990, p. 2.
¹⁵ Harry A. Stark, "World Outlook," *Wards Automotive Yearbook: 1989*, p. 76; Done, "Car Sales Defy Forecasts."

Table 20-4
Automobiles: U.S. exports to the EC and all other markets, 1985-89

Market	1985	1986	1987	1988	1989
<i>Quantity</i>					
Belgium and Luxembourg	102	595	1,685	4,136	4,309
Denmark	9	13	62	122	270
France	1,546	3,584	8,305	5,692	13,215
West Germany	2,414	4,615	6,532	18,975	19,732
Greece	21	29	41	96	79
Ireland	3	4	0	5	25
Italy	770	463	213	563	2,360
Netherlands	186	474	1,084	2,251	3,314
Portugal	5	2	2	7	9
Spain	27	37	83	83	184
United Kingdom	253	254	315	1,985	3,413
Total EC	5,336	10,070	18,322	33,915	46,910
All other	695,473	661,537	613,087	745,058	731,463
Total	700,809	671,607	631,409	778,973	778,373
<i>Value (1,000 dollars)</i>					
Belgium and Luxembourg	1,368	6,742	19,402	52,404	54,961
Denmark	160	189	906	1,870	3,589
France	14,333	39,668	118,867	87,787	200,482
West Germany	26,175	52,636	82,474	242,996	251,515
Greece	248	304	416	808	1,311
Ireland	21	71	0	35	281
Italy	7,846	5,490	3,139	6,755	26,973
Netherlands	2,163	6,430	15,053	28,938	40,195
Portugal	50	24	23	59	69
Spain	532	789	1,597	941	2,035
United Kingdom	2,741	3,497	5,169	15,208	27,268
Total EC	55,637	115,840	247,046	437,801	608,678
All other	5,964,455	6,137,983	6,442,168	7,873,966	8,285,856
Total	6,020,092	6,253,823	6,689,214	8,311,767	8,894,534

Source: Compiled from official statistics of the U.S. Department of Commerce.

accounting for only 7 percent of all automobiles exported from the United States. U.S. exports of autos to the EC are relatively low because both GM and Ford supply the EC market primarily from assembly plants located in Western Europe.

Imports

U.S. imports of automobiles from the EC amounted to \$4.4 billion (239,509 units) in 1985, rose to \$10.8 billion (480,270 units) in 1987, and declined to \$6.7 billion (282,470 units) in 1989 (table 5). U.S. imports of autos from the EC accounted for 7 percent of the total quantity of U.S. imports of autos in 1989. Declines during the late 1980s were mainly due to a softening in demand brought on by higher car prices resulting from the continued strengthening of foreign currencies against the dollar, from Japanese automakers' entry into the luxury market segment (a major market segment for EC automakers), and from an overall softening of the luxury car market in the United States.¹⁶ Additionally, EC automakers have lost U.S. market share in nonluxury segments to Japanese producers. Imports from the EC are not likely to return to 1987 levels until at least the mid-1990s.¹⁷

¹⁶ Stark, p. 83; Alan K. Binder, "Import Cars and Trucks," *Ward's Automotive Yearbook*: 1989, 1989, pp. 206-207; Jim Henery, "Low-End Luxury Set Stage in New York," *Automotive News*, Apr. 16, 1990, p. 4.

¹⁷ Binder, "Import Cars and Trucks," pp. 206-207.

The Automobile Industry in the EC

Industry Profile

The EC is the world's largest market for passenger cars, with 1989 sales totaling 13 million units. EC exports of automobiles amounted to 1.4 million units and the EC car industry made a net profit of \$6.3 billion in 1988 (\$15.4 billion if spare parts are included).¹⁸

The EC automotive industry (including the parts industry) directly employs about 1.7 million people, or approximately 8 percent of those employed in EC manufacturing. About 10 percent of all jobs in the EC directly or indirectly depend on the automobile sector.¹⁹ Capital expenditures by EC car manufacturers amounted to \$50.8 billion during 1981-86, placing the EC automobile industry among the leading sectors for investment, equal to the chemicals and food/tobacco sectors.²⁰

The six largest European carmakers are Volkswagen, Fiat, Peugeot, Renault, GM, and Ford. West German automaker Volkswagen AG and the Italian firm Fiat ranked first in 1988 European sales, with each firm holding 15 percent of the market. During 1987-88, Volkswagen's worldwide sales increased by 4 percent to 2.9 million cars.²¹ During

¹⁸ U.S. Department of State Telegram, "EC Industry Council, March 13: A Single Market for Cars," March 1990, Brussels, Message Reference No. 04123.

¹⁹ EC Commission, "Panorama of EC Industry," 1989, p. 14-5.

²⁰ "Panorama of EC Industry."

²¹ Ward's 1989 Automotive Yearbook, p. 84.

Table 20-5
Automobiles: U.S. Imports, from EC and all other sources, 1985-89

Source	1985	1986	1987	1988	1989
<i>Quantity (in units)</i>					
Belgium and Luxembourg	5,442	3,392	17,284	16,393	22,603
Denmark	0	0	0	0	14
France	11,118	8,139	26,707	15,990	4,885
W. Germany	195,846	191,111	377,542	264,249	216,263
Italy	3,290	4,525	8,648	6,053	9,319
Netherlands	21	48	30	3	8
United Kingdom	23,792	27,191	50,059	31,636	29,378
Total EC	239,509	234,406	480,270	334,324	282,470
All other	1,490,644	1,603,773	4,108,740	4,115,889	3,759,557
Total	1,730,153	1,838,179	4,589,010	4,450,213	4,042,027
<i>Value (1,000 dollars)</i>					
Belgium and Luxembourg	71,166	44,657	267,953	274,108	384,579
Denmark	0	0	0	0	11
France	118,618	93,574	255,998	171,178	58,765
W. Germany	3,522,895	4,789,873	8,901,850	6,441,720	5,020,555
Italy	69,790	83,658	177,965	152,152	262,709
Netherlands	429	1,109	351	32	15
United Kingdom	588,508	716,643	1,193,837	941,406	937,014
Total EC	4,371,406	5,729,513	10,797,955	7,980,596	6,663,649
All other	14,839,269	17,436,594	37,060,048	39,024,100	37,752,966
Total	9,210,675	23,166,107	47,858,003	47,004,697	44,416,615

Source: Compiled from official statistics of the U.S. Department of Commerce.

1988-89, Fiat's sales rose from \$34 to \$41 billion, and operating profit increased from \$2.9 billion to \$3.9 billion.²² France's Peugeot held 13 percent of the European market in 1988, with sales of 1.7 million vehicles.²³ Ford of Europe held a 12 percent share of Europe's market in 1988.²⁴ General Motors Europe sold 1.4 million vehicles in 1988 and was the leader in sales in Belgium, Holland, Denmark, and Switzerland.²⁵ Regie Nationale des Usines Renault returned to profitability in 1988, as passenger-car production rose by nearly 1 percent from 1987 to 1.4 million units in 1988.²⁶

Japanese Manufacturing in the EC

In 1986, Nissan Motor Manufacturing (United Kingdom) Ltd. began production of passenger cars in the United Kingdom, recording an initial annual output of 6,000 units and increasing to 40,000 units in 1988. In April 1989, Nissan announced that it would expand capacity from 60,000 to 400,000 cars a year. Nissan's local content amounted to 44 percent in 1987, increased to 60 percent in 1988, and exceeded 70 percent in 1989.²⁷ To further raise local content, Nissan plans to produce cylinder heads for engines, with production capacity of 200,000 cylinder heads in 1993. Employment at Nissan's British facility totaled 2,000 at the end of 1988.²⁸ Nissan Motor Iberica, S.A. produces commercial cars in Spain; production of commercial cars exceeded 20,000 units in 1987.²⁹

In 1989, Toyota Motor Corp. announced plans to build a \$1.2 billion plant in the United Kingdom, the largest single Japanese investment in Europe.³⁰ Production startup is scheduled for 1992, with capacity of 200,000 units. Employment will total 3,000. Also in 1989, Toyota announced investment in Wales for the production of engines to supply Toyota's British automobile facility. Production is expected to begin in late 1992, with production capacity of 200,000 units, and final employment of 300.³¹ In addition, Toyota has a joint venture with Volkswagenwerk AG for commercial car production in West Germany. Major components will be shipped from Japan, with local content levels expected to reach about 50 percent by 1990.³²

Honda Motor Co. Ltd. exports a large quantity of knock-down kits to its joint venture with the British

firm Austin Rover Group (ARG). In 1979, Honda Motor Co. Ltd. established a link with the United Kingdom's BL Limited and began automobile production at Rover's facility in 1981. Honda of the United Kingdom Manufacturing Ltd. (a United Kingdom subsidiary) is constructing a facility to produce engines and will have capacity to produce 100,000 automobiles, beginning in 1991. Projected employment is 1,500 for cars and 150 for engines.

In 1987, Isuzu Motors Ltd. established a joint venture with the firm General Motors Europe to produce 50,000 light trucks annually. The firm IBC Vehicles Ltd. (60 percent equity held by GM and 40 percent by Isuzu), employs 2,000 workers and is located in the United Kingdom. Isuzu Motors Ltd. plans a joint venture with GM to produce 3,000 to 5,000 multipurpose four-wheel-drive vehicles in the United Kingdom, supplying the EC market through the Opel brand.³³

Mazda Motor Corp. supplies finished cars to Ford Europe via an international specialization system in conjunction with Ford Motor Co. Fuji Heavy Industries (Subaru) has applied to the Government of France for approval to build a joint venture automobile production plant with S.A. Heuliez Automobiles. Annual production is targeted at 30,000 vehicles. Suzuki Motors, which holds a 17.3 percent share of Spain's Land Rover Santana, will use the Madrid-based firm's assembly lines to produce a four-wheel-drive vehicle beginning in 1990. Annual production is targeted at 24,000 vehicles.³⁴ By the mid-1990s, industry sources estimate that Japanese firms will be producing over 500,000 autos in their British factories. Total Japanese investment plans over the next 5 years for production facilities in the United Kingdom amount to \$2.6 billion.³⁵

U.S. Manufacturing in the EC

In order to preserve and increase their market share, U.S. automakers are increasing investment in the EC auto industry. Ford is planning to spend \$10 billion in Europe during the first half of the 1990s to enhance its position. Ford of Europe accounts for 34 percent of Ford Motor Co.'s worldwide profits, with automobile manufacturing facilities in six European countries.³⁶ The company has 22 plants in Europe overall. Though Ford of Europe's profits fell by 18 percent to \$1.2 billion in 1989, it was the group's second best year ever. Profits decreased in 1989 primarily due to increased new-product development costs.³⁷

GM's Automotive Components Group has established a specific European organization to

²² Ward's Automotive International, February 1990, pp. 2 and 90.

²³ Ward's 1989 Automotive Yearbook.

²⁴ *Ibid.*, p. 84.

²⁵ *Ibid.*

²⁶ *Ibid.*

²⁷ Eiichi Oyama, "Automobile Industry in Preparation for 1992 European Community Integration," *Digest of Japanese Industry & Technology*, No. 250/1989, p. 17 (hereafter DJIT).

²⁸ Japan Automobile Manufacturers Association, Inc., *The Motor Industry of Japan 1989*, pp. 16-17.

²⁹ DJIT, p. 18.

³⁰ "Carmakers Expand EC Plants to Win Inside Track," *Japan Economic Journal*, Dec. 31, 1988, p. 3.

³¹ Japan Automobile Manufacturers Association, Inc., *The Motor Industry of Japan*, 1989, pp. 16-17.

³² DJIT.

³³ *Ibid.*

³⁴ "Carmakers Expand EC Plants to Win Inside Track," p. 3.

³⁵ Japan Automobile Manufacturers Association Inc., "International Development of Manufacturing Operations," 1989.

³⁶ 1989 Ford Motor Co. Annual Report.

³⁷ *Ibid.*

coordinate GM's component activities in Europe and between Europe and the United States. The strong EC auto market helped GM Europe achieve a record \$1.8 billion profit in 1989, up 2.8 percent over 1988.³⁸ This accounted for 43 percent of GM's worldwide profit.³⁹ GM has 6 vehicle assembly plants and 19 component-manufacturing facilities in Europe, many of which are operating at full capacity. GM's Opel/Vauxhall operations are the fastest growing of the "Big Six" European carmakers.

Chrysler has no significant⁴⁰ manufacturing operations in Europe, as a result of selling its European holdings in 1978 in response to financial difficulties. In January 1990, however, Chrysler announced that it would produce minivans in 1991 in a joint venture with Steyr-Daimler-Puch, of Austria. Production of the vehicles is planned at the Austrian firm's Graz, Austria, plant.⁴¹ Chrysler is also negotiating with Fiat to form a tie-up of an undisclosed nature that may provide Chrysler with production capacity in the EC.

Nature of Changes as a Result Of EC 92

On December 19, 1989, the Commission of the European Communities issued a communication summarizing its plans for completing the single market in the motor-vehicle sector by 1993.⁴² The communication outlines a six-point proposal for: (1) technical standards harmonization and EC whole-type approval; (2) an approximation of indirect taxes; (3) the management and control of state intervention; (4) research and technology programs, particularly in the areas of engine performance, new materials, design technologies, materials recycling, and manufacturing techniques; (5) vocational training and retraining; and (6) dismantling internal quantitative restrictions in 1991 and 1992, to be replaced by a voluntary export restraint with Japan.⁴³ The six-point plan is discussed below.

Standards

The EC has been issuing technical regulations on cars for over 20 years. As part of the 1992 program, the EC aims to complete harmonization in this area, resulting in a single-uniform set of binding EC requirements and a single approval procedure, known as whole-type approval. Success in this area is linked to the resolution of VRAs for

Japanese autos. Currently, automobile producers have the option of submitting their vehicles for technical approval (homologation) under either a national or mixed national-EC approval system. Models or prototypes of motor vehicles must undergo an approval procedure in each country to certify that the type of vehicle meets national technical requirements. Once the model of the vehicle is approved, vehicles can be registered in that country. The mechanism whereby type-approval may be granted was the subject of Council Directive 70/156 of February 6, 1970. According to this directive, approximating the various national laws for motor vehicles required mutual recognition of member states' inspections on the basis of common provisions. Council Directive 70/156 also called upon all member states to implement national technical requirements. Of the required 44 vehicle standards directives, 3 have not been approved, and the 41 standards directives are optional; thus, cars sold in the EC market are not required to be wholly type-approved. The EC Commission's goal is to complete by 1992 the whole set of directives called for in the single 1970 directive, moving from optional to mandatory and exclusive EC-wide type-approval for motor vehicles. U.S. auto manufacturers have indicated that the movement to whole-type approval will result in decreased costs and a decreased administrative burden, and that U.S. manufacturers will find the EC market an easier one in which to sell cars. In early 1990, the EC Commission stated that it will continue its work on measures paving the way for implementation of Community type-approval for motor vehicles (including lorries, buses, coaches, tractors, and two-wheeled vehicles) and that technical harmonization rules will be supplemented by strict emission standards.⁴⁴

VAT, Indirect Taxes

The December 19, 1989, Communication from the Commission includes the equalization of indirect taxation as one of the six areas in which the EC will take action for completion of the single market in the motor-vehicle sector.⁴⁵ The EC defines the VAT as an indirect, or nonspecific, tax. In early 1990, the Eco/Fin (Economy and Finance) Council produced an agreement in principle on the harmonization of taxation. According to the communication, the EC agreed to maintain the basic VAT rates between 14 and 20 percent until the end of 1991, when a new tax regime is scheduled to be implemented. The new tax rates will be either a narrower rate or a minimum rate. Additionally, the Council will decide the scope of reduced rates among member states for certain essential goods before December 31, 1991.⁴⁶ Since intra-EC trade in

³⁸ "GM Europe Sets Mark," *Ward's Automotive International*, Update, vol. 5, No. 6 (March 1990), p. 7.

³⁹ 1989 General Motors Annual Report.

⁴⁰ Chrysler owns Lamborghini, but the Italian firm produces only very low-volume cars for niche markets.

⁴¹ Melinda Grenier Guiles, "Chrysler To Begin European Production of Vehicles for First Time in 12 Years," *Wall Street Journal*, Jan. 23, 1990, p. A1.

⁴² EC Commission, *Communication From the Commission, A Single Community Motor Vehicle Market*, Dec. 19, 1989.

⁴³ *Ibid.*

⁴⁴ *Programme for the Commission for 1990*, EC Commission, Jan. 10, 1990, p. 6.

⁴⁵ EC Commission, "A Single Community Motor Vehicle Market," Dec. 19, 1989, p. 4.

⁴⁶ "Guidelines for Tax Harmonization," EURECOM, vol. 2, No. 2, February 1990, p. 2.

motor vehicles is affected by disparities in taxes, the EC Commission is requesting member states to facilitate progress towards harmonizing VAT rates applicable to motor vehicles, and to not wait for the Council to complete its work on the elimination of tax barriers. The EC Commission considers "VAT" taxes that are exorbitantly higher than lower national taxes to be a barrier to trade. The EC Commission states that it will take steps to bring about progress in the area of indirect taxes of motor vehicles.⁴⁷ The EC Commission's plan for removing tax barriers within the EC includes a plan for a two-rate VAT system consisting of a standard-rate band of 14 percent to 20 percent, and a reduced rate band of 4 percent to 9 percent.⁴⁸ Member states would be free to set the specific rate within a band; however, the EC Commission is seeking to specify the band to which a specific product is assigned. Automobiles would be taxed within the higher, or standard rate.⁴⁹ Upon the sale of automobiles, the VAT rate for the country in which the automobile is registered would apply. For those that are unregistered, the VAT rate for the country of the owner's permanent residence would apply.⁵⁰ Member states losing revenues through the equalization of VAT or other indirect taxes could enhance such revenue through the increase of other types of taxes, such as a diesel fuel tax or automobile registrations.⁵¹

State Aid to the Auto Industry

In December 1988, the EC Commission adopted a framework on state aids in the motor-vehicle sector.⁵² The objective of the framework is to establish transparency of state aids to motor-vehicle producers and to impose a stricter discipline on the granting of state aid to avoid distortion of competition in the motor-vehicle sector. Based on article 93.1 EEC, the framework requires member states to notify the EC Commission of any proposal to grant aid of more than \$9.2 million under any scheme already approved by the EC Commission. The notifications will be examined by the EC Commission for their impact on the sector and their compatibility with other European Community objectives. The framework was adopted in 1989 by all member states except Spain and West Germany. Following the EC Commission's action against West Germany and Spain in July 1989 (IP(89)606) under

⁴⁷ EC Commission, "A Single Community Motor Vehicle Market" Dec. 19, 1989, pp. 5-6.

⁴⁸ For further discussion of the EC's tax harmonization efforts, see U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States*, (Investigation No. 332-267), USITC Publication No. 2204, July 1989, ch. 10, and USITC Publication No. 2268, March 1990, ch. 10.

⁴⁹ Deloitte, Haskins & Sells, "Deloitte's 1992 Guide," 1989, p. 41.

⁵⁰ "Indirect Taxation: an Update," *EC Bulletin*, Price Waterhouse, Issue No. 84 (September/October 1989).

⁵¹ Keith M. Rockwell and Bruce Barnard, "One Europe: 1992 and Beyond," *The Journal of Commerce*, p. 39.

⁵² OJ C 123 May 18, 1989.

article 93.2 of the EEC Treaty, Spain adopted the framework, and has been applying it to all aids in the automobile sector since January 1, 1990. West Germany, however, has continued to refuse to adopt the framework; and the EC Commission has since closed the case against West Germany with a decision that requires West Germany to notify the EC Commission in advance of all aids covered by the framework, beginning May 1, 1990. Aids effective before that date will be subject to the provisions of West German law on acquired rights; aids granted after that date, and of which the EC Commission has not been notified, will be illegal and could be subject to a recovery order.⁵³

Research and Development and Technology

The Single European Act (SEA) states that the Community's aim will be to strengthen and encourage the Community to become more competitive at an international level. In support of this directive, the EC Commission has presented to the Council a Framework program (Com(89) 379) for research and technological development (R&TD) covering the period 1990-94.⁵⁴ The Framework program encourages a greater degree of cross-border R&TD cooperation between industrial companies, including small and medium-sized firms, research centers, and universities.⁵⁵ In addition, in 1986 the European Community began an 8-year, \$600 million Prometheus Project to develop ways to ease traffic flows, improve safety, protect the environment, and save money for needed highway construction.⁵⁶ The Program for a European Traffic with Highest Efficiency and Unprecedented Safety is a joint research effort by 15 European carmakers, 105 electronics firms and suppliers, and an additional 90 research institutes, to determine how to improve traffic through the use of microelectronics and sensors, telecommunications, information processing, and artificial intelligence. Prometheus projects include road and traffic guidance systems, advance warning of road hazards, infrared vision enhancement, and head-up display.⁵⁷

Social Dimension

Social dimension of the internal market refers to the harmonization of member state policies on employment markets, industrial relations systems, worker safety and health regulations, and social welfare and social security systems.⁵⁸ In 1989, 11

⁵³ EC Commission, State Aid, "State Aids in the Motor Vehicle Sector Negative Decision Against Germany," (35/89), IP(90)150, Feb. 21, 1990.

⁵⁴ For further discussion of the EC's R&TD framework, see "Research and Development," ch. 16 of this report.

⁵⁵ EC Commission, *European Economy, Annual Economic Report 1989-90*, No. 42, November 1989, p. 62.

⁵⁶ *Automotive News*, "Unsnarling Europe's Traffic Mess," Apr. 16, 1990, p. 23.

⁵⁷ *Ibid.*

⁵⁸ For further discussion of social dimension, see USITC, *Effects of EC Integration*, USITC Publication 2268, pp. 18-1 to 18-11.

member states adopted a Charter of Fundamental Social Rights (the Social Charter), which established 12 tenets for workers' rights, including the right to vocational training. On November 30, 1989, the Council of Labour and Social Affairs Ministers adopted a EUROTECNET Program, inaugurated January 1990.⁵⁹ The objective of this 5-year Community Action Programme for the Promotion of Innovation in Vocational Training Resulting from Technological Change is to encourage innovation in vocational training to adapt to technological changes and their impact on employment, work, and qualifications, and to provide for necessary new skills and qualifications. The EUROTECNET programme will be comprised of national and transnational projects, taking into account the framework of guiding to develop principles and improve training policies and systems in new technologies. The EUROTECNET Programme will be coordinated with other similar EC programs. The Council approved a budget of \$5.8 million for the first 3 years.⁶⁰

Quantitative Restrictions

Currently, the United Kingdom, France, Spain, Italy, and Portugal impose restrictions on imports of automobiles from Japan. In December 1989, the EC announced that as of January 1, 1991, it will begin the process of removing all member-state quotas on automobiles. This process is to be completed by January 1, 1993. The EC will seek a voluntary restraint arrangement with Japanese producers to restrain their exports of automobiles for an undetermined period of transition expected to begin on January 1, 1991, and to continue even after January 1, 1993. Neither the length of the transitional period nor the market share to be held by Japanese-owned firms during that period has yet been determined. The EC has indicated that it will avoid setting minimum local-content requirements for those vehicles produced in the EC by Japanese-based manufacturers. EC officials have reportedly stated that automobiles produced in the United States by Japanese automakers are considered U.S. automobiles and will not be included in the EC's voluntary restraint arrangement with Japan.⁶¹

The Vice-President of the EC Commission responsible for competition policy is in favor of rapid liberalization of the EC auto market. According to the official, the transition period should not go beyond 1996, and the EC should pursue efforts to modernize and restructure its car industry. Recently, however, the EC Commission has proposed that the five member states having import restraints on autos dismantle their restraints after 1992, and that the EC impose a voluntary

export restraint that will run for 6 years. At the same time, measures would be introduced to improve the competitiveness of the EC automobile industry. A policy of restricted access to the EC market reportedly would have the following negative effects:

- (1) it would deny European consumers unrestricted choice and would force price increases not only in the EC market as a whole, but in terms of intra-EC trade;
- (2) the maintenance of restricted markets and national quotas after 1992 would reduce the credibility of the concept of the single market and would affect other sectors;
- (3) the policy would involve maintaining frontier controls on trade, which must be abolished in the single market, and an acceptance of an unsatisfactory market segmentation;
- (4) EC automobile manufacturing would become European centered, while the auto sector is becoming more global;
- (5) the EC risks damaging the prospects of its remaining major players in the international auto sector;
- (6) European manufacturers would delay restructuring of the auto industry, since only a free market will encourage them to adapt; and
- (7) restrictions would force the Japanese to shift production facilities to Europe, where they may be encouraged to move up-market in their production, or in third markets such as EFTA and Eastern Europe, from which they can enter the common market, even if Japanese investment in the EC is considered beneficial. The EC does not maintain restrictions against EFTA and Eastern European countries, and 50 percent local content in these countries establishes them as the countries of origin.⁶²

A December 1989 meeting of the General Affairs Council concerning the EC strategy for the automobile industry revealed differences of opinion among member states. The council agreed that proposals should be maintained as one package, and the issue of EC imports of autos from Japan should not be separated from that of improved performance of the EC auto sector. During the meeting, Spain, France, and Italy indicated that care should be taken in dismantling the import restraints and stressed the need for surveillance of imports of autos from Japan. In addition, the French Minister indicated concern about imports of Japanese cars built in the United States.⁶³

⁵⁹ "Council Adoption of EUROTECNET Programme," EC Commission, IP(89)920 Dec. 1, 1989, p.1.

⁶⁰ Ibid.

⁶¹ Representatives of General Motors Corp., interview by USITC staff, May 11, 1990; Detroit, MI.

⁶² Sir Leon Brittan, Vice President of the EC Commission, "A Single Market for Motor Vehicles: Why and When?" speech given at Cambridge Conservative Association Business Club, Feb. 9, 1990, pp. 3-4.

⁶³ Eurobrief, vol. 2, No. 9 (Jan. 12, 1990), p. 12.

In March 1990, the EC Commissioner for External Affairs met with Japan's Ministry of International Trade and Industry to discuss quantitative limits for Japanese automobiles exported to the EC after 1992. The Commissioner indicated that the EC aims to achieve a "gradual and progressive liberalization of the European market within a time frame' by monitoring Japanese exports to the European Community." The EC's three main points at that time were that automobiles produced in Europe are considered European, and the EC Commission would not make any proposal for regulations on local content; that Japanese cars produced in the United States are not an issue because the EC Commission did not expect to see many of these cars exported to the EC; and that Japanese cars produced in Eastern Europe would not be considered a problem by the EC Commission.⁶⁴ At a June 19 meeting, the member states decided against a local-content requirement and decided against including production from Japanese plants in the EC under the restraint arrangement. However, the member states have decided that the more automobiles the Japanese produce in the EC, the less they will be permitted to ship directly from Japan.

This position was recently modified to a more protectionist stance when it was announced that the EC would like to include autos produced in Japanese plants in the EC in a quota on Japanese auto sales in the EC.⁶⁵ The EC would like such a transition period to last at least until 1998. Industry sources indicate that the new EC position may be a bargaining tool to increase the length of the transition period.

Anticipated Industry Response

The overall impact of EC economic integration on U.S. automobile producers and their EC subsidiaries appears to be beneficial with respect to marketing autos in the EC. Furthermore, consumers will benefit from a vastly more competitive market. EC automakers, both domestic- and foreign-owned, are restructuring their operations in preparation for the economic integration. Thus, while the economic integration provides certain benefits, how effectively firms respond to it is expected to have major consequences on their competitive position both inside and outside of the EC.

Auto-parts firms are an integral part of automotive production systems, and the response of auto companies to the economic integration directly affects auto-parts firms in the EC and in other countries. The expected response of auto parts firms is discussed in the context of changes in the EC auto industry.

Harmonization of Standards, Emissions Requirements, and Taxes

Harmonization of EC technical standards, emissions regulations, and taxes are generally viewed as positive developments by U.S. industry representatives, although there is some concern regarding the implementation of certain regulations. Nevertheless, harmonization of these aspects of the auto industry will allow firms to sell their products more easily in the EC market, with less distortion of market forces.

U.S. industry sources indicate that the EC and U.S. automobile industries will benefit from harmonized technical standards. Harmonization of technical standards will likely result in lower manufacturing costs associated with standard design and simplified production and product development. While the EC aims to have one, uniform type approval, some auto manufacturers prefer the current blend of national/EC/ECE standards directives that permit imports of certain low-volume and specialty cars that may not be capable of meeting the uniform standards. According to these automakers, the problem confronting the EC is how to craft a derogation for these special situations.⁶⁶

U.S. automakers have also expressed concern about the requirement to obtain certification from an EC-based lab. They have expressed the desire to have self-certification of standards directives. Some U.S. auto-parts suppliers are also concerned about the certification process. A representative of the U.S. auto-parts industry suggests that suppliers are more concerned with the implementation of certification procedures than with specific directives.⁶⁷ For example, some U.S. suppliers believe that a part that receives type-approval for original equipment (OE) use will also have to achieve certification for aftermarket use even if the part is identical. U.S. suppliers also suspect that EC suppliers will receive preferential treatment in EC certification labs. For example, they fear that U.S. parts firms could be placed lower than their EC counterparts on waiting lists for parts certification. In sum, harmonization of parts standards is generally not viewed as a development that will stimulate U.S. exports of auto parts.⁶⁸ However, given the great diversity of national standards in the auto industry,⁶⁹ harmonization will simplify the marketing of auto parts in the EC.

As part of the harmonization process, the EC is currently expanding emission-standards legislation to include vehicles with an engine size of 1.4 liters or more. A proposal for a new directive has been introduced, covering all vehicles of gross vehicle weight less than 2.5 tons, regardless of engine size.

⁶⁶ Representatives of General Motors Corp., interview by USITC staff, Detroit, MI, May 11, 1990.

⁶⁷ Representative of MEMA, telephone interview by USITC staff, Washington, DC, May 14, 1990.

⁶⁸ Ibid.

⁶⁹ Representatives of Ford Motor Co., interview by USITC staff, Detroit, MI, May 5, 1990.

⁶⁴ *Automotive News*, "Europe Seeks Limits on Japan Exports," Apr. 2, 1990, p. 41.

⁶⁵ Richard Johnson, "Europe May Count Transplants in Setting Japanese Quota," *Automotive News*, July 23, 1990, p. 6.

Pending the acceptance of uniform emissions testing and certification, the EC will have an emission-standards program in place encompassing the entire EC vehicle population by yearend 1990.⁷⁰

U.S. auto industry representatives state that an EC-wide emissions standard would facilitate sales in the EC. However, U.S. industry representatives oppose the addition of new EC test procedures to gain emissions approval. U.S. test procedures have traditionally been acceptable in the EC, and U.S. industry officials note that they are at least as rigorous as EC test procedures.

Emissions laws may provide commercial opportunities for U.S. auto parts firms. The most notable example of such opportunities involves catalytic converters, the market for which is expected to increase substantially in the EC. Some U.S. firms producing engine induction components, engine management systems, and exhaust systems are also optimistic about the market for their products in the EC.⁷¹

The harmonization of value-added taxes on automobiles will likely benefit auto producers by reducing auto-price disparities to consumers, thereby simplifying EC-wide sales efforts. Increased transparency in government subsidy programs is expected to further reduce the distortion of competition by allowing EC member states to more readily evaluate the competitive effects of government subsidies.

Quantitative Restrictions

Removal of quantitative restrictions (QRs) has emerged as a much more controversial issue than other developments affecting the auto industry because it will force EC automakers to confront greater competition within the EC. Consequently, the responses of EC automakers to the removal of quantitative restrictions are more pronounced than are responses to other aspects of the economic integration. In spite of the EC's goal of a single free market, the relative economic significance of the auto industry may prolong the protection of EC carmakers as long as possible. Industry executives note that politicians are reluctant to permit major changes in an industry that has tremendous social, tax-revenue, and economic implications. For example, the various interests of Fiat control 8 to 10 percent of Italy's GNP. Accordingly, industry sources report that the EC auto market will not be fully open until 1997.⁷²

The long-term effectiveness of QRs on Japanese imports has been questioned. For example, the chairman of Vauxhall, a British firm principally owned by GM, recently stated that such restrictions are ineffective since Japanese firms will both produce cars in the EC and export cars to the EC

from the United States.⁷³ In fact, all Japanese auto plants in the United States are now exporting or have plans to export to the EC.⁷⁴ Exports of autos from Japanese-owned plants in the United States would likely increase if the EC enacts its stated preference to include autos produced in Japanese EC transplants in a quota on Japanese autos. Since the EC reportedly maintains that Japanese autos produced in the United States will not be included in a quota, there is no official barrier to exporting to the EC from these plants. It is unlikely that all Japanese transplants in the United States could substantially increase their exports to the EC in the short term. This is particularly true of Honda and Toyota, which enjoy strong U.S. demand for their transplant products. Although Nissan's U.S. plant produces near capacity, the firm is in the process of expanding its capacity and might be able to divert some autos from the U.S. market to the EC market.⁷⁵ Other Japanese transplants in the United States could probably export a significant portion of their output to the EC.

While U.S.-owned automakers might welcome limits on Japanese auto sales, including U.S. transplant products, they could be directly affected by such a policy. Important product lines of U.S.-owned automakers are produced in Japanese transplants in the United States. The Ford Probe, Geo Prizm, Plymouth Laser, and Eagle Talon are all produced in Japanese transplants. Furthermore, various other models of U.S.-badged autos are produced in other Japanese-owned plants in Japan or Canada. These models tend to have relatively strong U.S. sales, and although U.S.-owned firms show only limited interest in selling these models in the EC, their option to do so could be forfeited by an EC Japanese quota, thereby significantly reducing the flexibility of their global strategies.

Even though the ultimate effectiveness of a quota on Japanese products is questioned, the short-term effects of removing existing national restrictions could be significant. If EC automakers are not given time to adjust to heightened competition, at a time when investment in their existing operations is critical, the financial impact could be felt for years. One U.S. automaker favors EC QRs on imports from Japan through a transitional period coupled with the phaseout of national restrictions.⁷⁶

U.S. automakers have stated that the removal of national quotas would permit increased competition and could provide U.S. auto producers with an opportunity to expand sales in some of the currently more protected countries, such as Spain,

⁷⁰ See C (89) 662 final in "Standards," ch. 4 of this report.
⁷¹ Mark Phelan and Marjorie Sorge, "A Hot Market for Cool, Clean Air," *Ward's Auto World*, April 1990, p. 33.

⁷² "Japan, EC Near Agreement on Voluntary Auto Curbs," *Journal of Commerce*, July 17, 1990, p. 5A.

⁷³ "Vauxhall Posts 56% Jump in Pretax Profit, but Chairman Warns of Rising Competition," *European Wall Street Journal*, Apr. 27-28, 1990, p. 6.

⁷⁴ Lindsay Chappell, "Mitsubishi Tags Eclipse for Europe," *Automotive News*, July 2, 1990, p. 3.

⁷⁵ Lindsay Chappell, "Growing Pains Vex Transplants," *Automotive News*, Aug. 6, 1990, p. 1.

⁷⁶ Representatives of Ford Motor Co., interview by USITC staff, Detroit, MI, May 11, 1990.

Italy, France, and Portugal. There are, however, a number of related issues that have raised concern among U.S. automakers. For example, U.S. auto producers have expressed fears that certain EC trade measures, such as local-content requirements and public procurement policies, could be applied in a protectionist way, thereby forcing out third-country investment in Europe.

Recent developments and clarifications in QRs have greatly, though not entirely, allayed these concerns. According to one U.S. automaker, the enforcement of a more transparent and strict EC competition policy would favor third-country investment, since the conditions for state aid would be applied equally to all companies. State-aid practices currently being examined have revealed distorting practices on the part of some member states. A strict competition policy would mean that state subsidies for additional investment in the car industry would be examined from the perspective of the possibility of overcapacity in the EC car industry.⁷⁷ According to U.S. automakers in the EC, although removal of QRs is not likely to stimulate new U.S. investment, all EC automakers will have to invest in existing facilities to remain competitive during the 1990s.⁷⁸

Increased Competition and Industrial Restructuring

Anticipation of the removal of quantitative restrictions is having a dramatic effect on the EC auto industry because it will further open the world's largest auto market to global competition at the same time that EC member states become more integrated. Additionally, U.S.-owned parts firms in the EC are likely to face a less fragmented and more internationally oriented EC auto industry.

During the first 5 months of 1990, there is strong evidence that competitive pressure is building in anticipation of a more open EC market. Fiat, Peugeot, and Renault are widely believed to be vulnerable to an integrated market because of their overdependence on their home markets. Fiat and Peugeot have suffered substantial market-share losses in their home markets during 1990. In September 1990, Fiat temporarily laid-off one-third of its workforce. Volkswagen, which sells predominantly in the West German market, has experienced sales declines there, although overall sales have increased.⁷⁹

Not only will competitive pressure among the largest EC automakers increase, but Japanese automakers, which currently account for 11 percent of the European market, may also more than double

their market share by 1995.⁸⁰ The commitment of Japanese automakers to the EC market is evidenced by their already extensive investment in the EC. In this sense, Ford, which places a strong focus on the British market, may suffer as the United Kingdom becomes the center of Japanese marketing and production efforts. A recent study indicates that Japanese producers have a productivity advantage over their EC rivals.⁸¹

The EC integration process will also result in increased competition in the EC auto-parts industry. For example, EC parts firms are more fragmented than the automakers; many of these firms are small and highly reliant on their domestic market. While many EC automakers have traditionally encouraged parts firms to be domestically oriented by failing to introduce extensive cross-border components sourcing,⁸² some automakers, such as Ford, GM, VW, and Peugeot, have introduced an element of EC-wide sourcing.⁸³ This trend has intensified with changes in the ownership of EC automakers. Such changes can cause purchasing decisions to be transferred suddenly to other countries.⁸⁴ Larger parts firms are attempting to become more pan-European enterprises.⁸⁵

Japanese automakers have entered the EC mainly through greenfield plants because of restrictions on imports of Japanese vehicles. They have also had difficulty in arranging successful joint ventures and in establishing distribution networks. Japanese firms' strategies in the EC appear to be a repetition of their strategies in the U.S. market, that is, shifting toward higher priced European plants to produce mass-market models.

Auto industry sources state that direct investment in the EC by Japanese auto companies will provide both a key market opportunity and an important challenge to U.S. auto parts firms with EC subsidiaries. Japanese-owned auto plants in the EC will create a new market for auto parts in the EC. Japanese auto companies typically place strong demands on their suppliers. U.S. auto parts subsidiaries in the EC will, however, likely face intense competition for the business of Japanese auto plants. Furthermore, Japanese parts firms with longstanding relationships to Japanese auto firms are entering the EC market. These firms and others expect to enter or to expand their presence in the EC largely through joint ventures with EC firms and

⁸⁰ "Will Japan Do to Europe What it Did to Detroit," *Business Week*, May 7, 1990, pp. 52-53.

⁸¹ Richard Johnson, "Peugeot and GM Lead European Productivity Gains," *Automotive News*, Aug. 13, 1990, p. 25.

⁸² Daniel T. Jones, "A Second Look at the European Motor Industry," paper from IMVP International Policy Forum, May 1989.

⁸³ Mr. Kim Clark, interview by USITC staff, May 22, 1990; Daniel T. Jones, "The Competitive Position of the European Motor Industry: The Race for Added Value," paper from the IMVP International Policy Forum, May 1988.

⁸⁴ Kevin Done, "World Automotive Components," *Financial Times*, May 16, 1990, p. 4.1.

⁸⁵ Kevin Done, "Gearing Up for Big Changes," *Financial Times*, June 8, 1989, p. 3.2; Daniel T. Jones, "The Competitive Position of the European Motor Industry"

⁷⁷ Representatives of General Motors Corp., interview by USITC staff, Detroit, MI, May 11, 1990.

⁷⁸ Kim Clark of the Harvard Business School, telephone interview by USITC staff, May 22, 1992.

⁷⁹ Peter Robinson, "Sales War Begins as European Market Slows Down," *Ward's Automotive International*, July 1990, p. 6.; Kevin Done, "West European Car Sales Stage a Recovery," *Financial Times*, Aug. 20, 1990, p. 4.

through licensing agreements, rather than through direct foreign investment.

The strategy for European producers has been focused on acquisitions and forming alliances, such as Ford-Jaguar, GM-Saab, Volvo-Renault, and Daimler-Benz-Mitsubishi, and the likely tie-up between Chrysler and Fiat. Such joint efforts are viewed as essential to reducing costs, combining financial resources, and broadening market offerings by teaming mass-market producers with those with more expensive models. With six major automakers and a variety of specialty producers in the EC, it is questionable if there will be room in the market for all the current producers.⁸⁵ With increasing competition and the anticipated entry of the Japanese into the market come growing concerns of overcapacity, predictions of an end to strong growth of EC auto sales, and the possibility of additional acquisitions, alliances, or mergers in the EC auto industry.

Within firms, production processes from vehicle conception to manufacturing are changing rapidly. Whereas U.S. automakers were forced to begin reorganizing their production processes in the 1980s because of intense Japanese competition in the U.S. market, EC automakers have as yet escaped the pressure of Japanese automakers in their protected home markets. EC automakers have been insulated from Japanese competition because of EC firms' limited presence in the U.S. market and, until recently, the lack of high-priced luxury cars offered by Japanese firms. Consequently, they have lagged behind the United States and Japan in adopting more flexible and efficient production methods.⁸⁷ Furthermore, EC automakers have not had the "learning situations" available to them that U.S. firms have had through their cooperation with Toyota, Mazda, and Mitsubishi.⁸⁸

Current changes in the EC auto industry production system essentially parallel those that occurred in the U.S. auto industry in the 1980s. The resulting impact on the auto-parts industry is substantial and is similar to the impact of changes that have occurred, and still are occurring, in the U.S. auto-parts industry. For example, buyer-supplier relationships are becoming more long-term and cooperative; automakers are relying on fewer primary suppliers; suppliers are responsible for greater engineering and design of auto parts; quality is increasing; and just-in-time

production systems are being adopted.⁸⁹ Although these changes are not entirely a result of EC integration, the trends are being accelerated by the integration process.⁹⁰

These developments may make it more difficult for U.S. producers to export to the EC, which would be consistent with what many industry researchers see as a trend toward regional auto industries to become more self-contained production systems, rather than a movement toward greater interregional trade in the industry.⁹¹ Consequently, most U.S. auto parts companies interested in the EC market have set up production facilities in the region rather than relying on exports.⁹²

EC Investment in the Eastern Europe Auto Industry

Recent political and economic changes in Eastern Europe have forced automakers around the world—and particularly those in the EC—to include Eastern Europe in their overall European strategies. Furthermore, as competition in the EC increases and as overcapacity becomes a greater threat, Eastern Europe may provide an important outlet for EC producers.⁹³ Thus, Eastern Europe warrants consideration in any discussion of current changes in the EC auto industry.

Auto industry experts indicate that annual new-car sales in Eastern Europe could double from the current level of 2 million units to 4 million units by the year 2000.⁹⁴ The accelerated demand for more automobiles in Eastern Europe presents an untapped market to global automobile manufacturers, especially those that already possess a base in the EC and those with the wherewithal to make rapid adjustments in their investment and marketing strategies to keep up with current demand. The current average East European auto stock is estimated at 67 cars per 1,000 people, as compared with 376 cars per 1,000 people in Western Europe.⁹⁵

United States and Japanese automakers will find it less risky to approach the East European market through EC member states. Following the

⁸⁵ Representatives of Ford Motor Co., interviews by USITC staff, Detroit, MI, May 11, 1990, and a representative of MEMA, May 14, 1990; Wyles, p. 2.1; Kevin Done, "World Automotive Components," *Financial Times*, May 16, 1990, p. 4.1; Kevin Done, "World Automotive Components," *Financial Times*, June 8, 1989, pp. 3.1 to 3.8).

⁸⁶ Mr. Kim Clark, Harvard Business School, telephone interview by USITC staff, May 22, 1990.

⁸⁷ James P. Womack, "Strategies for a Post-National Motor Industry," paper for IMVP International Policy Forum, May 1989; Kim Clark, Harvard Business School, telephone interview by USITC staff, May 22, 1990.

⁸⁸ Representative of the Motor Equipment Manufacturers Association, interview by USITC staff, May 15, 1990.

⁸⁹ Peter Robinson, p. 20.

⁹⁰ Ford of Europe President Louis Lataif's statement, "Blietzkrieg: West Makers Roar Into East Europe," *Automotive News*, Apr. 9, 1990.

⁹¹ *Ward's Automotive International*, "East Bloc Offers Enormous Market Potential to West," April 1990, p. 5.

⁸⁵ National Consumer Council, *International Trade and the Consumer*, Working paper No. 4, July 1990, p. 17.

⁸⁷ Daniel T. Jones, "A Second Look at the European Motor Industry," paper from the IMVP International Policy Forum, May 1989; James Womack, "Strategies for a Post-National Motor Industry," paper from the IMVP International Policy Forum, May 1989.

⁸⁸ Representatives of Ford Motor Co. and General Motors Corp., interviews by USITC staff, Dearborn, MI, and Detroit, MI, May 11, 1990; John Wyles, "Fiat Strategies Take on a Japanese Flavour," *Financial Times*, June 1, 1990, p. 3.1; Ferdinand Protzmann, "German Car Makers Defend Status," *New York Times*, Mar. 19, 1990, p. D1.

Alcatel NV, and Siemens (including Rolm). In 1989, 13 firms accounted for about 49 percent of the world market for telecommunications equipment. Eight of these firms were in Europe and three were in Japan. The telecommunications-equipment market in the EC is estimated to account for about 20 percent of the world market, but each of the member states has only a small share of the world market compared with that of the United States or even Japan. The demand for telecommunications equipment is derived from the demand for telecommunications services.

The three principal types of telecommunications equipment are switching, transmission, and terminal equipment. Switching equipment includes items such as central office switches and private branch exchanges (PBXs), which are used to route telecommunications traffic over either the public switched telephone network or within the network of a single firm. Transmission equipment includes items such as amplifiers/repeaters that are used to boost signals during transmission, and fiber-optic cables and copper wires over which the signals are carried. Terminal equipment includes items such as standard telephone sets or modems used for computer-to-computer communications over regular telephone circuits. Switching and transmission equipment are generally commercial products that are purchased by telephone companies, PTTs, or large firms seeking to establish an internal communications network. Terminal equipment also includes articles sold in the consumer market, such as standard telephone sets, cordless telephones, and telephone-answering machines.

Cellular telephone systems and other new technologies are increasing the flexibility of the existing telecommunications infrastructure and new developments in paging systems and personal communications networks are likely to provide consumers with a greater degree of mobility in the future. In addition, the development of integrated services digital networks (ISDN) and integrated broadband networks is likely to increase the capabilities and features of the telecommunications

system, especially as they relate to digital communications.

U.S. Industry and Market profile

Shipments, imports, exports, and employment data for the U.S. industry are provided in table 1.

U.S. Producers' Shipments

Telecommunications equipment as defined under section 1373 of the Omnibus Trade and Competitiveness Act of 1988 consists of products classified under 21 separate rate-line items in the *Tariff Schedules of the United States*. These items include telephone and telegraph apparatus, communications satellites, optical fibers, certain radio receivers and transceivers, transmitters, antennas, and certain other radiotelephonic and radiotelegraphic apparatus. U.S. shipments of these telecommunications products increased from about \$24 billion in 1984 to about \$29 billion in 1988, representing an annual growth rate of more than 5 percent. Shipments of telephone and telegraph equipment (SIC 3661), the largest segment, exhibited a lower growth rate during the period, resulting in this segment's decline relative to that of the total industry. In 1988, U.S. shipments of telephone and telegraph equipment accounted for 55 percent of total U.S. shipments of telecommunications equipment compared with 60 percent in 1984.

U.S. Producers

Although there are more than 2,000 U.S. firms producing telecommunications products, the industry is highly concentrated and dominated by a few large firms. According to the 1987 Census of Manufactures, firms which employed more than 1,000 workers, accounted for approximately 70 percent of industry shipments and slightly more than 60 percent of industry employment, although these firms account for only about 5 percent of the number of establishments in the industry. These figures reflect a reduction in the level of industry concentration compared with that of 1982, when the

Table 21-1
Telecommunications equipment: U.S. producers' shipments, imports, exports, apparent consumption, and employment, 1984-88

Year	U.S. producers' shipments	Imports	Exports	Apparent consumption	Ratio of imports to consumption	Employment
					Percent	
		Million ECU				1,000 workers
1984	23,785	3,054	1,972	24,867	12	226.6
1985	27,046	3,069	2,185	27,930	11	239.1
1986	26,633	3,474	2,369	27,738	13	219.6
1987	27,953	4,421	2,652	29,722	15	215.9
1988	29,464	5,816	3,303	31,977	18	214.1

Source: Estimated by the staff of the U.S. International Trade Commission based on official statistics of the U.S. Department of Commerce

CHAPTER 21
TELECOMMUNICATIONS SECTOR

CHAPTER 21

TELECOMMUNICATIONS SECTOR

Introduction

Telecommunications is likely to become one of the key factors in the successful integration of the EC member states into a competitive union. Telecommunications equipment and services revenues account for 2.5 percent of the European gross domestic product. The sector is also vital to Community growth and the economic health of the member states. The EC market for telecommunications equipment is expected to grow annually by 7 percent during 1990-93. In support of this anticipated growth, the EC has embarked upon a wide-ranging liberalization movement in both equipment and services and has issued directives to harmonize the disparate rules existing among the member states. Opening the EC telecommunications market to competition is likely to result in lower production costs, make the Community more competitive with the United States and Japan, and offer consumers a greater variety of services at lower costs. In the 1990s, 60 percent of the jobs in the EC may depend directly or indirectly on telecommunications.¹

Important features of the EC directives will have different effects on equipment producers and service providers in the telecommunications industry. For this reason, and to provide clarity in discussion the various implications of the directives, this chapter will focus on the telecommunications equipment sector.²

The deregulation of the EC telecommunications market is related in part to necessity. The fragmentation of the EC's telecommunications market has long been recognized as one of the principal factors preventing European firms from competing effectively in world markets. In addition, advances in transmission and switching technology have rendered a share of the EC telecommunications infrastructure outdated. The EC national telecommunications monopolies are witnessing a transition in market competition from vendor-driven technology advances to user-driven applications. The slow acceptance of the changing realities of the global market for telecommunications equipment and services by the EC member states could place them at a disadvantage with other countries.

¹ *European Report*, No. 1588 (May 12, 1990), Internal Market, p. 1.

² The basic telephone and telegraph services, which currently account for about 85 percent of international revenues, remain reserved to the national monopoly providers and are not subject to deregulation under the liberalized EC telecommunications market. Therefore, these services are not included in this report. The value-added services, including information services, which are going to be most open to foreign competition by the EC directives will be addressed in a subsequent EC 92 followup report.

The debate on the course of action the EC should follow in the field of telecommunications was initiated with the issue of the EC Commission's Green Paper on the development of the telecommunications sector: *Towards a Dynamic Economy - Green Paper on the Development of the Common Market for Telecommunications Services and Equipment* (Com (87) 290). The Green Paper emphasized that the strengthening of the European telecommunications infrastructure was necessary for the promotion of a competitive market throughout the Community and for achieving the completion of the Community-wide market by 1992.³ The Commission recommended the acceleration of the work on existing action lines to ensure the long-term convergence and integrity of the telecommunications network within the Community, the rapid achievement of mutual type approval for terminal equipment, and the opening up of public telecommunications procurement contracts to competition.⁴ Directives covering type approval of terminal equipment (Com (89) 289) and public procurement (Com (89) 380) have been proposed as a means for dealing with the latter two action lines.

In the Green Paper, the Commission proposed the following six new lines of action: (1) creation of the European Telecommunications Standards Institute (ETSI); (2) provision for a common definition of an agreed-on set of conditions for Open Network Provision (ONP) to service providers and users; (3) provision for the common development of Europe-wide telecommunications services; (4) provision for the common definition of a coherent European position regarding the future of satellite communications in the EC; (5) provision for the common definition of telecommunications services and equipment with regard to relations with non-EC countries; and (6) provision for the common analysis of the social impact. The progress on these six new lines of action includes the establishment of ETSI in April 1988, and a framework directive on ONP conditions approved in June 1990. A paper on satellite communications is being drafted and is expected to be released during 1990.

Telecommunications Equipment Industry

World Market

With respect to global demand, the world market for telecommunications equipment reached an estimated \$120 billion in 1989.⁵ Principal suppliers to the world market include AT&T,

³ EC Commission, *Towards a Competitive Community wide Market Telecommunications in 1992: Implementing the Green Paper on the Development of the Common Market for Telecommunications Services and Equipment*, Com (88) 48 final, Feb. 9, 1988, p. 5.

⁴ *Ibid.*

⁵ "Going Global," *Telephony*, Aug. 28, 1989, p. 39.

commercial opening of the East European market and considering the potential growth in auto sales in Eastern Europe, EC member states have recently adopted more aggressive strategies to produce and market their vehicles in Eastern Europe. Volkswagen, Fiat, Renault, Peugeot-Citroen, the Rover Group, and BMW all made preliminary arrangements to produce and/or sell their vehicles in Eastern Europe.

In addition, U.S. automakers have also made similar adjustments in their marketing plans in order to gain a foothold in the East European market. During 1989-90, General Motors Europe established joint venture operations in Hungary and in East Germany through its Adam Opel subsidiary. Ford of Europe has announced plans to establish a components plant in Hungary.⁹⁶ Similarly, Chrysler has established links with RAF in Latvia (USSR) and with the Uljanovsk Automobile Factory to produce jeeps and vans, and General Motors embarked on a \$1 billion joint venture with VAZ of the Soviet Union to supply Soviet-made cars with catalytic converters that in turn will be sold in the EC market.

In an attempt to build a closer presence to the EC market, Japanese automakers are currently furthering ties with the East European firms. Suzuki has established a joint venture to produce automobiles in Hungary. Daihatsu, Mitsubishi, Isuzu, and Toyota are currently negotiating agreements with East European automakers, especially those in Czechoslovakia, East Germany, and Poland.⁹⁷

The growing East European car market will have a positive impact on EC and U.S. sales of automobiles. Since East European specifications and emission standards are now closely patterned after Community standards, GM Europe and Ford of Europe are in especially good positions to increase sales.

Not all auto companies are hurrying into Eastern Europe. Ford has chosen to move slow in this market, predicting that economic turmoil will initially hinder auto sales. Company officials do not believe that a delayed entrance into the market will create long-term strategic disadvantages.⁹⁸

Outlook

Overall, U.S.-owned firms are well positioned for the changed environment that will be intensified with the removal of QRs. General Motors and Ford have long been considered by many to be the most pan-European auto companies in Europe, and, as long as they invest in existing

⁹⁶ Richard W. Bruner, "Ford Picks Hungary as Site for Parts Plant," *Automotive News*, July 16, 1990, p. 1.

⁹⁷ The mosaic of information on specific joint-venture operations was derived from recent (1st half 1990) "Regional Wrap Up" sections of *Ward's Automotive International*, as well as from the pages of *Automotive News*, and *Automotive Parts International*.

⁹⁸ Peter Fuhrman, "A Tale of Two Strategies," *Forbes*, Aug. 6, 1990, p. 42.

operations to meet the competitive environment, it appears that they should be able to adjust well.⁹⁹ U.S. auto-parts firms have a strong international focus, are technologically innovative, and have experienced industrial restructuring in the United States that is largely being replicated in the EC auto industry. Thus, U.S. automakers and parts subsidiaries in the EC should be able to adapt relatively well to the changes in the EC auto industry in the 1990s and to the increased competitiveness of EC suppliers.

The economic integration will likely stimulate some investment in the EC auto industry, particularly by Japanese firms. As discussed, U.S. automakers already have a strong presence in the EC, and a recent study by A.T. Kearney concluded that many U.S. parts suppliers are interested in further investment in the EC market.¹⁰⁰ Industry sources believe that there will not be much new investment by U.S. companies in the EC because most U.S. firms committed to the market have already invested there.

The long-term impact of EC integration is likely to be felt beyond the borders of the EC. The importance of globalization of operations will be experienced by EC-owned automakers as their home market becomes more open. While EC-owned automakers have a presence in many world markets, that presence remains relatively weak in the North American market, particularly for the volume producers Volkswagen, Fiat, Peugeot, and Renault. As EC-owned firms adjust to heightened competition in the EC, they will be forced to increase their presence in the U.S. market if they are to remain competitive in the long term.

There are already indications that EC-owned firms are increasing their focus on the U.S. market. For example, following the lead of Japanese firms, Volkswagen opened a design center in California. BMW has introduced the 318is to the U.S. market at the relatively inexpensive (for BMW) base price of \$21,500 to increase its presence in less expensive segments. The firm will soon introduce a 318i model for under \$20,000. Company officials have confirmed a Chrysler-Fiat tie-up, which would likely increase Fiat's presence in the United States. Both Mercedes-Benz and BMW have reorganized their sales operations in the United States to become more responsive to dealers and to more aggressively market their products in the United States. Virtually all EC-owned firms are revamping their product lines and will introduce more competitive products. Finally, strategic alliances and mergers among EC firms will increase their ability to invest in U.S. production facilities, although there are currently no known plans to do so. In the long term, U.S. automakers will not be insulated in the North American market from the effects of EC integration.

⁹⁹ James Womack, International Motor Vehicle Program, MIT, telephone interview by USITC staff, Apr. 12, 1990.

¹⁰⁰ A.T. Kearney, *Survey of the International Position of U.S. Automotive Suppliers*, summary of study, May 1989.

Census of Manufactures reported that firms with 1,000 or more employees accounted for 75 percent of shipments, 70 percent of employment, and 10 percent of the number of industry firms.

In its definition of the telecommunications sector, *Business Week* selected 37 major firms, which included both equipment manufacturers and services providers. Among the industry leaders in *Business Week's* survey were AT&T, the Regional Bell Operating Companies (RBOCs), GTE Corp., MCI Communications, United Telecommunications, and McCaw Cellular Communications. In 1989, sales of equipment and services by the 37 firms amounted to almost \$159 billion.⁶ The two largest telecommunications equipment producers in the United States are AT&T and Northern Telecom, a subsidiary of Bell Canada.

U.S. Employment

Employment in the U.S. telecommunications equipment industry decreased from an estimated 227,000 employees in 1984 to an estimated 214,000 employees in 1989, representing a decline of about 6 percent.⁷ About 73 percent of the employees in the industry were production and related workers, and the remainder included marketing, engineering, and management personnel. The decline in employment resulted from efforts by the industry to reduce costs in response to increased competition. Advances in technology have also had a negative impact on employment as companies move more toward automated methods of production.

U.S. Investment

New capital expenditures by the U.S. telecommunications industry amounted to an estimated \$1.1 billion in 1987, with approximately 50 percent of this amount made by firms in the telephone and telegraph sector (SIC 3661).⁸ Capital investment in the telecommunications-equipment sector increased from about \$21 billion in 1984 to about \$24 billion in 1989. A major share of the investment was accounted for by customer premises equipment, switching apparatus, and transmission apparatus. The assets of the U.S. firms that *Business Week* listed in the telecommunications industry were valued at \$285 billion in 1989.⁹

Based on U.S. Department of Commerce data, U.S. investment in the EC in the radio, television, and communication industries, which includes the

⁶ "U.S. Companies Ranked by Industry," *Business Week*, Apr. 13, 1990, p. 242.

⁷ Estimated by the staff of the U.S. International Trade Commission based on official statistics of the U.S. Department of Commerce.

⁸ Estimated by the staff of the U.S. International Trade Commission based on the U.S. Department of Commerce, 1987 *Census of Manufactures, MC87-1-36D, Communication Equipment, Including Radio and Television, Industries 3651, 3652, 3661, 3663, and 3669*, June 1990.

⁹ "U.S. Companies Ranked by Industry," *Business Week*, Apr. 13, 1990, p. 242.

telecommunications industry, amounted to an estimated \$11 billion in 1987.¹⁰ U.S. investment in the EC telecommunications industry has grown since that time, with large investments by AT&T and other U.S. telecommunications firms. In addition, ITT Corp. has a 37-percent equity interest in Alcatel NV, the largest telecommunications firm in the EC. ITT announced that it would lower its stake in Alcatel to 30 percent but would retain this level of investment in anticipation of the developing market in Eastern Europe.¹¹ Total U.S. investment worldwide in the radio, television, and communication industries amounted to almost \$15 billion in 1987, making the EC, which accounts for over 70 percent of U.S. foreign investment, the largest recipient of U.S. telecommunications investment.

U.S. Imports

U.S. imports of telecommunications products increased from \$3.1 billion in 1984 to \$5.8 billion in 1988, or by 87 percent. Japan was by far the largest supplier to the U.S. market during the period, accounting for 44 percent of U.S. imports in 1984 and 39 percent in 1988. Canada was the second-largest supplier, accounting for 10 percent of U.S. imports in both 1984 and 1988. Conversely, the EC remained a relatively small supplier during the period, accounting for 3 percent of U.S. imports in 1984 and 6 percent in 1988. The ratio of U.S. imports to apparent U.S. consumption increased from 12 percent in 1984 to 18 percent in 1988.

The principal products imported into the United States include facsimile machines, parts for radio telephonic and telegraphic transmission and reception apparatus, feature and cordless telephone sets, and telephone answering machines. Many of these products are sold in the consumer market and are no longer produced in the United States. Facsimile machines are the largest single imported item, accounting for 16 percent of the total value of imports of telecommunications equipment in 1988. Telephone sets and parts were the largest import product group in 1984, accounting for 20 percent of the value of total imports of telecommunications equipment.

U.S. Exports

U.S. exports of telecommunications products increased from about \$2 billion in 1984 to more than \$3 billion in 1988, or by 67 percent. The EC member states provided the largest foreign market for U.S.-produced equipment, accounting for 17 percent of U.S. exports in 1984, and increasing to 20 percent in 1988. The United Kingdom was the largest country market for U.S. exports within the EC, accounting for almost 8 percent of total U.S.

¹⁰ Estimated by the staff of the U.S. International Trade Commission based on data contained in U.S. Department of Commerce, *U.S. Direct Investment Abroad, Preliminary 1987 Estimates*, table 4.

¹¹ "ITT To Sell Part of Its Stake in Alcatel to CGE for \$640M," *Electronic News*, June 18, 1990, p. 18.

exports. West Germany was the second-largest EC country market, accounting for more than 3 percent of total U.S. exports. The ratio of U.S. exports to U.S. domestic shipments increased from 8 percent in 1984 to 11 percent in 1988. The largest foreign market for U.S. exports during the period was Mexico, which accounted for an average of 12 percent of U.S. exports each year during 1984-88. Canada was the second-largest foreign market, accounting for about 11 percent of U.S. exports in both 1984 and 1988. Japan represented a small but growing market for U.S. products during the period, accounting for 3 percent of U.S. exports in 1984 and 7 percent in 1988.

The principal products exported by the United States are parts for radio-telephonic and telegraphic transmission and reception apparatus, telephone switchboard and switching equipment, and miscellaneous telephonic equipment and parts. These products tend to be sold in commercial or industrial markets in contrast to U.S. imports, which are sold in the consumer market. Parts for radiotelephonic and telegraphic apparatus were the largest single exported item, accounting for about 42 percent of the value of U.S. exports in 1988.

EC Industry and Market Profile

Shipments, imports, exports, and employment data for the EC industry are provided in table 2.

EC Producers' Shipments

EC shipments of telecommunications products increased from almost 16 billion ECU in 1984 to more than 17 billion ECU in 1988, representing an annual growth rate of slightly more than 2 percent. Shipments of switching equipment accounted for more than 50 percent of EC industry shipments in 1987, transmission equipment accounted for about 22 percent, and shipments of terminal equipment, such as telephone sets, accounted for the remainder.¹² The post, telegraph, and telephone

¹² "Telecommunications Equipment," *Panorama of EC Industry—1989*, p. 12-6.

Table 21-2

Telecommunications equipment: EC producers' shipments, imports, exports, apparent consumption, and employment, 1984-88

Year	U.S. producers' shipments	Million ECU		Apparent consumption	Ratio (percent) of imports to consumption	Employment
		Imports	Exports			
1984	15,693	2,659	4,404	13,948	19	250.5
1985	17,056	3,200	4,770	15,486	21	236.9
1986	16,930	3,052	4,285	15,697	19	220.8
1987	17,203	3,586	4,615	16,174	22	217.6
1988	17,281	3,686	3,782	17,185	21	208.5

¹ Estimated by the staff of the U.S. International Trade Commission.

Source: "Telecommunications Equipment," *Panorama of EC Industry—1989 and Intra-EC and Extra-EC Trade Flows in Telecommunications Equipment in 1988*, XIII/208(89)-E—final, XIII.D.2 Telecommunications Policy, Regulatory aspects, Analyses and Sector Studies, June 1989.

administrations (PTTs) are the principal customers for EC telecommunications manufacturers, purchasing about two-thirds of industry output.¹³

EC Producers

There are more than 1,000 manufacturers of telecommunications equipment in the EC; however, the industry is concentrated, with the top 10 firms accounting for over 80 percent of Community production. The two largest firms in the EC are Alcatel and Siemens, which are estimated to account for 40 to 50 percent of total EC production.¹⁴ EC producers supply much of the switching and transmission equipment purchased in the Community, but a large percentage of terminal equipment items, such as facsimile machines or inexpensive consumer telephone sets, is supplied by imports, principally from Pacific Rim countries. U.S. firms with operations in the EC include AT&T, with facilities in the Netherlands and a 20-percent interest in the Italian state-owned telecommunications group Italtel, and ITT with its major equity position in Alcatel.¹⁵

EC Employment

Employment in the production of telecommunications equipment in the EC decreased from 251,000 employees in 1984 to 208,000 employees in 1988, representing a decline of about 4 percent per year. The decline in EC employment is largely a function of technological advances, as telecommunications equipment moves from electromechanical to electronic analog and digital technology.¹⁶ Production of advanced equipment

¹³ *Ibid.*, p. 12.5.

¹⁴ "Telecommunications Equipment," *Panorama of EC Industry—1989*, p. 12-8.

¹⁵ Keith Rockwell and Bruce Barnard, *One Europe: 1992 and Beyond*, 1989, p. 104.

¹⁶ "Telecommunications Equipment," *Panorama of EC Industry—1989*, p. 12-7.

based on digital technology is more easily automated, which has contributed to the decline in employment. Also, a slowdown in network construction has had a negative impact on the level of employment.¹⁷ The declining trend in employment is expected to continue with technological advances and increased industrial restructuring.

EC Investment

Investment in telecommunications in the EC amounted to more than 22 billion ECU in 1986. Approximately 25 percent of this investment was made in telephone switching equipment.¹⁸ Although the total level of investment by all the EC member states in the United States cannot be determined, Siemens (West Germany) has made major investments in the U.S. market in an attempt to become the third supplier to the RBOCs behind AT&T and Northern Telecom. European suppliers have generally regarded the standards adopted by the RBOCs as barriers to entry to the U.S. market.

EC Imports

The principal sources of EC imports of telecommunications equipment in 1988 were Japan with 1.2 billion ECU (33 percent) and the European Free Trade Area (EFTA) countries with 950 million ECU (26 percent). The United States was the EC's third-leading supplier of imports in 1988, with 819 million ECU, or 22 percent of the total.¹⁹ In 1984, the positions of the United States and Japan were reversed with the United States accounting 1.0 billion ECU, or about 38 percent of EC imports and Japan accounting 459 million ECU, or 17 percent.²⁰ The reversal reflects an 18-percent decline in imports from the United States from 1984 to 1988 coupled with an increase in imports from Japan of 166 percent during the period.

EC imports of terminal equipment amounted to 1,977 million ECU, or about 54 percent of the value of total imports in 1988. Within the terminal equipment group, imports of facsimile machines amounted to more than 710 million ECU, accounting for more than 30 percent of all terminal equipment imports and over 20 percent of total imports of telecommunications equipment. Japan was the principal source of facsimile machines, supplying facsimile machines worth 653 million ECU in 1988. These machines represented

¹⁷ Organization for Economic Cooperation and Development, *The Telecommunications Industry: The Challenges of Structural Change*, Paris, 1988, p. 80.

¹⁸ Herbert Ungerer, *Telecommunications in Europe*, (Luxembourg: Office for Official Publications of the European Communities, 1988), p. 29.

¹⁹ EC Commission, Directorate General XIII, *Intra-EC and Extra-EC Trade Flows in Telecommunications Equipment in 1988*, XIII/208(89)-EN-final, XIII.D.2 Telecommunications Policy, Regulatory Aspects, Analyses and Sector Studies, June 1989, p. 6.

²⁰ *Ibid.*, p. 27.

more than 50 percent of the value of total EC imports of telecommunications equipment from Japan in 1988. Imports of transmission equipment amounted to 722 million ECU in 1988, representing about 20 percent of the total. The United States was the principal supplier of transmission equipment to the EC market, accounting for about 45 percent of EC imports in this category. Imports of switching equipment were valued at 511 million ECU, or about 14 percent of the total. EFTA countries were the leading sources of EC imports of switching equipment, supplying about 195 million ECU, or 38 percent of such imports.²¹

Intra-EC trade in telecommunications equipment totaled about 3.3 billion ECU in 1988, almost equaling the level of trade the Community conducts with the rest of the world. Trade in transmission equipment accounts for almost 40 percent of intra-EC trade, and trade in terminal equipment accounts for just under 30 percent of the total. Switching equipment and other miscellaneous equipment account almost equally for the remaining 30 percent of intra-EC trade.²²

EC Exports

EC exports of telecommunications equipment generally fluctuated downward during 1984-88, with exports in 1988 reaching the lowest level for any year during the period. The principal export markets for EC products in 1988 were the EFTA countries, which absorbed 1,038 million ECU, or 27 percent, and the United States, which absorbed 412 million ECU, or 11 percent. The relative importance of the EFTA countries as an export market for EC products increased steadily during the period. In 1984, the EFTA countries accounted for only 18 percent of EC exports, but this percentage rose during each subsequent year. The United States represented a small market for EC exports during the period both in relative and absolute terms. In 1984, the United States accounted for only 8 percent of EC exports.²³

Terminal equipment was the principal EC export item in 1988. Exports of terminal equipment in 1988 were valued at 1,530 million ECU, which accounted for 40 percent of total exports in that year. Exports of transmission equipment were the second leading export item, accounting for 1,164 million ECU, or slightly more than 30 percent of the total. Exports of switching equipment accounted for 555 million ECU, or about 15 percent of total exports. The remaining 15 percent of EC exports were miscellaneous telecommunications products.²⁴

²¹ *Ibid.*

²² *Ibid.*, p. 52.

²³ *Ibid.*

²⁴ *Ibid.*, p. 51.

Possible Impact From the EC 92 Program

As currently developed, the possible impact of the EC 92 program on the U.S. telecommunications industry is concentrated in the areas of standards, competition policy, and public procurement. Major changes in the structure of the telecommunications sectors of the member states will take place in these areas, which in turn, could affect market conditions and the cost of doing business in the EC for foreign-produced products.

Standards

The EC Commission has recommended a policy to establish Europeanwide open network standards that are likely to provide equal opportunity for all market participants.²⁵ Europeanwide standards will also become a key factor in public procurement liberalization and the ongoing deregulation of the telecommunications services market. The EC approach to telecommunications standards is to ensure "interoperability," which contrasts with the U.S. position of "no harm to the network." The EC standards directives covering mutual recognition of type approval of terminal equipment and the Open Network Provision (ONP) of access to the network infrastructure are likely to have the greatest impact on the U.S. industry.

Terminal Equipment

Background

Council Directive 86/361/EEC introduced the initial stage of mutual recognition of type approval for telecommunications terminal equipment and anticipated full mutual recognition. Such equipment includes telephone sets, modems, and private branch exchanges (PBXs). The Green Paper views full, mutual type-recognition of terminal equipment as vital to the development of a competitive Communitywide market in terminal equipment. Council Resolution 88/C 257/01 of June 30, 1988, on the development of a common market for telecommunications services and equipment, considered full, mutual recognition of type approval for terminal equipment a major goal of telecommunications policy. All of these documents have recognized that the EC telecommunications sector is one of the industrial mainstays of the Community and that the terminal equipment sector is a vital part of the telecommunications sector. The proposed directive on the full mutual recognition of type approval for terminal equipment (Com (89) 289) represents the most recent step in this process.²⁶

²⁵ Green Paper, p. 5.

²⁶ See U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States First Follow-Up Report* (Investigation No. 332-267), USITC Publication 2268, March 1990, pp. 6-107 to 6-109.

Mutual recognition of type-approval for telecommunications terminal equipment would permit the sale of these telecommunications products in the 12 member states after 1 member state certifies that the equipment is in compliance with the essential requirements of the directive. This process would eliminate the requirement to have each member state certify that telecommunications equipment is in compliance before it can be sold in that market, thus reducing the burden on U.S. firms who wish to market their products in the EC.

Member states are to take the necessary steps to ensure that the terminal equipment placed on the market complies with the essential requirements laid down in the directive. These requirements include ensuring safety of users and employees of public networks, protecting the network from harm, and the interworking (i.e., compatible functioning) of terminal equipment with network equipment for the purpose of making or charging for connections. Compliance with some of the harmonized standards that have been developed will be made mandatory by the EC Commission following consultation with a newly established Approvals Committee for Telecommunications Equipment (ACTE). Terminal equipment is to be certified as being in conformity by either an EC type-examination or an EC declaration of conformity. Although manufacturers may indicate that their equipment is in compliance with the directive by providing a "CE" mark of conformity, the directive appears to require that all equipment must be first type approved by "notified bodies," which have been designated by the member states for this purpose. A certificate of conformity issued by a "notified body" in one member state will serve as an indication that the terminal equipment conforms to national conformity specifications and is sufficient in that a second member state shall not impose a requirement for repetition of tests.

The adoption of a common standard for the certification of terminal equipment applicable in all EC member states is likely to make it easier for U.S. manufacturers to design and produce equipment for that market and provide U.S. manufacturers with increased economies of scale in production. There is a likelihood that certain U.S. "bodies" may become "notified bodies" (i.e., U.S. testing laboratories may be allowed to certify that equipment meets EC specifications). But this is not likely to take place until after the EC has concluded a formal arrangement with the United States.

U.S. Industry Views

The U.S. industry endorses three central elements of the directive. First, the full mutual recognition of type approval of terminal equipment is essential to the establishment of a single internal market for terminal equipment and the elimination of barriers to trade in terminal equipment. Second, the industry endorses the principle of the "declaration of conformity" procedures that provide

for self certification by manufacturers. In addition, the industry believes that some modifications in the directive would allow manufacturers to bring their products to market more quickly and to exploit new and emerging technologies. Third, the industry supports the provision in the directive under which "notified bodies" in the EC would recognize documentation issued by appropriate bodies in third countries, when agreements to do so exist between the EC and third countries. Such action would be mutually beneficial for trade in terminal equipment.

U.S. industry concerns about the directive include certain aspects of the certification process and the extent of equipment coverage. The documentation required by the directive appears to be unnecessarily broad, going beyond that needed to determine an item's conformity with the essential requirements. The proposed "EC surveillance," which calls for onsite inspections of facilities and documents is likely to be costly and to deter manufacturers from employing the self-certification procedures outlined in the directive, thereby negating one of its potential benefits. The definition of "terminal equipment" is overly broad and covers a variety of devices and components that have no bearing on the essential requirements set out in the directive. Finally, the inclusion of "interworking" within the essential requirements could slow down the conformity process and stifle innovation. The U.S. industry feels that limiting the essential requirements to user safety, safety of network personnel, and protection of the network from harm would be sufficient.

At its April 1990 Plenary Session, the European Parliament described the proposed directive on type approval for telecommunications terminal equipment as "too vague." The Parliament supported the initiative, but attached a number of amendments designed to clarify the wording of the text.²⁷ In particular, the Parliament called for a clarification of the definition of a "telecommunications terminal" and of the requirement, in "justified cases," for the interworking of the equipment.²⁸ The International Chamber of Commerce (ICC) also criticized the wide definition of terminals and the definition of "interworking" contained in the proposal. The ICC contends that the proposed directive would actually increase costs and make the system more costly for industries while protecting the monopolistic control of national PTTs.²⁹

Open Network Provision

The Open Network Provision (ONP) directive³⁰ is part of the process of harmonization and

²⁷ *European Report*, No. 1578 (Apr. 7, 1990), Internal Market, p. 9.

²⁸ *EC-Business Report*, May 1, 1990, p. 11.

²⁹ *European Report*, No. 1589 (May 16, 1990), Business Brief, p. 4.

³⁰ See USITC, *The Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-106 to 6-107.

liberalization in the telecommunications sector initiated under the Green Paper. The directive lays down criteria for establishing ONP conditions. These criteria address the conditions of access to the network infrastructure for competitive telecommunications service providers (such as those offering value-added telecommunications services), and the procedures that national telecommunications authorities/carriers are to follow in providing access to the infrastructure. ONP conditions are to be defined in stages, and to be followed by future directives relating to specific areas, such as leased lines, packet- and circuit-switched data services, integrated services digital network (ISDN), voice telephony, mobile services, and broadband network resources.

The principle of the ONP directive has been welcomed by large segments of the U.S. business community. However, there are concerns about inadequate definitions of ONP conditions for technical interfaces, supply and usage conditions, and tariff principles that might apply to users and private service providers. Therefore, it is difficult to determine the potential impact of the directive, but the ONP conditions which may be applied to such private service providers should not be as stringent as those applied to the PTTs. The business community is also concerned that the ONP conditions may delay the creation of an open market for competitive telecommunications services.³¹ These issues will be addressed in greater detail in a subsequent EC 92 followup report.

The Council of Ministers formally adopted a "common position" on the ONP directive in February 1990. A major feature of the revised proposal for the ONP directive is that technical interfaces and service features will become the subject of European standards to be adopted by the European Telecommunications Standards Institute (ETSI). The standards will be voluntary, but the Commission can make reference to a particular standard mandatory in order to guarantee the interoperability of transfrontier services. Service providers that comply with voluntary standards will be able to offer their services throughout the Community. The ONP directive (Com (90) 387) was approved during the June 28, 1990 meeting of telecommunications ministers and will go into effect on January 1, 1991.³²

Electromagnetic Compatibility and Broadcasting Directives

Electromagnetic Compatibility

The standards directives on electromagnetic compatibility (EMC)³³ and television

³¹ American Chamber of Commerce in Belgium, *Business Guide to EC Initiatives*, Spring 1990, p. 83.

³² U.S. Department of State Telegram, "EC Telecommunications Council June 28: The Results," June 1990, Brussels, Message Reference No. 09935.

³³ See USITC, *The Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-109 to 6-112.

broadcasting³⁴ may have an influence on U.S. participation in the EC market. The concept of electromagnetic compatibility refers to the ability of a device to function satisfactorily in its electromagnetic environment without introducing intolerable electromagnetic interference to other electrical equipment within its environment.³⁵ The EMC concept is broader than the concept of radio frequency interference used in U.S. regulations and could require that U.S. manufacturers modify their products before they are marketed in the EC. The EC intends to have CENELEC establish, draft, and create harmonized standards at the European level for EMC. Products complying with the standards will be assumed to comply with the essential protection requirements outlined in the directive. The product coverage is very broad, covering almost any electrical item that might emit electromagnetic interference, or be affected by it.

In the telecommunications area, products such as mobile radio and commercial radiotelephone equipment and telecommunications network apparatus could be affected by the requirements of the directive. Also, the EMC directive would be the first directive to require third-party testing and, as a result, could adversely affect U.S. laboratories, according to Charles Ludolph, Director of the U.S. Department of Commerce's Office of European Community Affairs, in testimony at a hearing before the Small Business Export, Tax Policy and Special Problems Subcommittee on April 30, 1990.³⁶

Broadcasting

The broadcasting directive calls for a majority proportion of television transmission time (exclusive of news, sports events, games, advertising, and teletext services) to be reserved for European works where practicable. The directive stipulates that movies cannot be broadcast within 2 years of their theatrical release unless otherwise agreed upon between the movie's rights holders and the broadcaster. In the case of cinematographic works coproduced by the broadcaster, this period shall be limited to 1 year. The directive also places such limits on televised advertising as the duration of advertising, the number of times advertising is permitted to interrupt a program, the product or service being advertised, and the content of the advertising.

The number of television stations in Europe increased from 28 in 1980 to 68 in 1989, and soon after 1990, it is expected that 100 stations will be in operation. Industry sources claim there is likely to be an extra 200,000 hours of air time available each year, of which an estimated 16,000 hours will be

prime-time sitcoms and drama. The French Government indicates that Europeans can only provide 2,500 hours of "prime-time fiction" to fill these hours, and therefore must buy the remainder. The most likely source for additional programming is the United States.

U.S. companies, such as NBC, are negotiating with potential partners in the EC, while other U.S. companies have already established partnerships. However, industry sources indicate that these investments are not the result of the directive and were in process before the directive was first discussed. U.S. companies hold majority positions in many of their investments in the EC, and while they are likely to be willing to increase their investment in the EC, they are not likely to give up control.

U.S. producers are mixed in their predictions for the long-term effects of the directive on the U.S. industry. Some producers feel that because of the growing demand for programming in the EC, and for U.S. programming in particular, the directive may not have a long-term negative effect on the U.S. industry. Others feel that any directive that limits the options of U.S. producers in the EC is detrimental. These producers feel that such a quota as called for by this directive may set a precedent for broadcasting industries in other countries and perhaps for their theatrical industries as well.

In a statement provided to the U.S. International Trade Commission, the Motion Picture Association of America (MPAA) reported that the EC market accounts for a majority of the foreign revenues of MPAA member companies and that the directive will extend restrictions to member states that do not currently have them. The MPAA statement indicates that, "It (the directive) will also immediately freeze the proportion of telecast time allocated to EC and non-EC programming at 1988 levels with all the readily apparent implications for telecasters' purchasing policies. It will not affect the more restrictive national quotas already in place in France and the United Kingdom. The EC quota provision establishes a minimum, leaving the member states free to impose higher quotas for EC program material. Since adoption of the EC Quota Directive, France has tightened its quota restrictions against U.S. programming." The MPAA statement indicates further that, "Finally, the imposition of an EC Quota merely sets the stage for more protectionist measures at a later date. Specific numerical quotas could be next. Also if these restrictions are tolerated in the quota area, it cannot be discounted that additional onerous requirements such as special duties and levies non-EC audio-visual material could follow."

³⁴ Ibid, pp. 6-112 to 6-115.

³⁵ Ibid, p. 6-109.

³⁶ "EMI Testing by European Labs Seen as Lever for U.S. Labs," 1992—*The External Impact of European Unification*, May 4, 1990, p. 3.

Public Procurement

In the area of public procurement,³⁷ public organizations spend approximately 15 percent of the Community's GDP per year, and thus have a major influence on the economy. The level of trade in the excluded sectors is below that of trade in other sectors of the European economy. Open procurement would allow the industries in the excluded sectors, including the telecommunications sector, to purchase the best products that the market can offer.³⁸ Open procurement procedures will be nondiscriminatory, free from unlawful influences, and based on commercial criteria.³⁹ The "excluded sectors" directive, which covers telecommunications because it is one of the sectors not subject to EC-wide or international procurement rules, is important because of the level of telecommunications procurement controlled by the PTTs. For example, about \$5 billion of the approximately \$8 billion in telecommunications equipment purchased in West Germany in 1989 was purchased by the Bundespost, West Germany's telecommunications authority.⁴⁰ Similar procurement levels exist for other member states.

Although the EC has advocated a policy that would open up national markets for telecommunications equipment procurement, actual progress has been limited. In West Germany, the Bundespost awarded 99.5 percent of its contacts to national firms during 1984-88. In France, the United Kingdom, the Netherlands, and Portugal, 100 percent of telecommunications procurement contracts went to national firms.⁴¹ Opening up public procurement in the telecommunications sector would give U.S. firms potential access to one of the largest sectors in the EC telecommunications market.

U.S. industry concerns with the "excluded sectors" directive include the 50-percent value-added rule for the definition of an EC product and the 3-percent price preference given to Community products.⁴² Difficulty with the 50-percent value-added rule is compounded by the fact that the method of calculating local content for the purposes of public procurement remains unclear. The 50-percent value rule can also affect the flow of capital, as companies invest in EC operations in order to meet the local content requirements.⁴³ Further, EC officials have said that

³⁷ See USITC, *The Effects of EC Integration*, USITC Publication 2204, July 1989, pp. 4-18 to 4-19 and 4-43 to 4-44.

³⁸ EC Commission, "Public Procurement Procedures for Water, Energy, Transport and Telecommunications Services," Press Release, June 22, 1988.

³⁹ Reinhard Schulte-Braucks, "Telecommunications Law and Policy in the European Community," *Fordham International Law Journal*, vol. 13, No. 2, 1989-90, p. 243.

⁴⁰ Claude Fontheim, "The European Telecommunications Equipment Market," paper prepared for AEI conference on the United States and Europe in the 1990s, Mar. 5-8, 1990, p. 13.

⁴¹ See USITC, *The Effects of EC Integration*, USITC publication 2204, July 1989, p. 4 18.

⁴² For more information, see ch. 6 of this report.

⁴³ U.S. Council for International Business, *The European Single Market*, March 1990, p. 29.

there may be a difference between the "contract price" and the contract "value."

Competition Policy

In the area of competition policy, the EC has taken steps to open up the market to new competitors in the terminal equipment and services markets so that the Community can react more quickly to technological, economic, and world-market trends. There are also indications that the EC seeks to separate the regulation of the telecommunications network from its operation so that the telecommunications administrations would not be both the regulator and the operator of the infrastructure. However, the telecommunications administrations would be allowed to participate as a competitor in the newly emerging liberalized markets for services and terminal equipment.⁴⁴

In May 1988, the EC Commission issued a directive under article 90 to liberalize the market for telecommunications terminal equipment.⁴⁵ In the article 90 process, the EC Commission may issue a directive on the basis of the competition rules of the Treaty of Rome without first having the directive approved by the Council of Ministers and the European Parliament. After the EC Commission issued the telecommunications terminal equipment directive, the French Government sued the EC Commission on the grounds that it had overstepped its bounds by using article 90 to deregulate the market for terminal equipment. In February 1990, the advocate general issued an advisory opinion, ruling against the EC Commission's use of article 90. A final ruling by the Court of Justice on this case has not been issued.

The outcome of the case on the terminal equipment directive may have an impact on the directive to liberalize telecommunications services that was also issued as an article 90 directive by the EC Commission. The directive on telecommunications services, Com (90) 703 final, imposes the obligation on member states to limit the public network operator's monopoly to voice and telex services. The directive also requires the separation of regulatory bodies from the public network operators in order to ensure nondiscriminatory enforcement. The EC Commission issued the article 90 directive on telecommunications services as a complement to the ONP directive. The article 90 directive on telecommunications services was officially notified to the member states on July 13, 1990 after approval of both the telecommunications services and ONP directive was reached at the June 28, 1990, meeting of telecommunications ministers. The use of article 90 process by the EC Commission emphasizes its strong determination to liberalize the EC market for telecommunications equipment and services. A ruling against the EC Commission on the terminal equipment directive by the court could slow down

⁴⁴ Green Paper, p. 13.

⁴⁵ See USITC, *The Effects of EC Integration*, USITC Publication 2204, July 1989, pp. 9-20 to 9-23.

this deregulation process and force the EC Commission to rely more on the article 100A process, which requires the cooperation of the Council of Ministers and the European Parliament, rather than on the article 90 process. Industry analysts are concerned that the article 100A process could result in further changes to the substance of the telecommunications services directive.

Outlook

The overall impact of EC economic integration on the U.S. telecommunications industry appears to be beneficial. In the area of standards, the harmonization of type approval for terminal equipment is expected to reduce the costs U.S. firms incur in marketing their products in the EC. Similarly, with harmonization of the conditions of usage, tariff principles, and network interfaces, the ONP directive is expected to aid in the development and provision of transfrontier telecommunications services. However, the EMC directive may impact on the U.S. industry's ability to do business in the EC because of the difference between U.S. and EC regulatory concepts (i.e., radio frequency interference versus electromagnetic compatibility). The U.S. industry has mixed views on the long-term impact of the broadcasting directive. Some industry members feel that there will be no long-term negative effect because of the growing demand for programming; others, however, feel that any directive that limits the options of U.S. producers would be detrimental. In the area of public procurement, the opening up of this market is expected to benefit U.S. firms because of the amount of telecommunications equipment that the PTTs purchase each year. Finally, in the area of competition policy, the outcome of the court case on the article 90 directive on liberalizing the market for telecommunications terminal equipment could have an impact on the article 90 directive liberalizing the market for telecommunications services.

Public Testimony and Statements of U.S. Industry Associations

The U.S. International Trade Commission held a public hearing on June 21, 1990 on the effects of European integration on the United States. Mr. Edwin B. Spievack, President of the North American Telecommunications Association (NATA), testified at this hearing. NATA represents more than 600 members that manufacture and distribute state-of-the-art telecommunications equipment. Major European and Asian manufacturers are members of NATA in addition to those of the United States. Mr. Spievack indicated at the hearing that the European market was closed to U.S. telecommunications products, and that the situation in the EC was not likely to improve with economic integration in 1992.⁴⁶ He indicated that

⁴⁶ North American Telecommunications Association, Statement, June 21, 1990, p. 1.

U.S. exports to Europe amount to about 2 to 2.5 percent of the total telecommunications construction budget each year and that this percentage has remained fairly steady over time. According to Mr. Spievack, the European telecommunications market represents a totally managed environment, and that the market is controlled by the PTTs, which are tied in turn to manufacturing conglomerates through relatively imperturbable relationships that act to keep competing products out of the market. Mr. Spievack reported that privatization is no guarantee of competition and pointed out that when the telecommunications system was privatized in the United Kingdom, the new private monopoly simply took over from the old public monopoly.

According to Mr. Spievack, from Europe's perspective, the United States is entitled to export plants and employment, take advantage of tax incentives and cheap labor, and transfer U.S. technology as it wishes. U.S. telecommunications plants in Europe will be treated similarly to their European counterparts. Each will receive a guaranteed production allocation from the governmental authority in exchange for agreeing to a fixed level of employment, but importing will not be the accepted way of doing business.

The rules of understanding in the member states effectively bar U.S. telecommunications trade with Europe, according to a statement provided by Mr. Spievack. The distribution of telecommunications products in Europe is principally controlled by the PTTs, or through monopoly concessions granted by the PTTs. A product cannot be distributed unless it is certified for distribution by the government ministry, or its designated certification agency. Certification establishes design standards for equipment that will be connected to the telecommunications network. Thus, certification can affect the design and indirectly the technology that is connected to the network. The certification process can be used to limit the introduction of new technology or innovation.

In contrast, U.S. rules, or "interface standards," specify electrical voltages, signaling parameters, noise levels, and related characteristics that equipment must meet at the point of contact with the network. Manufacturers are free to employ whatever technology they wish provided that these interface standards are met. Thus, U.S. manufacturers can innovate and use new technologies in their telecommunications products without having to be concerned with meeting design standards as they do in Europe.

It is possible to set up independent distribution channels in some countries, according to Mr. Spievack's statement. These situations arise when the product is certified for connection to the network, but has not been certified for distribution through the government monopoly. In such cases, U.S. products could be sold through independent distributors, but according to the statement, this

method carries with it a cultural stigma: not being supplied through the official channel. According to Mr. Spievack's testimony at the hearing, in France and West Germany and in most of Spain, products are distributed through the government. A dual distribution system exists in Italy.⁴⁷

Mr. Spievack testified that he felt that the impact of EC 92 on the U.S. telecommunications industry will be minimal. The United States will continue to export about 2 to 2.5 percent of the annual telecommunications construction budget and import about 1.6 percent of the U.S. construction requirement.⁴⁸ As to access to the European market, Mr. Spievack indicated that he did not think that there was any difference between large and small firms; both face similar difficulties in getting to the European market. Large firms had more money to put into the effort, but according to Mr. Spievack, even the largest American firms were not at a significant level of business in Europe.⁴⁹

The Telecommunications Industry Association (TIA), which represents more than 500 manufacturers of telecommunications equipment, also filed a statement with the U.S. International Trade Commission concerning the instant investigation. The TIA views the EC 92 process as a "two-edged sword." The opportunities provided by the opening of the European market are numerous; however, a unified European market could exacerbate problems for U.S. firms, if such buy-national policies, which U.S. business currently face in the EC, are extended to the unified EC market. U.S. manufacturers with European subsidiaries are likely to benefit from the EC 92 process, but it is unclear just how U.S. exports to the EC will be affected by EC 92. The goal of TIA's members is to compete with European companies regardless of the location of manufacture. TIA wishes to ensure that U.S. companies not presently in Europe do not have to establish operations in the EC in order to participate in the market.

TIA's statement indicates that market access problems in Europe stem from traditional government policies designed to preserve domestic jobs. TIA noted that the directives of particular concern were those relating to public procurement, standards, type approval, and open network provision. Since the EC telephone administrations are government-owned, their purchases are deter-

mined by public-procurement policies. Although the proposed directive on public procurement would open contracts to competitive bidding and eliminate national preferences, public entities could still exclude proposals that did not have 50-percent local content. TIA is concerned with how the 50-percent rule will be defined and particularly that U.S. exporters will have a problem competing in the EC market as a result of this rule.

TIA notes that the harmonization of standards could be beneficial to U.S. firms through the elimination of 12 different country standards and the creation of a single EC standard. However, if the standards-setting process is not open and transparent, it could become a trade barrier for U.S. firms. U.S. companies with European operations may participate in the European Telecommunications Standards Institute, but they can only participate in working groups if they are involved in the areas of discussion. Nonresident U.S. firms may participate as observers, but these firms do not have the opportunity to become involved in the standards-setting process. TIA feels that keeping the standards-setting process open and transparent is very important for U.S. firms.

Type approval of telecommunications terminal equipment is required before the equipment can be connected to the network. TIA members support the harmonization of the type-approval process among the various EC member states. TIA wants the criterion for type-approval to be one of "no harm to the network," and desires that the process be open, transparent, and nondiscriminatory. While the type-approval directive is a significant step forward, TIA feels that in order for the terminal equipment market to become truly competitive, independent channels of distribution need to be opened up. Currently, most terminal equipment is distributed through the PTTs.

TIA feels that the open network provision (ONP) directive holds promise for U.S. equipment manufacturers, based upon significant demand in the EC for advanced network services. To the extent that the ONP directive allows for competition in network services, TIA believes that demand for the necessary equipment will accelerate. Since U.S. manufacturers of data communications equipment have some of the most advanced products in the world, the prospects for increased U.S. exports look good. TIA feels that it is the job of both the industry and the U.S. Government to ensure that EC policy provides competitive opportunities for U.S. equipment suppliers.

Additional Views of U.S. Industry Officials

In discussions with officials of U.S. firms over the possible impact of EC 92, concerns were expressed over standards, public procurement, and research and development. These officials indicated the belief that the principal supplier/PTT relationships in the EC will continue into the future

⁴⁷ Testimony before the U.S. International Trade Commission by Edwin Spievack, President of the North American Telecommunications Association on June 21, 1990, transcript, p. 73.

⁴⁸ Testimony before the U.S. International Trade Commission by Edwin Spievack, President of the North American Telecommunications Association on June 21, 1990, transcript, p. 77.

⁴⁹ Testimony before the U.S. International Trade Commission by Edwin Spievack, President of the North American Telecommunications Association on June 21, 1990, transcript, p. 83.

in spite of any directives that are issued. Under the present system, the cost of research and development in telecommunications conducted by the principal EC suppliers is funded by the PTTs through high-priced contracts. For example, the PTTs typically pay their principal suppliers more per line for a central office switch than a comparable U.S. purchaser would be willing to pay in order to obtain the product. The extra price per line that the PTT pays the principal supplier is designed to cover research and development expenses. In the United Kingdom, the procurement process is different than in the other EC member states in that, British Telecom (BT) Laboratories undertake the design for a new product and subsequently offer the design to BT's principal suppliers for manufacture. U.S. firms have great difficulty in competing against such types of research and development subsidies as they are funding research and development from operational revenues.

According to industry sources, a useful strategy for U.S. firms to pursue in order to penetrate the European, as well as other foreign markets, may be initially to market a small telecommunications product line. U.S. firms could thus attempt to have their equipment incorporated into a peripheral area of the network, where its function is not critical, and thereby demonstrate that their equipment will function without causing harm to the network. For example, by supplying a piece of equipment for a

rural area and permitting the equipment to perform, a U.S. firm could demonstrate to a PTT that it will work reliably with the other equipment in the network. In this way, U.S. firms could earn a reputation for supplying reliable products. U.S. firms could also attempt to penetrate those market segments where it is "easy" for the PTTs to buy products from foreign companies. Market segments where politics play a large role, such as in the procurement of central office switches, are likely to be much more difficult to enter.

A second aspect of the European market is that firms that appear "European" are more likely to win contracts. For example, Pacific Telesis is a member of a consortium that will provide cellular telephone service to West Germany. Pacific Telesis has established a good business relationship with Motorola; and Motorola is a leading supplier of cellular telephone equipment. However, when the West German contract for cellular telephone equipment was announced it was awarded to Siemens (West Germany) and Ericsson (Sweden). Ericsson won the contract reportedly because it looked more "European" than Motorola. In awarding contracts for telecommunications equipment in Europe, national firms reportedly come first, followed by firms in other EC member states, and then by European firms from non-EC member states.

CHAPTER 22
CHEMICALS AND PHARMACEUTICALS SECTOR

CHAPTER 22

CHEMICALS AND PHARMACEUTICALS SECTOR

The U.S. chemical industry (including pharmaceuticals) was chosen to be one of the industries highlighted in this report because of the significant impact EC 92 could have on future U.S. access by U.S. chemical and pharmaceutical firms in this market. In 1989, U.S. chemical exports to the EC were valued at \$9.8 billion, or 12 percent of all U.S. exports to this market. During this same period, the United States had a positive balance of trade in these products with the EC nations of approximately \$770 million.

Industry Profile

The U.S. chemical industry is one of the largest industries in the United States, directly employing more than 1 million people and producing more than 50,000 different chemicals and formulations in more than 12,000 different chemical plants. The chemicals produced in these plants are sold in more than 180 other nations. The United States currently maintains a positive trade balance in the chemicals and allied products sector, as defined by the Standard Industrial Classification (SIC) system, with at least 20,000 different U.S.-produced chemicals included in international trade.

Preliminary 1987 U.S. Census of Manufactures data indicate that U.S. chemicals and allied products sector (SIC Major Group 28) shipments were valued at \$229 billion. Pharmaceutical sector (SIC Group 283) shipments were valued at about \$39 billion and accounted for more than 17 percent of chemicals and allied products shipments; pharmaceutical sector value added amounted to approximately \$28 billion and accounted for 23 percent of value added in chemicals and allied products.

Chemicals

The U.S. chemicals and allied products industry produces tens of thousands of chemical products from a multitude of raw materials, including petroleum and natural gas, metals, minerals, vegetable oils, and animal fats and oils. The diversity of these types of firms provides an almost infinite array of possibilities for the the U.S. chemical industry as it is challenged with opportunities and uncertainties associated with the merging of the European market.

The rationalization of the U.S. chemical industry that took place during the mid-1980s was in response to the problems that beset the industry in the previous decade. Numerous divestitures, plant closings, and company reorganizations allowed U.S. producers to cut their overhead costs to better allocate their remaining resources and thereby produce both industrial and consumer products more efficiently.

Although the United States is considered to be one of the three traditional chemical-producing areas of the world, individual European firms, particularly those firms located in EC member nations, are the largest producers and marketers of chemicals¹ in the world, as shown in the tabulation, at the bottom of the page, of the world's 14 largest chemical-producing firms:²

However, the U.S. chemical industry remains dominant in the domestic market and competitive with other international chemical producers in most foreign markets.

¹ Data for the U.S. chemicals and allied products sector and the EC chemicals sector include data on pharmaceuticals and medicinals.

² *Chemical & Engineering News*, May 28, 1990, pp. 27-29 and *Chemical & Engineering News*, June 18, 1990, pp. 34-83.

Company	Rank	Location	Chemical sales, 1989
			Million dollars
BASF ¹	1	West Germany	25,328
Hoechst ¹	2	West Germany	24,414
Bayer AG ¹	3	West Germany	23,031
ICI Ltd. ¹	4	United Kingdom	21,592
DuPont	5	United States	15,249
Dow Chemical	6	United States	14,179
Ciba-Geigy	7	Switzerland	12,565
Rhone-Poulenc ¹	8	France	11,453
Enimont ¹	9	France	11,452
Exxon	10	United States	10,559
Norsk Hydro	11	Norway	9,613
Akzo ¹	12	Netherlands	8,838
Mitsubishi	13	Japan	8,102
Union Carbide	14	United States	7,962

¹ Companies located in EC member nations.

Pharmaceuticals

The U.S. pharmaceutical industry is considered to be one of the largest and one of the most technologically sophisticated of such industries in the world. In 1989, the U.S. industry accounted for over \$50 billion (domestic and foreign sales) of a global market estimated to be valued at about \$150 billion. The top three companies worldwide in 1988 were Merck (United States), accounting for 4 percent of the world market; Glaxo Holdings (United Kingdom), 3 percent; and Ciba-Geigy (Switzerland), with 2.8 percent. This ranking changed in 1989 as several mergers and acquisitions were completed.³ Such activity is continuing in 1990. It has been suggested that the industry is entering a "period of consolidation" and could eventually be dominated by "a small number of larger research & development (R&D) based companies."⁴

The U.S. pharmaceutical industry shares many similarities with pharmaceutical industries in other developed countries. For example, it displays a relatively high degree of vertical integration but is less integrated horizontally. The pharmaceutical industry is multinational and primarily privately owned. The industry is subject to domestic regulations in regard to product efficacy, product standards, and product testing. It is also afforded a relatively high degree of domestic patent, copyright, and trademark protection for its products and processes.

U.S. Production

Chemicals

U.S. production of chemicals and allied products has been increasing steadily since 1985, with almost all of the major sectors of the industry maintaining steady patterns of growth throughout this period. The only exception occurred during 1985-86, at which time the inorganics sector had not yet returned to a growth pattern after the 1985-86 recession.⁵

The value of all shipments for U.S. firms classified by the U.S. Department of Commerce as primary producers of chemicals and allied products are shown in the following tabulation.⁶

³ Included are the mergers of SmithKline Beckman (United States) and Beecham (United Kingdom); Squibb and Bristol-Myers; and Marion and Merrell Dow.

⁴ Jane Docherty and Katrina Labaere, "The Pharmaceutical Industry: Preparing for the Nineties," *EC Bulletin*, No. 84, September/October 1989, p. 13.

⁵ *Chemical & Engineering News*, "Growth Maintains a Strong Pace," June 19, 1989, p. 38.

⁶ U.S. Department of Commerce, *U.S. Industrial Outlook, 1989 and U.S. Industrial Outlook, 1990*.

Year	Value of shipments	Percent change from preceding year
	Million dollars	
1985	197,311	(¹)
1986	197,091	(0.1)
1987	229,015	16.1
1988	258,925	13.1
1989	274,459	6.0

¹ Not applicable.

² Estimated.

The value of shipments increased by 2.1 percent during 1987-88 and 3.2 percent during 1988-89 in real terms. The U.S. Department of Commerce projects that the value of shipments of chemicals and allied products will increase by about 2 percent in real terms in 1990.⁷

Each of the major sectors of the U.S. chemicals and allied products industry exhibited significant growth during this period; most significantly the organic chemicals sector (SIC 2865 and 2869) experienced a growth rate of about 12 percent in value of shipments during 1987-89, and the plastics materials and resins sector (SIC 2821), experienced an increase in its value of shipments of more than 29 percent during 1987-88 and more than 8 percent during 1988-89. Both of these increases were directly attributable to an increase in demand for plastics products that exceeded the ability of producers to increase their available supply. Therefore the producers of the organic chemicals used to produce the polymers and resins, as well as the producers of the plastics materials, saw their prices increase by as much as 20 percent as demand for their products kept their plants operating at almost full capacity. Although it is anticipated that there will be growth in these areas in 1990, the rate of growth is expected to be significantly slower than seen during the last 2 years, as producers' inventories were believed to have expanded during the final months of 1989.

Pharmaceuticals

Industry shipments of pharmaceuticals increased steadily during 1985-89, from \$31.3 billion to \$46.8 billion. Products in finished-dosage form accounted for over 80 percent of total pharmaceutical shipments during 1985-89.⁸ The three top product classes in 1988, in terms of shipments, were preparations acting on the central nervous system (21 percent), preparations affecting parasitic and infective diseases (15 percent), and preparations acting on the cardiovascular system (15 percent). Unlike in the EC, where, in many cases, the member state is the largest buyer of

⁷ *Ibid.*

⁸ The bulk active ingredient, or the pharmacologically active component, is formulated into dosage forms such as capsules, tablets, creams, lotions, etc., that are generally ready for sale once packaged. These pharmaceutical preparations are typically composed of the active ingredient plus diluents or extenders.

⁹ Individual national health-care authorities are the major purchasers of prescription pharmaceuticals in the EC.

pharmaceuticals,⁹ U.S. wholesalers accounted for almost 70 percent of sales of these ethical products by domestic manufacturers in 1987.¹⁰ The U.S. Federal, State, and local governments accounted for about 6 percent of such sales.¹¹

U.S. production capacity for pharmaceuticals has increased moderately since 1983 and will probably continue to grow at a moderate rate during the next 10 years, keeping pace with the expected annual growth rate of less than 5 percent in U.S. production of these chemicals.¹² Generic sales are currently estimated to be valued at more than \$7 billion for products classified under SIC 2834, or about 30 percent of the domestic market for ethical pharmaceuticals in 1989.¹³ By 1995, however, the U.S. patents on approximately 200 products will expire, potentially expanding the generic market by approximately \$6 billion during 1990-95.¹⁴ This expansion could result in increased production capacity for generics.

U.S. Employment

Chemicals

Employment in the U.S. chemicals and allied products industry remained fairly stable during the past decade, declining by approximately 1.4 percent between 1979 and 1989.¹⁵ This decline occurred primarily as a result of the rationalization that took place during the mid-1980s, which permitted the U.S. chemical industry to remain competitive despite changes in the structure of the international industry. Employment increased during 1987-89 in response to increasing demand. The following tabulation shows the total employment in the U.S. chemicals and allied products industry along with the average weekly wage for industry production workers during 1985-89:

Year	Total Employment	Average weekly wage— production workers
	1,000 workers	
1985	1,046	\$485.1
1986	1,022	501.9
1987	1,028	523.3
1988	1,063	535.9
1989 ¹	1,094	545.0

¹ Estimated by the U.S. Department of Labor.

¹⁰ "Generic" is defined as being non proprietary and denoting a drug name that is not protected by a trademark and that is usually descriptive of the drug's chemical structure. An "ethical" product, in this context, is defined as one that is restricted to sale only on a doctor's prescription.

¹¹ Pharmaceutical Manufacturers Association (PMA), *Statistical Fact Book*, December 1989, p. 5.

¹² U.S. Department of Commerce, *U.S. Industrial Outlook* 1990, p. 50-54.

¹³ *Ibid.*, p. 50-53; "Pharmaceuticals '90," *Chemical Marketing Reporter*, Mar. 19, 1990, p. SR35.

¹⁴ U.S. Department of Commerce, *U.S. Industrial Outlook* 1990, p. 50-53.

¹⁵ According to official statistics of the U.S. Department of Labor.

Although the number of total workers employed by the U.S. chemicals and allied products industry declined steadily between 1979 and 1986, the level of productivity increased significantly. The value of industry shipments per employee increased from about \$133,183 in 1979 to more than \$192,857 in 1986, when the major part of the industry rationalization was completed.

Pharmaceuticals

Employment in the U.S. pharmaceutical industry increased during 1985-89 from 164,000 employees to approximately 180,000. According to statistics released by the Pharmaceutical Manufacturers Association (PMA), the majority of these employees were involved in the manufacture of ethical products.¹⁶ Production workers accounted for the largest share, about 35 percent, of the employees involved in producing ethical products. Productivity in the pharmaceutical industry increased slightly in 1989 after declining by a small amount in 1988.

U.S. Exports

Chemicals

In 1989, the U.S. industry exported approximately 36.5 billion dollars' worth of chemicals and allied products, which accounted for almost 16 percent of its total chemical output, valued at \$229.0 billion.¹⁷ This represented an increase in exports of U.S.-produced chemicals of more than 14 percent, when compared with U.S. exports in 1988. In comparison, chemical exports from the EC nations in 1988 were estimated to be valued at \$135 billion, four times the value of U.S. chemical exports and almost 10 times the value of Japanese chemical exports during the same period.¹⁸

One reason for this increase in U.S. chemicals exports could be an increase in the amount of interaffiliate trade between multinational firms. One such firm located in an EC member nation indicated that approximately 15 percent of its EC-U.S. trade pattern was accounted for by interaffiliate transactions.¹⁹ It is believed that this pattern is representative for many of the larger multinational producers of chemicals that have rationalized their production strategies during the past decade. Interaffiliate trade among smaller firms, based either in EC nations or in the United States, is believed to account for less than 15 percent of their overall trade. EC chemical

¹⁶ According to the PMA *Statistical Fact Book* (p. 21), in 1987 firms producing ethical products employed approximately 175,000 people in the United States and about 143,000 people abroad.

¹⁷ According to official statistics of the U.S. Department of Commerce.

¹⁸ Commission of the European Communities, *Panorama of EC Industry, 1989*, p. 7-2, and "Facts and Figures," *Chemical & Engineering News*, June 19, 1989, p. 77.

¹⁹ Obtained by a Commission staff member on a field trip to the EC in June 1990.

exports accounted for about 23 percent of total EC chemicals and allied products production in 1986.²⁰

Total U.S. chemical exports in 1989 accounted for approximately 10 percent of all U.S. exports. U.S. exports of chemicals and allied products to the EC, valued at \$9.8 billion, accounted for nearly 12 percent of all U.S. exports to EC nations.

The total value of U.S. exports entering the 12 nations of the EC amounted to nearly \$9,758 million, nearly 27 percent of total U.S. chemical exports, and more than twice as large as any current single foreign market. The next three largest individual export markets of the U.S. chemicals and allied products industry in 1989 were Japan, Canada, and Mexico. These nations accounted for the following shares of U.S. chemical exports in 1989:²¹

Market	Export value	Share of U.S. exports
	Million dollars	Percent
Japan	4,664	12.8
Canada	4,210	11.5
Mexico	2,195	6.0
EC member nations, total	9,758	26.7

Pharmaceuticals

The traditional trade surplus enjoyed by the U.S. pharmaceutical industry is still in effect today but has been declining since 1982. During 1985-89, U.S. exports of pharmaceutical products increased from \$2.7 billion to \$4.4 billion. The top three markets during these years were Japan, West Germany, and Canada. U.S. exports of pharmaceuticals to the EC in 1989 were valued at about \$1.9 billion. The top three markets in the EC in 1989 were West Germany, Italy, and Ireland. Related-party transactions accounted for a moderate share of these exports since many major U.S. pharmaceutical firms have subsidiaries in the EC and produce their product locally rather than importing it from the United States. As such, a large share of U.S. exports of pharmaceuticals is composed of bulk chemical that will be processed and/or packaged in the European facility.²²

U.S. Imports

Chemicals

U.S. imports increased steadily during 1985-89, at an average annual rate of approximately 9

²⁰ Ibid.

²¹ According to official statistics of the U.S. Department of Commerce.

²² PMA, *Statistical Fact Book*, 1988, p. 12; According to PMA's *U.S. Trade in Drugs and Medicinal Chemicals: Analysis of Trends and Forecasts to 1990* (June 1987), p. 42, "higher-income countries which have well-established pharmaceutical industries... import intermediate products for further processing or packaging." The book indicates that the import demand for finished dosage form products is relatively inelastic.

percent. However, the trade surplus in chemicals has continued to expand during these years, as shown in the following tabulations (in billions of dollars):²³

Year	U.S. Imports	U.S. Exports	Trade Surplus
1985	14.6	21.8	7.2
1986	15.1	22.5	7.4
1987	16.4	26.0	9.6
1988	19.9	31.9	12.0
1989	20.5	36.5	16.0

As can be seen from the data in the previous tabulation, the continuous increase in U.S. imports of chemicals, in this particular case, does not seem to be having an adverse impact on the U.S. industry or the overall U.S. economy. Instead, these imports appear to be assisting the economic growth both of the U.S. chemicals and allied products industry and the corresponding chemical industries in other major industrial nations. As mentioned previously, one reason could be the amount of interaffiliate trade between multinational firms with locations both in EC member nations and in the United States.²⁴

The major sources for U.S. chemical imports in 1989 were Canada and the world's other major chemical-producing nations, West Germany, Japan, and the United Kingdom, as shown in the following tabulation:²⁵

Source	Import value, 1988	Share of U.S. imports
	Million dollars	Percent
Canada	3,928	19.1
West Germany	2,802	13.7
Japan	2,367	11.5
United Kingdom ...	2,018	9.8

With regard to U.S. chemical imports from the EC, a closer examination of recent U.S. chemical import data indicates that the EC nations, taken as a whole, have maintained a relatively stable share of the U.S. chemical import market. In 1985, U.S. chemical imports from EC nations were valued at \$6.3 billion and accounted for about 43.1 percent of U.S. imports. U.S. imports from the EC had climbed to nearly \$9.0 billion in 1989 but still accounted for about 43.8 percent of U.S. imports. Additionally, the overall share of the U.S. market for which the EC nations account has also remained fairly stable, as can be seen in the following tabulation:²⁶

²³ Compiled from official statistics of the U.S. Department of Commerce.

²⁴ Information obtained during fieldwork.

²⁵ Compiled from official statistics of the U.S. Department of Commerce.

²⁶ Compiled from official statistics of the U.S. Department of Commerce.

Year	U.S. imports from the EC	U.S. apparent consumption	EC share of U.S. apparent consumption
	Million dollars		Percent
1985	6,293	204,550	3.1
1986	6,491	204,484	3.2
1987	7,228	238,669	3.0
1988	8,897	270,992	3.3
1989	8,988	290,425	3.1

Pharmaceuticals

During 1985-88, U.S. imports of pharmaceutical products increased from \$2.1 billion to \$3.5 billion, or by 67 percent. The top five sources of these imports during this time were the United Kingdom, West Germany, Japan, Switzerland, and Italy.²⁷

Total U.S. imports of pharmaceuticals in 1989 were valued at \$3.6 billion. The top three sources of these imports in 1989 were the United Kingdom (20 percent), West Germany (15 percent), and Japan (11 percent). U.S. imports of these products from the EC were valued at about \$2.0 billion in 1989, or about 55 percent of the total. The three leading EC sources of these products were the United Kingdom, West Germany, and Italy.

²⁷ The ranking of these countries varied during 1985-89. Import levels were predicted to decline in 1986-87 as the strength of the U.S. dollar declined relative to EC currencies. However, imports actually continued to increase, primarily due to a reluctance among foreign suppliers to pass along price increases and risk the possibility of losing market share. PMA, *U.S. Trade in Drugs and Medicinal Chemicals*, June 1987, p. x.

Size Distribution of U.S. Firms

Chemicals

As noted previously, only 3 of the world's 10 largest producers of chemicals and allied products are based in the United States, whereas six are based in EC member nations. The first tabulation at the bottom of the page lists the 10 largest chemical-producing firms in the United States in 1989, based on the value of their chemical sales.²⁸

These firms are generally representative of the more highly diversified and vertically integrated producers of chemicals and are known both as producers of basic chemical products as well as producers of their downstream derivatives. Of the companies known primarily as producers of specialty chemicals, the six with the largest, in terms of chemical sales, are shown in the second tabulation at the bottom of the page.²⁹

²⁸ *Chemical & Engineering News*, May 7, 1990, p. 28-29.

²⁹ *Chemical & Engineering News*, June 19, 1989, pp. 52-53 and *Chemical & Engineering News*, May 7, 1990, pp. 28-29.

Rank	Name	Chemical sales, 1989	Chemical sales share of total sales
		Million dollars	Percent
1	DuPont	15,249	42.9
2	Dow Chemical	14,179	80.6
3	Exxon	10,559	11.1
4	Union Carbide	7,962	91.1
5	Monsanto	7,782	66.6
6	Hoechst Celanese	5,658	94.0
7	Occidental Petroleum	5,203	25.9
8	General Electric	4,929	30.3
9	BASF	4,461	82.3
10	Amoco	4,274	17.8

Overall Rank	Name	Chemical sales, 1988	Chemical sales share of total sales
		Million dollars	Percent
32	Rhone-Poulenc	1,600	100.0
33	Dow Corning	1,575	100.0
34	National Starch	1,569	100.0
42	Ciba-Geigy	1,200	34.3
45	Lubrizol	1,124	92.1
48	Nalco Chemical	1,071	100.0

The ratio of chemical sales to total sales for the specialty chemical firms of 80 percent was, true to expectations, significantly higher than the 25-percent ratio associated with the 20 largest U.S. chemical firms, indicating the greater dependence of these specialty chemical firms on the overall health of the U.S. chemical industry.

Pharmaceuticals

The U.S. pharmaceutical industry comprises approximately 1,250 firms, of which, according to industry sources, approximately 750 companies are involved in the domestic production of ethical pharmaceuticals in both bulk and dosage form.³⁰ Many of these firms are concentrated geographically in New Jersey, New York, Pennsylvania, Indiana, Illinois, Michigan, Missouri, Ohio, California, and Puerto Rico.

When compared with other domestic industries, the U.S. pharmaceutical industry is considered to be quite fragmented since individual companies account for relatively low shares of the domestic market. According to the U.S. Department of Commerce, however, approximately 60 companies accounted for the majority of R&D in the industry in 1989, as well as for the majority of industry production and sales.³¹

U.S. Industry Investment

Chemicals

The chemicals and allied products industry is highly capital intensive. Companies with assets totaling less than \$25 million account for less than 5 percent of total chemical industry assets. The total assets of the U.S. chemical and allied products industry, as of mid-1989, amounted to approximately \$285 billion, and accounted for more than 11 percent of all U.S.-owned manufacturing assets.³² Industry sources expect that the value of chemicals industry assets will rise to \$290 billion or higher by mid-1990.³³

The level of capital investment expenditures by the U.S. chemicals and allied products industries increased significantly during 1987-89, increasing by more than 17 percent during 1987-88 and by nearly 11 percent during 1988-89, as can be seen in the following tabulation (in billions of dollars):³⁴

Year	All manufacturing	Chemicals
1985	153.48	16.44
1986	142.69	16.81
1987	145.90	16.42
1988	165.70	19.25
1989	184.54	20.35
1990	190.89	21.75

Capital investment in the chemical industry has increased during 1985-90 at an average annual rate of about 6.0 percent, compared with an average annual increase in capital spending for all domestic manufacturing industries of about 5.6 percent.

As of 1986, chemicals and allied products industry assets totaled \$217 billion, compared with U.S. direct investment abroad (USDIA)³⁵ by the U.S. industry totaling \$75.6 billion.³⁶ Nearly 43 percent of this total, or \$32.2 billion, was invested in the chemical industries of EC member nations.

Pharmaceuticals

U.S.-based companies are well established in the European market and currently account for approximately 25 percent of sales of pharmaceuticals in the EC pharmaceutical market. U.S. pharmaceutical investment in the EC in 1986 was estimated at \$14 billion. Production and R&D facilities are generally concentrated in a few countries, primarily for economic considerations. Formulation facilities, however, can be decentralized and are therefore likely to be located in the country whose market is to be served. This provides better market supply and, in some cases, has reportedly been taken into consideration by national authorities when approving prices.

In 1986, it was estimated that 26 foreign pharmaceutical firms had R&D and production facilities in the United States. Total assets of U.S. affiliates of companies based in Europe, as estimated for 1986, were valued at approximately \$8.9 billion.³⁷ The largest share of the assets was attributed to firms with parents operating out of Switzerland (56 percent). In descending order, the next three largest shares belonged to affiliates with parent companies based in the EC: United Kingdom (34 percent), West Germany (5 percent), and France (1 percent).³⁸

³⁵ USDIA is the ownership or control, directly or indirectly, by one U.S. person of 10 percent or more of the voting securities of an incorporated foreign business enterprise or an equivalent interest in an unincorporated foreign business enterprise. A foreign affiliate is a foreign business enterprise in which there is a U.S. direct investment.

³⁶ U.S. Department of Commerce, Bureau of Economic Analysis, *U.S. Direct Investment Abroad*, June 1988.

³⁷ This figure is defined as the "Total Assets of Affiliates, by Industry of Affiliate by Country of Ultimate Beneficial Owner" U.S. Department of Commerce, *Foreign Direct Investment in the United States: Operations of U.S. Affiliates of Foreign Companies (Preliminary 1986 Estimates)*, June 1988.

³⁸ Based on the countries indicated in U.S. Department of Commerce, *Foreign Direct Investment in the United States*.

³⁰ The remainder are primarily manufacturers of generics.

³¹ PMA indicates that, in terms of prescription dollars, the 20 largest U.S. firms accounted for about 75 percent of the domestic market in 1986. According to *Panorama of EC Industry, 1989*, published by the EC Commission, the 10 largest pharmaceutical companies in the world account for about 25 percent of the world market.

³² Chemical Manufacturers Association, *The U.S. Chemical Industry Performance in 1989 and Outlook*, January 1990, p. 8.

³³ *Ibid.*

³⁴ "Facts and Figures," *Chemical & Engineering News*, June 18, 1990, p. 50.

Innovation is seen as one way to offset the decrease in pricing of pharmaceutical products that generally results from the entry of generic manufacturers into the market after the expiration of the patent protection agreement, any marketing exclusivity agreements, or both for a particular product. R&D expenditures by the domestic industry have been steadily increasing over the past several years. As such, the number of firms able to conduct such innovative research continues to decline. On the average, a domestic firm is said to allocate approximately \$400 million towards R&D expenditures. This amount is expected to increase to about \$1 billion in the next decade, and, in turn, is expected to promote more mergers and consolidations in the industry.

U.S. pharmaceutical companies invested a total \$7.4 billion in R&D in 1989, compared with \$6.5 billion in 1988. Total industry R&D expenditures represented approximately 16 to 17 percent of industry sales in 1988-89. Approximately one-fifth of these R&D expenditures were reportedly invested overseas.³⁹ Almost 70 percent of the overseas R&D expenditures during 1986-87 were invested in Western Europe.⁴⁰

Another form of investment in the pharmaceutical industry is the cost associated with bringing a new drug to market. On the average, this cost is estimated at about \$125-250 million, depending on the factors included in making the estimate.⁴¹ The average time associated with bringing the new product to market is about 10 years from its patent application. It has been estimated that the average Food and Drug Administration review time for the 20 new drugs approved in 1988 was about 31 months. The approximate review time overseas for those products out of the 20 that were first approved in foreign markets was said to be about 15 months, or about half of that in the United States.⁴²

The U.S. industry has also been investing in Japan. Merck, for example, recently acquired Banyu Pharmaceuticals in Japan. The acquisition of Banyu is said to have "already allowed Merck to be the only non-Japanese company with a major presence in Japan."⁴³ Other U.S. companies have either purchased Japanese companies or are said to be considering entering into joint-venture and licensing agreements with Japanese companies. The largest pharmaceutical company in Japan,

Takeda Chemical Industries, had total sales of approximately \$5 billion in 1988 and was ranked 19th in terms of pharmaceutical firms worldwide.⁴⁴

Japanese firms are said to be currently actively considering joint ventures with U.S. firms in an effort to enter into Western markets and have entered into various licensing and marketing agreements throughout Europe.⁴⁵ The Japanese are considered most likely to concentrate on small or medium-sized U.S. or EC pharmaceutical firms that have developed their sales network but have a limited product list.⁴⁶ Industry sources expect that Japanese firms will make "major investments" in Europe during the next 10 years in an effort to "exploit the significant scale of their new drug development effort."⁴⁷

Possible Impact From EC 92 Programs

The EC Chemicals and Allied Products Market and the U.S. Position

Chemicals

The EC chemical market, like that of the United States, has remained strong throughout the latter half of the last decade, exhibiting growth in each year without experiencing the downturn predicted annually by industry experts. During 1980-90, the Western European chemical industry experienced an average annual growth rate in sales of 3.3 percent, compared with a 1.7-percent growth rate for all Western European manufacturing industries. In 1988, total chemical sales of producers in the 12 EC nations were valued at approximately \$312 billion, 29 percent greater than the total value of U.S. shipments of chemicals and allied products during the same period. This disparity is related primarily to the larger and more varied nature of the EC market.⁴⁸ In 1989, EC chemical sales increased to about \$316 billion, accounting for approximately 28 percent of world chemical sales.⁴⁹ Of total EC sales in 1989, West Germany accounted for more than 24 percent, France about 16 percent, and the United Kingdom nearly 13 percent.

The EC balance of trade in chemicals has remained strongly positive, reaching approximately \$29.3 billion in 1988 and nearly \$25.5 billion in 1989.⁵⁰ Capital investment by the EC chemical industry, which had decreased during

³⁹ PMA, *Statistical Fact Book*, December 1989, p. 2-2.

⁴⁰ The term "Western Europe," in this case, excludes Turkey, Yugoslavia, and Albania, but includes Greece and Scandinavia; PMA, *1987-89 Annual Survey Report: U.S. Pharmaceutical Industry*, 1989, p. 2A.

⁴¹ PMA, *Statistical Fact Book*, December 1989, p. 13; "Drug Development Costs Up Sharply, New Study Finds," *Chemical Marketing Reporter*, Apr. 23, 1990, p. 4.

⁴² PMA, *Statistical Fact Book - Facts at a Glance*, 1990, p. 18.

⁴³ According to *Financial World* (May 30, 1989, p. 70), Merck is said to have acquired at least one other Japanese pharmaceutical firm in the past 8 years; "Pharmaceuticals '90," p. SR8.

⁴⁴ *Financial World*, p. 70.

⁴⁵ *Chemical Week*, May 10, 1989, p. 19.

⁴⁶ *Asian Wall Street Journal*, Aug. 28, 1989, p. 6.

⁴⁷ "Drug Firms Fear Effect of Pricing Regulations," *European Chemical News*, Feb. 12, 1990, p. 12.

⁴⁸ *Chemical & Engineering News*, "U.S. Chemical Companies Ponder Europe After 1992," Nov. 6, 1989, pp. 7-13; and European Chemical Industry Federation, *Facts and Figures: West European Chemical Industry*, 1990, p. 9.

⁴⁹ European Chemical Industry Federation, *Facts and Figures*, 1990, pp. 9-13.

⁵⁰ European Chemical Industry Federation, *Situation and Outlook of the European Chemical Industry 1989-90 and Basic Economic Statistics 1988-89*, June 1990.

1980-84, has increased steadily during 1984-89. EC chemical industry capital investment reached \$15.3 billion in 1988 and \$18.0 billion in 1989. However, the ratio of capital spending to gross sales in the EC nations was approximately 6.5 percent in 1989, compared with approximately 8 percent in the United States and 9 percent in Japan.⁵¹ Employment in the EC chemical industry in 1989 was about 1.9 million, approximately 5 percent less than the number employed during 1985.⁵²

Apparent consumption of chemicals and allied products in the EC declined slightly, remaining predominantly stagnant during 1981-85, a period during which the U.S. market was also stagnant. Both production and consumption rebounded during the latter half of the decade, as indicated in the following tabulation concerning the EC chemical industry (in millions of dollars⁵³):⁵⁴

Year	EC apparent consumption ¹	EC net Exports ¹	Total EC production ²
1981	168,804	20,993	193,782
1982	162,089	18,429	183,703
1983	157,78	319,467	181,618
1984	151,910	19,697	161,262
1985	163,333	20,481	171,707
1986	205,768	22,214	199,162
1987	236,400	24,769	(³)

¹ Statistics are for EC 11 only, Greece excluded.

² Eurostat data; EC 11 only, not including Portugal; not including Spain (1984, 1985), Spain, Netherlands, and Greece (1986).

³ Not available.

Major sectors within the EC market include plastics; fertilizers; soaps, toiletries, and cosmetics; and pharmaceuticals. The following tabulation highlights EC apparent consumption data for these major chemical end-product sectors (in millions of dollars⁵⁵):⁵⁶

Year	EC apparent consumption ¹	EC net Exports ¹	Total EC production ²
Sector	1983	1987	
Chemical industry	173,561	212,400	
Plastics	10,423	13,057	
Fertilizers	6,500	7,000	
Soaps, toiletries, and cosmetics	5,653	118,210	

¹ Estimated.

⁵¹ Ibid.

⁵² Ibid.

⁵³ Data converted from ECU to US\$ using exchange rates detailed in a publication of the U.S. Mission to the European Community, *Economic Data Book*, p. 38

⁵⁴ EC Commission, *Panorama of EC Industry, 1989*, p. 7-1.

⁵⁵ Data converted from ECU to US\$ using *Economic Data Book*, p. 38.

⁵⁶ Ibid., pp. 7-1 through 8-6.

U.S. chemical industry exports to the 12 EC nations have grown steadily during 1985-89, at an average annual rate of about 13 percent. These exports are expected to continue to grow at a similar pace in 1990. The following tabulation shows the value of U.S. exports to EC nations during 1985-89 (in millions of dollars):⁵⁷

Year	Value of U.S. exports to EC	
	All products	Chemicals
1985	46,713	5,911
1986	50,251	6,271
1987	57,230	7,085
1988	71,306	8,318
1989	82,525	9,758

U.S. exports of chemicals to the EC accounted for nearly 12 percent of all U.S. exports to the EC during 1989. Exports of U.S.-produced chemicals and allied products in 1989 accounted for 3 percent of the EC chemicals market. The sectors of the U.S. chemical industry with the most significant exports to the EC, as defined by the SITC, are shown in the following tabulation:

Sector	1989 U.S. Exports to EC	Share of chemical exports to the EC
	Million dollars	Percent
Organic chemicals (SITC 51)	3,036	31.1
Medicinal and pharmaceutical products (SITC 54)	1,573	16.1
Plastics in primary forms (SITC 57)	1,397	14.3
Inorganic chemicals (SITC 52)	939	9.6

These four U.S. chemical industry sectors together account for more than 71 percent of U.S. chemical exports to the EC. In general, the EC market absorbs approximately 25 to 28 percent of all U.S. chemical exports. However, the one notable exception is the medicinal and pharmaceutical products area, in which nearly 43 percent of all U.S. exports goes to EC nations.

Pharmaceuticals

The EC pharmaceutical industry has been characterized as "one in which typically the final consumer does not pay for the product, in which the producer is not free to fix his product price, and in which the government is simultaneously the principal paying agent and price controller."⁵⁸ The

⁵⁷ Compiled from official statistics of the U.S. Department of Commerce.

⁵⁸ Paolo Cecchini, *The European Challenge 1992: The Benefits of a Single Market*, p. 66.

Nature of Changes as a Result of EC 92

Chemicals

EC industry comprises approximately 2,100 firms. Turnover in the EC industry in 1987 was valued at \$48.4 billion,⁵⁹ with export earnings estimated at \$3.7 billion, or about 8 percent of EC production.⁶⁰ European countries supplied approximately 85 percent of the \$12.2 billion of intra-European trade in pharmaceuticals in 1987. In 1989, the EC pharmaceuticals market was said to be valued at about \$39 billion. The top three markets within the EC in 1989 were West Germany (25 percent), Italy (22 percent), France (21 percent), and the United Kingdom (11 percent).

Employment in the EC pharmaceutical industry amounted to about 409,000 in 1987, compared with about 455,000 for European Federation of Pharmaceutical Industries' Associations (EFPIA) countries. The EFPIA represents the pharmaceutical industry in Europe and is a federation of the national pharmaceutical associations in 16 European countries. These countries are as follows: Austria, Denmark, France, Greece, Italy, Norway, Spain, Switzerland, Belgium, Finland, West Germany, Ireland, the Netherlands, Portugal, Sweden, and the United Kingdom. R&D expenditures for EFPIA companies were valued at about \$6.8 billion in 1987.

Investment in the EC pharmaceutical industry, excluding R&D expenditures, was valued at \$2.0 billion in 1987. Investment expenditures in the pharmaceutical industries in West Germany and the United Kingdom accounted for 55 percent of total such expenditures. Expenditures in machinery, plant facilities, and vehicles accounted for about 72 percent of the expenditures in West Germany and the United Kingdom, whereas construction expenditures accounted for about 23 percent.⁶¹

⁵⁹ EC Commission, *Main Statistics on the Community's Pharmaceutical Industry*, 1989, p. 1.

⁶⁰ The Western European market is estimated to represent about 25 percent of the world market for pharmaceuticals. West Germany was said to be the only member state that exports a "significant amount" of product to Japan.

⁶¹ EC Commission, *Main Statistics on the Community's Pharmaceutical Industry*, 1989, p. 6.

There are nine specific directives already adopted by the EC (as of February 1990) that are expected to affect chemical industries based in nations outside the EC that are involved in the EC market, either by export or by direct investment, as well as the EC chemical industry itself.⁶² Generally, these directives deal with specific guidelines, some of which have already been approved by the Commission, that will be implemented throughout the Community in order to standardize certain trade practices. The approval of these directives, in most cases, predisposes member nations to enact new legislation implementing the component guidelines included in the directives. The nature of the effects to be felt by the U.S. and other chemical producers outside the EC will be determined by both the time it takes member nations both to enact the mandated legislation and the manner in which enforcement of the legislation is managed.

The U.S. chemicals and allied products industry expects the following product-oriented directives to have the potential for the greatest effect on commerce between the United States and the EC.⁶³

⁶² U.S. International Trade Commission, *The Effects of Greater Economic Integration Within the European Community on the United States: First Follow-Up Report* (Investigation No. 332-267), USITC Publication 2268, March 1990; The Conference Board, Research Report No. 921, 1992: *Leading Issues for European Companies*, 1989; "The Changing Map of Europe," *Harvard Business Review*, May/June 1989, pp. 77-101; European Information Service, *European Report*, various issues; and U.S. Department of Commerce, *EC 1992: A Commerce Department Analysis of European Community Directives*.

⁶³ Based on conversations with representatives of U.S. firms and industry associations; The Conference Board, Research Report No. 921, 1992; and U.S. Department of Commerce, *EC 1992*.

Figure 22-1
Chemicals and allied products: Product-oriented directives with greatest potential effect on commerce between the United States and the EC

Directive No.	Description
76/769	Restrictions on the marketing and use of (1) asbestos (adopted Dec. 20, 1985; 7th amendment; latest related directive 85/610) and (2) PCBs and PCTs (adopted Jan. 10, 1985; 7th amendment; latest related Directive 85/467).
73/404	Nonionic detergents (adopted Dec. 12, 1985; latest related Directive 86/94).
88/379	Classification, packaging, and labeling of dangerous preparations (adopted June 7, 1988).
90/35	Defines which bottles should be fitted with child-proof caps.
76/116	Liquid fertilizers (adopted Mar. 22, 1988; latest related Directive 88/123).
89/284	Calcium, magnesium, sodium, and sulfur content of fertilizers (adopted Apr. 13, 1989).
89/530	Trace elements in fertilizers (adopted Sept. 9, 1989).
67/548	Classification, packaging, and labeling of dangerous substances (1990).
76/768	Cosmetics (adopted Dec. 21, 1988; 4th amendment; latest related directive 88/667).
76/768	Cosmetics (adopted Dec. 21, 1989; 5th amendment/89/617).

Source: Compiled by the staff of the International Trade Commission.

These directives will provide for the following changes in EC member nations' laws and procedures:

- Increased levels of protection for both the environment and the consuming public throughout EC member nations. A minimum level of consumer and environmental regulation would be prescribed. From this foundation, member nations could construct their own consumer and environmental protection laws. Industry sources expect that the foundation for such legislation sought throughout EC member nations will tend to approximate those regulations already in force in the United States. However, it is expected that certain nations will undoubtedly tend toward far more stringent regulations based on their own internal experiences.
- Uniform labeling requirements throughout the EC and establishment of criteria for universal acceptability of product labels in all member nations. Such changes will probably include far more explicit labeling requirements than have been employed in member nations in the past, particularly as regards clear labelling of questionable materials that may be included in the product in question.

The following directives were considered in depth in the initial study and the first followup study of the EC economic integration:⁶⁴

- Registration Procedures for Plant-Protection Products (Com (89) 34 Final)
- EC Environmental Agency (Com (89) 303; Com (89) 542; Com (85) 3387)

The following new issues surrounding the implementation of these directives are being carefully watched by the U.S. industry:⁶⁵

1. A clarification of the identity of the agencies to be notified as to decisions regarding the petition for approval for the use of specific chemicals in pesticide products.
2. A definition of what constitutes an acceptable testing organization for approval of the use of new chemicals during the period of implementation of EC member nations' formal registration regulations, and the determination of

methods of access to the papers and materials that bear the seal of approval of the approved testing body.

The remaining concerns of the U.S. industry center on the nature and authority that will be associated with the expected EC analog to the U.S. FDA. Expectations related to the imminent development of this body range from one with a weak organization dependent upon the individual EC member nations to enforce any established "guidelines" to a somewhat stronger body with the power to enforce minimum protection legislation throughout the Community. However, the major effects of any such organization will be felt most strongly by the pharmaceutical sector of the chemical industry.

Expectations concerning the overall impact of these directives, taken as a package, of the U.S. chemicals and allied products industry, range from none to strong effects, and span the entire spectrum from positive to negative.

The responses seem to vary related to—

1. Size and diversity of the firm.
2. Level of current involvement in the EC market.
3. Expectations regarding future involvement in the EC market.
4. Primary chemical product/sector of the company.

Those firms that already possess large shares of their target markets and are either satisfied with their current level of activity in the EC or do not wish to enter EC markets generally are not concerned with the changes associated with the EC 92 directives. Firms with comparable backgrounds but with greater expectations concerning growth in EC market share are tending to look more favorably on the opportunities afforded by the changes mandated by the directives if they already have a foothold in their target EC market. Those firms that have not previously taken advantage of such opportunities in EC member nations, either by investment, association, or trade, are expecting the initial development of these markets to become increasingly more difficult.

Those smaller firms without the resources to invest in the EC market at the present time also feel that they will no longer have the economic or the financial capability to initiate such investments once the EC 92 directives are completely brought into force. Also, many small firms currently involved in the EC market through trade, but not by investment, are fearful of losing at least some of their current market share to EC firms and third nations' chemical producers with investments in the EC. In the more extreme cases, these small firms feel that they will be totally displaced from the EC market by larger firms capable of increasing their EC investments.

⁶⁴ USITC, *Effects of EC Integration*, USITC Publication 226, March 1990.

⁶⁵ European Information Service, *European Report*, various issues; *Technical Harmonization*, various issues; and *Eurobases: Info 92*, online data base sourced from Brussels, Belgium.

Pharmaceuticals

A number of directives have been issued during the past few years that relate to the pharmaceuticals sector in the EC. Directives that have already been proposed, and, in some cases, implemented, include—

- The “extension” directives;
- The accession of the EC to the European Pharmacopoeia;
- A package of three veterinary proposals;
- Three proposals concerning the rational use of drugs;
- The Transparency Directive; and, more recently, although not a directive.

In addition, a regulation on patent restoration has been issued that allows for the creation of a supplementary protection certificate for medicinal products (the legal aspects of this regulation will be covered in more depth in another section of this report).

Two issues important to the industry that are still under consideration are the existence of disparate national pricing/reimbursement systems on a member-state basis and the creation of a single-market authorization procedure for pharmaceuticals. These issues effectively impact both the EC and the U.S. industry and are interrelated to some degree, since industry sources indicate that a free market and free circulation need free pricing. As such, industry representatives consider it necessary to have parallel development between economic and regulatory issues.⁶⁶

National Pricing/Reimbursement Systems

Pricing controls on pharmaceutical products marketed in the EC are implemented by almost all of the member states. Decisions on pricing by public authorities are said to be influenced by “factors such as investment commitment, employment impact, and export potential.”⁶⁷ These individual pricing systems and other factors result in different prices for pharmaceutical products in each of the member states.⁶⁸

⁶⁶ USITC field interviews in the EC with representatives of EC based and U.S.-based multinational firms and representatives of industry trade associations during Jan. 8–19, 1990.

⁶⁷ Docherty and Labaere, “The Pharmaceutical Industry,” p. 13.

⁶⁸ According to a recent article in *European Chemical News*, (Feb. 12, 1990, pp. 11–12), the member states are ranked as follows in regard to drug pricing (in order of increasing prices): Greece, Portugal, Spain, Italy, France, Belgium, the United Kingdom, Ireland, Denmark, the Netherlands, and West Germany. The article states that the president of France’s pharmaceutical industry trade association believes that “the current low prices [in France] have the perverse effect of pushing firms to compensate through increased sales.” According to EC Commission *Main Statistics on the Community’s Pharmaceutical Industry*, (p. 11), in 1987, France accounted for about 36 percent of households’ consumption of pharmaceutical products, compared with 29 percent in Italy and 18 percent in West Germany.

It is estimated that the final prices to consumers for products in member states with the highest prices and those with the lowest can vary as much as 500 percent.⁶⁹ Industry sources indicate that the differences in the prices result from differentials in factors such as the following: national reimbursement systems, distribution margins,⁷⁰ exchange rates, inflation rates, VAT rates,⁷¹ and the standards of living, in individual countries.⁷² For example, if one assumes identical manufacturers prices, differences in the VAT rates and in the “allowable” distribution margins in each member state can cause the price to the final consumer to range from about 40 percent higher than the manufacturer’s price (Portugal) to about 270 percent higher (Denmark).⁷³ The pharmacist’s margin in each member state reportedly accounts for a large share of this difference.⁷⁴

This price differentiation, in turn, results in increased parallel trade, particularly from the southern countries,⁷⁵ trade barriers, or both.⁷⁶ According to *The European Pharmaceutical Market*, parallel importation is the importation of a product from a low-priced country in to a higher priced country. Industry sources expect that increased parallel trade, which, under this scenario could result in as much as a 10-percent decrease by value in the EC market,⁷⁷ would affect primarily the multinational firms that market products throughout the EC, whether these firms are based in the United States or the EC. According to EFPIA and PMA, the undercutting in price that results from parallel trade would result in a decrease in revenue, which could potentially have a negative impact on R&D.⁷⁸

⁶⁹ Leigh Hancher, *The European Pharmaceutical Market: Problems of Partial Harmonization*, p. 9. Higher prices generally exist in the northern countries, whereas lower prices generally exist in the southern countries.

⁷⁰ The distribution margins include the wholesaler’s margin and the pharmacist’s margin.

⁷¹ The standard VAT rate for pharmaceuticals, for example, can range from 14 percent in Germany to zero in the United Kingdom.

⁷² USITC field interviews in the EC with representatives of EC-based and U.S.-based multinational firms and representatives of industry trade associations during Jan. 8–9, 1990.

⁷³ Shearson Lehman Hutton, *A Controversial Vision of the Future: Challenges Posed by Pharmaceutical Deregulation*, February 1989, pp. 66, 76 and *Main Statistics on the Community’s Pharmaceutical Industry*, p. 14. Many member states limit maximum margins for wholesalers and pharmacists.

⁷⁴ “A Controversial Vision of the Future,” p. 76; “Main Statistics on the Community’s Pharmaceutical Industry,” p. 14. According to *A Controversial Vision of the Future*, (p. 76), this margin is generally higher in countries in which local regulations allow pharmacists to own only one store (countries cited as examples of this are Denmark, West Germany, and France).

⁷⁵ “Drug Firms Fear Effect of Pricing Regulations,” Feb. 12, 1990, p. 11; According to Leigh Hancher’s *The European Pharmaceutical Market* (p. 9), parallel importation is the importation of a product from a low-priced country into a higher-priced country.

⁷⁶ Ibid.

⁷⁷ *A Controversial Vision of the Future*, p. 31.

⁷⁸ *Intradepress, Eurobrief*, Feb. 23, 1990, p. 142; According to a written submission to the Commission from Mr. Harvey E. Bale, Jr., Ph.D., Senior Vice President, International Section,

Prices are considered the "main determinant of margins, research capacities, and internationalization."⁷⁹

Individual member states also have reimbursement systems that vary from country to country. State funding ranges from 50 percent to almost 80 percent of the total bill for pharmaceuticals under individual member-state health-care systems.⁸⁰ Pharmaceutical spending, on the average, represents about 10 to 20 percent of a country's health care expenditures. As such, national authorities in some member states are implementing reforms in an effort to control expenditures.⁸¹ For example, West Germany—traditionally a country with high prices and free pricing—recently enacted the "Health Reform Act" (HRA). The HRA fixes reimbursement levels for products that are off patent and that have a relatively high volume at a level between the generic price and the original manufacturer's price (reputedly closer to the former than the latter). The HRA does not, however, set an absolute price. Under phase 2 of the HRA, a reference price will be introduced for products that are "chemically related and are pharmacologically and therapeutically comparable."⁸² whereas in phase 3, a reference price will be introduced for "products in particular combinations of products, which are not necessarily chemically related, but which are pharmacologically and therapeutically comparable."⁸³ The system has reportedly already resulted in an average decrease of about 25 to 30 percent in the prices of West German pharmaceutical products.⁸⁴ Pharmaceuticals were said to account for approximately 15 percent of production by the West German chemical industry in the first quarter of 1989.⁸⁵

⁷⁹ —Continued

Pharmaceutical Manufacturers Association, July 6, 1990 (Bale submission); As mentioned in Heinz Redwood's *The Price of Health*, lower prices for products hinder the development of research-based industry because the funding for innovation cannot be sustained.

⁸⁰ "Pharmaceutical Pricing: A Cause for French Concern," *European Chemical News*, Mar. 20, 1989, p. 20.

⁸¹ *A Controversial Vision of the Future*, p. 28.

⁸² The cost-containment programs are not directly driven by the EC 92 program.

⁸³ *Ibid.*, p. 34.

⁸⁴ *Ibid.*

⁸⁵ Within individual categories, some of the prices are said to have decreased by about 70 percent; "Pharmaceuticals '90," p. SR35; the *Verband der Chemischen Industrie e.V.*, Mar. 31, 1989, p. 11, obtained by Commission staff while on a field trip to the EC in June 1990, indicates that business in the first quarter of 1989 was "somewhat slower than in the first quarter of 1988... as a result of continued uncertainty about the effects of restructuring the health care sector."

Under the HRA, the original manufacturer has the option of reducing the product to the reimbursement level or charging the customer extra. According to industry sources, original manufacturers attempted to lower their prices to a level just above that being reimbursed. They found, however, that the consumer who was used to receiving 100-percent reimbursement opted more often for the generic product, which was generally near or at the reimbursement level.

⁸⁶ *Verband der Chemischen Industrie e.V.*, Mar. 31, 1989, p. 11, obtained by Commission staff while on a field trip to the EC in June 1990.

The Dutch are said to be considering adopting a program similar to that in West Germany. The United Kingdom has also introduced reforms in an effort to curb expenditures by the National Health System (NHS).⁸⁸ Under the new system in the United Kingdom, which is said to be controversial, physicians are expected to adhere to national drug budgets that have been established to allow for more "cost-effective prescribing," even though the United Kingdom has one of the lower rates of consumption of pharmaceuticals on a per capita basis.⁸⁷

Single-Market Authorization Procedure

The second issue of concern to the industry is the creation of a single-market authorization procedure that would be valid in all 12 member states. Such a system has to be implemented in order to create a single market in 1992 and to allow for free circulation of pharmaceutical products in the EC.

Under the most recent draft, there would be three avenues by which a company could get a product approved. The first of these is a centralized procedure that would use a reinforced version of the current Committee for Proprietary Medicinal Products (CPMP) and would be mandatory for biotechnology products and optional for high-technology products or new-chemical entities. The second route would be a decentralized procedure involving binding multistate approval. The third would be a national route that would be used solely for products intended for consumption in an individual member-state market. The multinational companies are cited as most likely to benefit under the new system because their innovation results in products that are used throughout the EC and that would gain from either a centralized process or from binding mutual recognition.⁸⁸ Smaller companies and third country companies entering the market are also expected to benefit from the decreased costs and time spent in obtaining 1 approval instead of 12.

Countries using the multistate procedure would be able to choose the country in which they wish to act as rapporteur by submitting one application. When multiple applications are submitted, the country that first receives the application would be the rapporteur. The choice of country as rapporteur is potentially important because some member states are perceived by the industry as processing such applications faster than others.

⁸⁸ According to the *Chemical Marketing Reporter* (Mar. 19, 1990, p. SR35), the NHS, which accounts for the majority of treatment in the United Kingdom, is funded by taxes.

⁸⁷ *Ibid.*; According to the article, it is estimated that the new system will reduce the profitability of companies operating in the United Kingdom, which would, in turn, result in reduced investment levels. Ultimately, the country could experience a loss of about \$1.2 billion over 10 years in its pharmaceuticals trade balance. The article also cites the following per capita rates of drug consumption in 1988 for three EC member states (the figures were issued by the Dutch pharmaceutical industry association): the United Kingdom, \$64; France, \$140; and West Germany, \$134.

⁸⁸ "Pharmaceuticals '90," p. SR35.

Under the present approval system, the delay in processing applications for authorization through the multistate option varies between member states. France is said to be adhering to the most to registration deadlines, averaging about 6 months; while other countries are experiencing delays of up to 2 to 3 years. One industry source has estimated that delays in approval of registration under the current system cost the industry about 0.5 to 1.0 percent of EC industry costs. These costs include loss of revenue from a decrease in effective patent life, loss of working capital, and the cost of staff within the company necessary to process multiple registrations.⁸⁹ The proposed system is viewed by industry as allowing for more flexibility for companies in choosing an approval route. The new system could also decrease delays in approval on a member-state level and reduce the possibility of a bureaucratic backlog of applications that would probably be associated with implementation of just one central route for approval. For the most part, the contents of the current draft are said to be similar to that discussed in the last report.⁹⁰ One significant change, however, that is of concern to the industry is a provision that would allow for the elimination of the national approval systems for Europeanwide access by 1996, except for local companies who want to market a product in one member state.

Advertising

The industry has also been watching developments in a directive in regard to the advertising of pharmaceutical products in the EC. The directive was formally proposed on June 6, 1990. In the United States, advertising of prescription products is allowed but regulated by the FDA so that consumer interests are protected. The EC Commission is currently looking at providing separate rules for advertising to the general public instead of health professionals. According to information provided recently by the EC Commission, advertisements to the public would be limited to "self-medication" products, subject to certain conditions. Advertising to health-professionals would be subject to a more complex set of rules that would concern, among other things, medical sales representatives, financial inducements, and the distribution of free samples. According to the EC information, the monitoring of such advertising, whether to the public or to healthcare professionals, is expected to be provided.

Duty Suspensions

As stated in the last report, the pharmaceutical industry is also concerned about the potential effects of the recent implementation of new EC guidelines for the granting of duty suspensions for certain products imported into the EC.⁹¹ The new

guidelines are perceived by industry to be more restrictive than earlier such guidelines and are expected to result in a lower number of duty suspensions being granted. The new guidelines are said to represent a cost to U.S. companies and may result in the relocation of some U.S. production facilities to the EC.⁹² Industry sources estimate that approximately \$600 million in duties has been suspended on EC imports of finished and raw materials, at a time when, according to industry representatives, the United States is about to grant suspensions on duties totaling about \$200 million,⁹³ in addition to those already in place.

"In an effort to recoup these revenues and to encourage local production, the [EC] Commission has adopted guidelines which deny duty suspension in the following instances:

- Where the products are subject to an exclusive trading agreement (i.e., where a U.S. company provides the products only through its subsidiaries within the EC);
- Where there are therapeutically substitutable, equivalent, or identical products available in sufficient quantities within the EC (the concept of substitutability has been scientifically proven to be inapplicable in the area of pharmaceuticals);
- Where the benefits of duty suspensions would not be passed on to the EC in the form of jobs or increased business;
- Where the goods are finished products; or
- Where the duty suspension would conflict with any other EC policy."⁹⁴

Industry representatives are seeking to resolve the issue in the GATT Uruguay Round via a multilateral agreement. According to the industry, however, even if this approach is successful, implementation could take several years.⁹⁵

Patent-Term Restoration

The patent-term restoration issue is also important to both the U.S. and the EC industry. The United States enacted legislation about 6 years ago that allows for the extension of the effective patent life of a product by up to 5 years, depending on the amount of time lost during regulatory review. Japan reportedly also enacted legislation for this purpose in 1988. The EC directives on biotechnology and high technology that were

⁸⁹ Bale submission.

⁹⁰ *Ibid.*; Chemicals and pharmaceuticals are said to represent about half of the total revenue loss, or about \$300 million.

⁹¹ *Ibid.*; The Bale submission also indicates that companies are also required to submit substantial information that could be proprietary with their application for a duty suspension. This is considered yet another barrier to the export of goods or raw materials to the EC.

⁹² *Ibid.*

⁸⁹ Paolo Cecchini, *The European Challenge 1992*, p. 67.
⁹⁰ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-76 to 6-79.

⁹¹ *Ibid.*, p. 6-71.

adopted in 1986 incorporated a limited degree of protection to these two product groupings, basically allowing for qualified protection for confidentiality of data.⁹⁶

A regulation on patent restoration that allows for the creation of a supplementary protection certificate for medicinal products was recently issued. The certificate is regarded by many as a device rather than a patent. The certificate, based on legislation recently introduced in France, would automatically take effect when a patent expires and would cover the particular indications registered for the product at the time of expiration. The additional period of market exclusivity would vary but would be a maximum of 10 years. Provisions are also made for patented drugs that have received marketing approval after January 1984 and whose patents are expected to expire after July 1992.

Anticipated Industry Response and Likely Market Structure

Chemicals

The response of the U.S. chemical industry to the economic merger of the EC nations and the accompanying facilitating directives has been somewhat moderated by the apparent lack of knowledge on the part of many firms in the domestic industry. Although many of the larger multinational firms already active both producing in the United States and selling in the U.S. market have either affiliates or parent companies based in EC member nations, the amount of communications regarding the EC 92 directives to have generally reached the U.S. companies has been relatively meager. It is particularly the small producer that is markedly unaware of the major imminent changes in the market situation.

There is almost unanimous agreement among those U.S. companies that are maintaining a close watch on EC developments that those firms with active investments in the EC market, either by affiliations, subsidiaries, or joint ventures, will probably benefit in the long run from the EC 92 program. This view expressed by many industry representatives also anticipates increasing advantages in the long run associated with Eastern European nations and their inability to meet their own consumers' demands for consumer-oriented chemical products. Most of the directives pertaining to the chemical industry, although at times generating additional costs for the producers, are viewed as somewhat simplifying the marketing of products within the Community. For example, U.S. chemical producers will no longer be subject to a multitude of different regulations when submitting new products for initial approval into the

⁹⁶ European Federation of Pharmaceutical Industries' Associations, *Memorandum on the Need of the European Pharmaceutical Industry for Restoration of Effective Patent Term for Pharmaceuticals*, p. 5.

member nations' markets. Once a testing mechanism is finalized for new product approval within the EC, the approved test will be one that will be acceptable in all of the member nations. Also, with the consolidation of many of the ingredient requirements for chemical products such as laundry detergents, U.S. firms will no longer be forced to have a variety of formulations of the same product for different member nations.

As the prospective European Environmental Agency has yet to have its form or its rules content finalized, the U.S. chemical industry is not yet sure whether its response will be positive, negative, or mixed. Those firms already active throughout the EC market are anticipating a simplification in their procedural requirements, although there may well be an inevitable increase in the bureaucracy in the EC, as well as an increase in the level of regulation. Firms that deal in the EC market through trade rather than through affiliates also see increased levels of regulation and enforcement as necessary for the environment and welcome any simplification of their product approval procedures as beneficial.

In general, the prospect of producing a product, either in the United States for export to EC nations, by a subsidiary or affiliate in an EC nation, or both, marketable throughout the EC without different standards and requirements associated with marketing, chemical content, or labeling will increase the economies of production of these products and will probably be looked upon favorably by the U.S. chemical industry.

Although there is no expected change in the overall structure of the U.S. chemical industry's presence in the EC as a result of the EC 92 program, there is an expectation that there will be an increase in both the number of U.S. firms involved in EC nations and in the size of the average investment in the EC chemical industry. Most U.S. firms currently active in the EC agree that entering the EC market may become more difficult as the economic unification progresses, less because of European nationalism than because of the increased desirability of doing business in EC nations and the increased level of competition that will result.⁹⁷

Pharmaceuticals

Producers of pharmaceuticals in the EC, including subsidiaries of U.S. multinationals operating in Europe, are all watching the direction of the ongoing harmonization for 1992. Representatives of the pharmaceutical industry have been actively involved in the directive-drafting process, and in general, their overall reaction is

⁹⁷ Based on conversations with representatives of U.S. industry associations; "Getting Set for 1992," *Chemical & Engineering News*, Oct. 12, 1988, pp. 30-32; and "U.S. Chemical Companies Ponder Europe after 1992," *Chemical & Engineering News*, Nov. 6, 1989, pp. 7-13.

positive. The primary effect of many of the directives that have already been proposed would be to put into EC law provisions that are already in effect at the member-state level. It is believed that many of the changes should result in a premarketing approval process that is easier to use and more efficient.⁹⁸ Industry sources expect that most of the directives proposed, if not all, will apply in the same manner to both EC-based and U.S.-based pharmaceutical firms operating in the EC, as well as to firms of other countries operating in the EC. U.S.-based companies are well established in the European market⁹⁹ and, according to some sources, might be better placed than many EC-based firms to take advantage of the opportunities presented by the harmonization of the market since U.S.-based firms already routinely operate in and among all 12 member states.¹⁰⁰

National Pricing/Reimbursement Systems

There are differing opinions in industry on how to best resolve the pricing issue. Industry sources have expressed concern that if prices in the member states converge under the single market¹⁰¹ or if an "average" EC price for individual products is set at a median level between the highest and lowest prices, then consumers living in countries with lower standards of living would not be able to afford the higher priced product and companies operating in countries that traditionally have had higher prices could lose revenue that could be used for various programs, including the funding of R&D efforts.

Most industry sources believe that the EC Commission will not be taking any action in regard to the pricing systems of individual member states.¹⁰² According to one source, however, under the Transparency Directive, the EC Commission will be required to submit by January 1, 1992, any additional proposals that are deemed necessary to "eliminate the disruptive effects which the existence of national controls may have on the operation of the internal market."¹⁰³ At this time, member states will be required to provide the EC Commission with detailed information about their national pricing systems.¹⁰⁴

The Transparency Directive, which became effective January 1, 1990, addresses part of the concern on pricing. It sets forth procedural provisions relating to the time limits for member

states making pricing decisions, the citing of criteria used by member states in making the decision, and the rights of appeal and publication of the decisions.¹⁰⁵ It has been suggested that the directive could reduce discriminatory practices, particularly overt national practices associated with factors such as investment, that have been associated with some past official pricing decisions. The industry "questions any implication, however, that the directive would in any way positively impact trade."¹⁰⁶ Industry representatives stress that the directive does not address the issue of restrictive price controls or the effect of parallel imports on prices once the single market is created.¹⁰⁷ All member states are considered "free to keep such restrictions in place or, if they so choose, to impose even more onerous restrictions."¹⁰⁸

The cost-containment programs being enacted are expected to affect R&D in the EC. Currently, the pharmaceutical firms in countries with higher prices for pharmaceuticals generally have better established and ongoing R&D efforts than firms in countries with lower priced products.¹⁰⁹ France, Switzerland, the United Kingdom, and West Germany incurred R&D expenses of approximately \$5.2 billion, or about 76 percent of the European total in 1987.¹¹⁰ Some West German companies, however, have suggested that production will decrease by as much as 25 percent as a result of the new national pricing system, which, in turn, could reduce R&D expenditures in the future.¹¹¹ According to a trade association in one of the member states stated, ignoring the idea that "reasonable prices" are necessary to continue R&D spending "would lead to an eventual dissolution of the European industry, with dependence for new medicines being handed on a plate to the United States and Japan."¹¹²

A number of industry sources have also suggested that some EC R&D facilities, funds, or both, could "emigrate," particularly to the United States.¹¹³ Two observations by industry sources appear to support this possibility. First of all, it is perceived that companies will not invest funds in countries whose pricing policies do not allow for profitable operations.¹¹⁴ Secondly, some genetic engineering and biotechnology operations in

⁹⁸ U.S. Department of Commerce, *Europe Now: A Report*, Winter 1989-90, p. 2.

⁹⁹ One industry source has mentioned that subsidiaries of U.S. companies in the EC have been referred to as "European companies of American parentage."

¹⁰⁰ According to the U.S. Department of Commerce publication *Europe Now*, (p. 2), increased investment by companies not already operating in the EC could have a negative effect on all firms operating in Europe by increasing competition.

¹⁰¹ Heinz Redwood, *The Price of Health*, 1989, p. 44.

¹⁰² Bale submission.

¹⁰³ EC Commission, *The Rules Governing Medicinal Products in the European Community*, 1989, vol. 1, p. 19.

¹⁰⁴ *Ibid.*

¹⁰⁵ *Ibid.*

¹⁰⁶ Bale submission.

¹⁰⁷ *Ibid.*; *Intradepress, Eurobrief*, Feb. 23, 1990, p. 142.

¹⁰⁸ Bale submission.

¹⁰⁹ As mentioned previously, generic products become less competitive with branded products as the price differential between the two narrows.

¹¹⁰ EFPIA, *EFPIA in Figures: 1986-87*, (1988), p. 19.

¹¹¹ It has been stated in Heinz Redwood's *The Price of Health* (p. 45) that "no country that has practiced cost containment in health care at the expense of its pharmaceutical industry has managed to nurture a pharmaceutical industry that can compete globally;" "Pharmaceuticals '90," p. SR35.

¹¹² "Drug Firms Fear Effect of Pricing Regulations," p. 11.

¹¹³ Heinz Redwood, *The Price of Health*, p. 43; "Pharmaceuticals '90," p. SR35.

¹¹⁴ *Ibid.*

West Germany could be relocated as a result of "tough safety regulations on biotechnology" that are being implemented on both a national and a state level.¹¹⁵ According to industry sources, this legislation has been prompted in part by expressions of concerns by special interest groups, such as environmentalists.

Generics

The efforts to control expenditures by national health authorities are expected to increase the market for generic products, produced by both innovative companies and independent generics manufacturers. In 1988, generics accounted for an estimated 7 percent of the EC market, or about \$2.7 million. One industry source has estimated that by 1994 the market for generics will be valued at about \$3.5 million. It is expected, however, that eventually, as prices decrease in countries that have implemented new pricing systems to reduce costs, the increase in the generics market will level off as the prices of generic products become less competitive with those of branded products.

In the United Kingdom and West Germany, sales of generics reportedly account for 13 percent of the individual markets. One generic company in West Germany is expected to be a market leader in the next few years. Generics also have a strong position in the Netherlands. According to industry sources, there is less of a generic industry in the southern countries because the prices are not high enough to make such an industry profitable.¹¹⁶

Single-market Authorization Procedure

In regard to the single-market authorization procedure, the U.S. pharmaceutical industry would like to emphasize that its opinion was sought in regard to the creation of this system and that the EC Commission has already addressed a number of the concerns raised by the industry.¹¹⁷ For the most part, the contents of the current draft are said to be similar to that discussed in the last report.¹¹⁸ The industry is concerned, however, about the provision that would allow for the elimination of the national approval systems for Europeanwide access by 1996, except for local companies who want to market a product in one member state. The U.S. industry currently uses the national systems fairly extensively. Representatives of the industry have made the suggestion that all the systems remain in place until 1996, at which time the systems and their use could be reviewed and modified appropriately.

¹¹⁵ "Pharmaceuticals '90," p. SR35. The article cites BASF and Henkel as two examples: BASF is said to be building a new facility in Massachusetts after it was prevented from doing so in West Germany; Henkel has relocated its biotechnology research to a new plant in California.

¹¹⁶ USITC field interviews in the EC with representatives of EC-based and U.S.-based multinational firms and representatives of industry associations during Jan. 8-19, 1990.

¹¹⁷ Bale submission.

¹¹⁸ USITC, *Effects of EC Integration*, USITC Publication 2268, March 1990, pp. 6-76 to 6-79.

The industry also suggests that while the new system is being implemented, a transition period should be in effect to allow the industry to retain access to the existing national approval route. The new system is expected to take some time to implement and, because of the scope of the changes instituted by the new authorization procedures, could experience temporary bottlenecks. Access to the national routes would allow for an "escape valve" for the industry.¹¹⁹

Industry sources expect that once the single market and the single-market authorization procedure are in place, third countries, such as Japan, will find it easier to enter the EC market since they will be facing 1 set of criteria rather than 12, according to industry sources. Additional consolidation in the industry could occur as more firms merge, participate in joint ventures, or both in order to optimize R&D expenditures and to more efficiently access the EC market. It should be noted, however, that consolidation is perceived as an ongoing trend in the pharmaceutical industry. According to industry sources, the creation of the single market may well further such plans that are already under way and be a consideration in future such plans, but should probably not be considered the single motivational factor in future such plans.

Patent-Term Restoration

Industry representatives believe that the extension of patent protection will be an "important contribution to restoring the economic viability of the pharmaceutical industry in Europe. This, in turn, should enable the industry to maintain its R&D commitment," allowing it to be more competitive with the U.S. and Japanese industries.¹²⁰ By extending the effective patent term of certain products, this proposal will allow innovative companies to recover part of their ongoing investment in R&D.

CEFIC, the Conseil Europeen des Federations de l'Industrie Chimique, has stated that it "recognizes the problems faced by the pharmaceutical and agrochemical sectors" in regard to reduced effective patent life resulting from the increasing amount of time expended in seeking marketing approval for a product and that it "also recognizes that these problems are immediate and that a solution is urgently needed."¹²¹ CEFIC also indicates, however, that other chemical sectors might also experience reduced periods of effective patent terms for products as the result "of the broad operations of the chemical industry."¹²² CEFIC suggests that any device created to resolve this situation be capable of being extended to cover other chemical sectors as necessary.

¹¹⁹ Bale submission.

¹²⁰ Ibid.

¹²¹ According to a CEFIC position paper entitled "CEFIC Memorandum on Patent Term Restoration," June 1989, that was obtained by a USITC staff member on a field trip to the EC in June 1990.

¹²² Ibid.; In the memorandum, CEFIC cites as an example "having to meet national requirements relating to the use of chemicals, operation of processes, or marketing of products."

APPENDIXES

APPENDIX A
REQUEST LETTER

Congress of the United States
Washington, DC 20515

October 11, 1988

88 OCT 13 11:01

OFFICE OF THE CLERK
DOCKET/USITC

OFFICE OF THE CLERK

88 OCT 13 11:16

DOCKET	DOCKET NUMBER
	1469
Office of the Secretary	
1111 1111 1111	

The Honorable Anne Brunsdale
Acting Chairman
U.S. International Trade Commission
500 E Street, S.W.
Washington, D.C. 20436

Dear Madam Chairman:

A development of major international importance and of increasing interest to the House Committee on Ways and Means and the Senate Committee on Finance is the economic integration of the European Community (EC) into a single market, scheduled to be in place by the end of 1992. The form and content of the policies, laws, and directives removing economic barriers and restrictions and harmonizing practices among the EC member states may have a significant impact on U.S. trade and investment and on U.S. business activities within Europe, overall and in particular sectors. The process of creating a single market may also affect progress and results in the ongoing Uruguay Round of GATT multilateral trade negotiations.

In order to provide a basic understanding of these developments, their significance, and possible effects, on behalf of the Committees we are requesting that the U.S. International Trade Commission conduct an investigation under section 332(g) of the Tariff Act of 1930 to provide objective factual information on the EC single market and a comprehensive analysis of its potential economic consequences for the United States.

The Commission's report should focus on the following aspects of the proposed single market, in particular:

1. The anticipated changes in laws, regulations, policies, and practices of the EC and individual member states that may affect U.S. exports to the EC and U.S. investment and business operating conditions in Europe, such as changes in customs requirements and procedures, government procurement practices, investment policies, services directives, and tax systems. The analysis should include consideration of the relationship and differences between policies and principles, such as sectoral reciprocity, proposed for the EC single market and current EC or

The Honorable Anne Brunsdale
October 11, 1988

member state obligations and commitments under bilateral or multi-lateral agreements and codes to which the United States is a party.

2. The likely impact of such changes on major sectors of U.S. exports to the EC, such as agricultural trade and telecommunications.

3. An assessment of whether particular elements of the single market may be trade liberalizing or trade discriminatory with respect to third countries, particularly the United States.

4. The relationship and possible impact of the single market exercise on the Uruguay Round of GATT multilateral trade negotiations.

We understand that the European Community intends to accomplish its goal of a unified market through the adoption of some 286 Internal Market Directives, which currently are in various stages of preparation, and that a text is not yet available to the public for approximately one-fourth of the proposed directives.

Given the great diversity of topics which these directives address, and the fact that the remaining directives will become available on a piecemeal basis, the Commission should provide the requested information and analysis to the extent feasible in an initial report by July 15, 1989, with follow-up reports as necessary to complete the investigation as soon as possible thereafter. Shortly after receipt of this letter, Commission staff should consult with staffs of our Committees to agree on the topics to be covered in the initial report.

In preparing these reports, the Commission should seek views and input from the private sector. The Commission should also cooperate with and utilize existing information available from U.S. Government agencies to the fullest extent possible.

Sincerely yours,



Lloyd Bentsen
Chairman
Committee on Finance



Dan Rostenkowski
Chairman
Committee on Ways and Means

APPENDIX B
FEDERAL REGISTER NOTICES

LTFV imports of generic cephalixin capsules from Canada. Accordingly, effective October 27, 1988, the Commission instituted preliminary antidumping investigation No. 731-TA-423 (Preliminary).

Notice of the institution of the Commission's investigation and of a public conference to be held in connection therewith was given by posting copies of the notice in the Office of the Secretary, U.S. International Trade Commission, Washington, DC, and by publishing the notice in the *Federal Register* of November 4, 1988 (53 FR 44676). The conference was held in Washington, DC, on November 16, 1988, and all persons who requested the opportunity were permitted to appear in person or by counsel.

The Commission transmitted its determination in this investigation to the Secretary of Commerce on December 12, 1988. The views of the Commission are contained in USITC Publication 2143 (December 1988), entitled "Generic Cephalixin Capsules from Canada: Determination of the Commission in Investigation No. 731-TA-423 (Preliminary) Under the Tariff Act of 1930. Together With the Information Obtained in the Investigation."

By order of the Commission.

Issued: December 14, 1988.

Kenneth R. Mason,

Secretary.

[FR Doc. 88-29293 Filed 12-20-88; 8:45 am]

BILLING CODE 7020-02-M

[332-267]

The Effects of Greater Economic Integration Within the European Community on the United States

AGENCY: United States International Trade Commission.

ACTION: Institution of investigation and scheduling of hearing.

SUMMARY: Following receipt on October 13, 1988 of a request from the Committee on Ways and Means of the United States House of Representatives and the Committee on Finance of the United States Senate, the Commission instituted investigation No. 332-267 under section 332(g) of the Tariff Act of 1930 (19 U.S.C. 1332(g)) to provide objective factual information on the EC single market and a comprehensive analysis of its potential economic consequences for the United States. The Committee requested that the Commission investigation focus in particular on the following:

1. The anticipated changes in laws, regulations, policies, and practices of

the EC and individual member states that may affect U.S. exports to the EC and U.S. investment and business operating conditions in Europe, such as changes in customs requirements and procedures, government procurement practices, investment policies, service directives, and tax systems. The Committees requested that the analysis include consideration of the relationship and differences between policies and principles, such as sectoral reciprocity, proposed for the EC single market and current EC or member state obligations and commitments under bilateral or multilateral agreements and codes to which the United States is a party.

2. The likely impact of such changes on major sectors of U.S. exports to the EC, such as agricultural trade and telecommunications.

3. An assessment of whether particular elements of the single market may be trade liberalizing or trade discriminatory with respect to third countries, particularly the United States.

4. The relationship and possible impact of the single market exercise on the Uruguay Round of GATT multilateral trade negotiations.

The Committees requested that the Commission provide the requested information and analysis to the extent feasible in an initial report by July 15, 1989, with follow up reports as necessary.

EFFECTIVE DATE: December 13, 1988.

FOR FURTHER INFORMATION CONTACT: For information on other than the legal aspects of the investigation contact either Mr. John J. Gersic at 202-252-1342, or Mr. David R. Konkel at 202-252-1451.

For information on legal aspects of the investigation contact Mr. William W. Gearhart at 202-252-1091.

PUBLIC HEARING: A public hearing in connection with the investigation will be held in the Commission Hearing Room, 500 E Street SW., Washington, DC, beginning at 9:30 a.m. on April 11, 1989, and continuing as required on April 12, 1989. All persons shall have the right to appear by counsel or in person, to present information, and to be heard. Persons wishing to appear at the public hearing should file requests to appear and should file prehearing briefs (original and 14 copies) with the Secretary, United States International Trade Commission, 500 E Street SW., Washington, DC 20436, not later than 5:00 p.m., March 28, 1989. Post-hearing briefs may be submitted no later than April 26, 1989.

WRITTEN SUBMISSIONS: In lieu of or in addition to appearances at the public hearing, interested persons are invited to submit written statements concerning

the investigation. Written statements should be received by the close of business on April 26, 1989. Commercial or financial information which a submitter desires the Commission to treat as confidential must be submitted on separate sheets of paper, each clearly marked "Confidential Business Information" at the top. All submissions requesting confidential treatment must conform with the requirements of § 201.6 of the Commission's *Rules of Practice and Procedure* (19 CFR 201.6). All written submissions, except for confidential business information, will be available for inspection by interested persons. All submissions should be addressed to the Secretary at the Commission's office in Washington, DC.

Hearing impaired persons are advised that information on this matter can be obtained by contacting the Commission's TDD terminal on (202)-252-1810.

By order of the Commission.

Issued: December 15, 1988.

Kenneth R. Mason,

Secretary.

[FR Doc. 88-29291 Filed 12-20-88; 8:45 am]

BILLING CODE 7020-02-M

[Investigation No. 337-TA-279]

Certain Plastic Light Duty Screw Anchors; Commission Determination Not To Review Initial Determination and Schedule for Filing of Written Submissions on Remedy, the Public Interest, and Bonding

AGENCY: U.S. International Trade Commission.

ACTION: Notice.

SUMMARY: Notice is hereby given that the U.S. International Trade Commission has determined not to review an initial determination (ID) finding a violation of section 337 of the Tariff Act of 1930 in the above-captioned investigation. The parties to the investigation, interested government agencies, and interested members of the public are requested to file written submissions on the issues of remedy, the public interest, and bonding.

FOR FURTHER INFORMATION CONTACT: Mitchell W. Dale, Esq., Office of the General Counsel, U.S. International Trade Commission, telephone 202-252-1087.

SUPPLEMENTARY INFORMATION: The authority for the Commission's disposition of this matter is contained in section 337 of the Tariff Act of 1930 (19 U.S.C. 1337) and in §§ 210.53(h) and 210.58(a) of the Commission's Interim

§ 207.22 of the Commission's rules (19 CFR § 207.22) each party is encouraged to submit a prehearing brief to the Commission. The deadline for filing prehearing briefs is November 8, 1989.

Testimony at the public hearing is governed by § 207.23 of the Commission's rules (19 CFR 207.23). This rule requires that testimony be limited to a nonbusiness proprietary summary and analysis of material contained in prehearing briefs and to information not available at the time the prehearing brief was submitted. Any written materials submitted at the hearing must be filed in accordance with the procedures described below and any business proprietary materials must be submitted at least three (3) working days prior to the hearing (see § 201.6(b)(2) of the Commission's rules (19 CFR 201.6(b)(2)).

Written submissions. Prehearing briefs submitted by parties must conform with the provisions of § 207.22 of the Commission's rules (19 CFR 207.22) and should include all legal arguments, economic analyses, and factual materials relevant to the public hearing. Posthearing briefs submitted by parties must conform with the provisions of § 207.24 (19 CFR 207.24) and must be submitted not later than the close of business on November 20, 1989. In addition, any person who has not entered an appearance as a party to the investigation, may submit a written statement of information pertinent to the subject of the investigation on or before November 20, 1989.

A signed original and fourteen (14) copies of each submission must be filed with the Secretary to the Commission in accordance with § 201.8 of the Commission's rules (19 CFR 201.8). All written submissions except for business proprietary data will be available for public inspection during regular business hours (8:45 a.m. to 5:15 p.m.) in the Office of the Secretary to the Commission.

Any information for which business proprietary treatment is desired must be submitted separately. The envelope and all pages of such submissions must be clearly labeled "Business Proprietary Information." Business proprietary submissions and requests for business proprietary treatment must conform with the requirements of §§ 201.6 and 207.7 of the Commission's rules (19 CFR 201.6 and 207.7).

Parties which obtain disclosure of business proprietary information pursuant to § 207.7(a) of the Commission's rules (19 CFR 207.7(a)) may comment on such information in their prehearing and posthearing briefs, and may also file additional written

comments on such information no later than November 24, 1989. Such additional comments must be limited to comments on business proprietary information received in or after the posthearing briefs.

Authority: This investigation is being conducted under authority of the Tariff Act of 1930, title VII. This notice is published pursuant to § 207.20 of the Commission's rules (19 CFR 207.20).

Issued: September 15, 1989.

By order of the Commission.

Kenneth R. Mason,

Secretary.

[FR Doc. 89-22212 Filed 9-19-89; 8:45 am]

BILLING CODE 7020-02-M

[332-267]

Effects of Greater Economic Integration Within the European Community on the United States

AGENCY: United States International Trade Commission.

ACTION: Scheduling of followup reports.

SUMMARY: Following receipt on October 13, 1988, of a request from the Committee on Ways and Means of the United States House of Representatives and the Committee on Finance of the United States Senate, the Commission instituted investigation No. 332-267 under section 332(g) of the Tariff Act of 1930 (19 U.S.C. 1332(g)) to provide objective factual information on the EC single market and a comprehensive analysis of its potential economic consequences for the United States. The Committees requested that the Commission provide the requested information and analysis to the extent feasible in an initial report by July 15, 1989, with followup reports as necessary to complete the investigation. Notice of institution of the investigation and scheduling of a hearing was published in the Federal Register of December 21, 1988 (53 DR 51328).

The report on the initial phase of the investigation was sent to the Committees on Monday, July 17, 1989; copies of the report "The Effects of Greater Economic Integration within the European Community on the United States" (Investigation 332-267, USITC Publication 2204, July 1989) may be obtained by calling 202-252-1809 or from the Office of the Secretary, U.S. International Trade Commission, 500 E St. SW., Washington, DC 20436. Requests can also be faxed to 202-252-2186.

Followup reports will be issued approximately every 6 months. Each will summarize the previous report and EC

single market directives that become available after the cutoff date of the previous report. The followup reports will have a format similar to the original report.

EFFECTIVE DATE: September 11, 1989.

FOR FURTHER INFORMATION CONTACT: For further information on other than the legal aspects of the investigation contact Mr. John J. Gersic at 202-252-1342. For further information on the legal aspects of the investigation contact Mr. William W. Gearhart at 202-252-1091.

WRITTEN SUBMISSIONS: Interested persons are invited to submit written statements concerning the investigation. Written submissions to be considered by the Commission for the second report should be received by the close of business on November 30, 1989. Commercial or financial information which a submitter desires the Commission to treat as confidential must be submitted on separate sheets of paper, each marked "Confidential Business Information" at the top. All submissions requesting confidential treatment must conform with the requirements of § 201.8 of the Commission's Rules of Practice and Procedure (19 CFR 201.8). All written submissions, except for confidential business information, will be available for inspection by interested persons. All submissions should be addressed to the Secretary at the Commission's office in Washington, D.C.

Hearing impaired persons are advised that information on this matter can be obtained by contacting the Commission's TDD terminal on 202-252-1810.

Issued: September 13, 1989.

By order of the Commission.

Kenneth R. Mason,

Secretary.

[FR Doc. 89-22210 Filed 9-19-89; 8:45 am]

BILLING CODE 7020-02-M

New Steel Rails From Canada (Final); Determinations

On the basis of the record¹ developed in the subject investigations, the Commission determines,² pursuant to section 705(b) of the Tariff Act of 1930 (19 U.S.C. 1671d(b)), that an industry in the United States is threatened with

¹ The record is defined in § 207.2(h) of the Commission's Rules of Practice and Procedure (19 CFR 207.2(h)), as amended, 53 FR 33041 (Aug. 29, 1988).

² Chairman Brunsdale, Vice Chairman Cass, and Commissioner Ludwick dissenting.

(1) A reservation to the United States of a right-of-way for ditches or canals under the Act of August 30, 1890.

(2) Valid existing rights including but not limited to any right-of-way, easement, or lease of record.

(3) Mineral estates will be transferred with the surface on both the non-Federal and Federal lands.

Publication of this notice has the effect of segregating all of the above described Federal land from appropriation under the public land laws and these lands are further segregated from appropriation under the mining laws, but not from exchange pursuant to section 206 of the Federal Land Policy and Management Act of 1976. The segregative effect of this notice will terminate upon issuance of patent or in two years from the date of the publication of this notice, whichever occurs first.

Detailed information concerning the exchange is available for review at the Salmon District Office of the Bureau of Land Management, Highway 93 South, Salmon, Idaho 83467.

For a period of 45 days, interested parties may submit comments to the Salmon District Manager at the above address. Any adverse comments will be evaluated by the Idaho State Director, BLM, who may vacate or modify this realty action and issue a final determination. In the absence of any action by the State Director, this realty action will become the final determination of the Department of the Interior.

Dated: March 23, 1990.

Katbe Rhodes,

Acting District Manager.

[FR Doc 90-7659 Filed 4-3-90; 8:45 am]

BILLING CODE 4310-00-M

INTERNATIONAL TRADE COMMISSION

(Investigation No. 731-TA-438 (Final))

Limousines from Canada

AGENCY: United States International Trade Commission.

ACTION: Termination of investigation.

SUMMARY: On March 29, 1990, the Commission received a letter from petitioner in the subject investigation (Southampton Coachworks, Ltd., Farmingdale, NY), withdrawing its petition. Accordingly, pursuant to § 207.40(a) of the Commission's Rules of Practice and Procedure (19 CFR 207.40(a)), the antidumping investigation concerning limousines from Canada

(investigation No. 731-TA-438 (Final)) is terminated.

EFFECTIVE DATE: March 29, 1990.

FOR FURTHER INFORMATION CONTACT: Mary Trimble (202-252-1193), Office of Investigations, U.S. International Trade Commission, 500 E Street SW., Washington, DC 20438. Hearing-impaired individuals are advised that information on this matter can be obtained by contacting the Commission's TDD terminal on 202-252-1810. Persons with mobility impairments who will need special assistance in gaining access to the Commission should contact the Office of the Secretary at 202-252-1000.

Authority: This investigation is being terminated under authority of the Tariff Act of 1930, title VII. This notice is published pursuant to § 207.40 of the Commission's rules (19 CFR 207.40).

By order of the Commission.

Kenneth R. Mason,

Secretary.

Issued: March 30, 1990.

[FR Doc. 90-7808 Filed 4-2-90; 9:20 am]

BILLING CODE 7020-02-1

(Investigation No. 337-TA-309)

Certain Athletic Shoes With Viewing Windows; Decision Not To Review an Initial Determination

AGENCY: United States International Trade Commission.

ACTION: Notice.

SUMMARY: Notice is hereby given that the Commission has determined not to review the presiding administrative law judge's (ALJ's) initial determination (ID) granting a motion for leave to file an amended complaint in the above-captioned investigation.

FOR FURTHER INFORMATION CONTACT: William T. Kane, Esq., Office of the General Counsel, U.S. International Trade Commission, 500 E Street, SW., Washington, DC 20438; telephone: (202)-252-1116. Copies of the nonconfidential version of the ID and all other nonconfidential documents filed in connection with this investigation are available for inspection during official business hours (8:45 a.m. to 5:15 p.m.) in the Office of the Secretary, U.S. International Trade Commission, 500 E Street SW., Washington, DC 20438; telephone: (202)-252-1000. Hearing-impaired individuals are advised that information on this matter can be obtained by contacting the Commission's TDD terminal at (202)-252-1810.

SUPPLEMENTARY INFORMATION: The Commission voted to institute this investigation on January 16, 1990. The notice of investigation was published in the Federal Register on January 23, 1990. (55 FR 2421-2). On February 9, 1990, complainant Autry Industries, Inc., filed a motion (Motion No. 309-1) for leave to file an amended complaint. On February 21, 1990, respondent Reebok International Ltd. filed a response in opposition to the motion, and the Commission investigative attorney filed a response indicating no opposition to the motion. On February 23, 1990, the presiding ALJ issued an ID (Order No. 3) granting complainant's motion. No petitions for review or agency comments were received.

This action is taken pursuant to section 337 of the Tariff Act of 1930, as amended (19 U.S.C. 1337), and Commission interim rules 210.53-210.55 (19 CFR 210.53-210.55, as amended).

Issued: March 28, 1990.

By order of the Commission.

Kenneth R. Mason,

Secretary.

[FR Doc. 90-7711 Filed 4-3-90; 8:45 am]

BILLING CODE 7020-02-M

(332-267)

The Effects of Greater Economic Integration Within the European Community on the United States

AGENCY: United States International Trade Commission.

ACTION: Scheduling of public hearing and deadline for submissions in connection with second follow-up report.

SUMMARY: The Commission has commenced work on the second of a series of follow-up reports updating its initial report issued in July 1989 in connection with investigation No. 332-267, *The Effects of Greater Economic Integration Within the European Community on the United States*. The reports were requested under section 332(g) of the Tariff Act of 1930 (19 U.S.C. 1332(g)) by the House Committee on Ways and Means and the Senate Committee on Finance in a letter received on October 13, 1988. Notice of the institution of the investigation and scheduling of a public hearing was published in the Federal Register of December 21, 1988 (53 FR 51328), and notice of the procedure to be followed in follow-up reports was published in the Federal Register of September 20, 1989 (54 FR 38751).

The second follow-up report will follow a format similar to that of the earlier reports. However, the second follow-up report will contain, in addition, new chapters on R & D and technology and an analysis of the impact of EC integration efforts on three U.S. industries—automobile, telecommunications, and chemicals/pharmaceuticals. Persons having an interest in these areas or industries in particular, or any of the matters covered by the reports, may be interested in participating in the Commission's June 21, 1990, public hearing and/or in making written submissions in accord with the procedures set forth below.

The report on the initial phase of the investigation was sent to the Committees on Monday, July 17, 1989. The first follow-up report was sent to the Committees on Friday, March 30, 1990. Copies of either the initial report, *The Effects of Greater Economic Integration Within the European Community on the United States* (Investigation 332-267, USITC Publication 2204, July 1989) or the first follow-up report (Investigation 332-267, USITC Publication 2268, March 1990) may be obtained by calling 202-252-1809, or from the Office of the Secretary, U.S. International Trade Commission, 500 E Street SW., Washington, DC 20436. Requests can also be faxed to 202-252-2188.

The second follow-up report will be sent to the Committees on September 28, 1990.

EFFECTIVE DATE: March 23, 1990.

FOR FURTHER INFORMATION CONTACT: For further information on other than the legal aspects of the investigation contact Mr. John J. Gersic at 202-252-1342. For information on the legal aspects of the investigation contact Mr. William W. Gearhart at 202-252-1091.

PUBLIC HEARING: A public hearing in connection with the investigation will be held in the Commission Hearing Room, 500 E Street SW., Washington, DC, beginning at 9:30 a.m. on June 21, 1990. All persons shall have the right to appear by counsel or in person, to present information, and to be heard. Persons wishing to appear at the public hearing should file requests to appear and should file prehearing briefs (original and 14 copies) with the Secretary, United States International Trade Commission, 500 E Street SW., Washington, DC 20436, not later than 5 p.m., June 7, 1990. Post-hearing briefs may be submitted no later than July 5, 1990.

WRITTEN SUBMISSIONS: In lieu of or in addition to appearances at the public hearing, interested persons are invited

to submit written statements concerning the investigation. Written submissions to be considered by the Commission for the second follow-up report should be received by the close of business on July 6, 1990. Commercial or financial information which a submitter desires the Commission to treat as confidential must be submitted on separate sheets of paper, each marked "Confidential Business Information" at the top. All submissions requesting confidential treatment must conform with the requirements of § 201.6 of the Commission's *Rules of Practice and Procedure* (19 CFR 201.6). All written submissions, except for confidential business information, will be available for inspection by interested persons. All submissions should be addressed to the Secretary at the Commission's office in Washington, DC.

Hearing impaired persons are advised that information on this matter can be obtained by contacting the Commission's TDD terminal on 202-252-1810.

By order of the Commission.

Issued: March 28, 1990.

Kenneth R. Mason,
Secretary.

[FR Doc. 90-7709 Filed 4-3-90; 8:45 am]

BILLING CODE 7020-02-M

DEPARTMENT OF JUSTICE

Lodging of Modified Consent Decree Pursuant to the Clean Water Act

In accordance with Departmental policy, 28 CFR 50.7, notice is hereby given that a proposed Modified Consent Decree in *United States v. City of New Bedford* has been lodged with the United States District Court for the District of Massachusetts. The modified consent decree addresses alleged violations by the City of New Bedford, MA of the 1987 Consent Decree.

The proposed Modified Consent Decree revises various parts of the 1987 Consent Decree, including the facility's planning schedules for the secondary wastewater treatment plant and combined sewer overflow ("CSO") abatement projects. The Modified Consent Decree also requires New Bedford to pay to the United States stipulated penalties in the amount of \$60,000.

The Department of Justice will receive for a period of thirty (30) days from the date of this publication comments relating to the proposed Modified Consent Decree. Comments should be addressed to the Assistant Attorney General, Land and Natural Resources

Division, Department of Justice, Washington, DC 20530, and should refer to *United States v. City of New Bedford*, D.J. Ref. 90-5-1-1-2823.

The proposed Modified Consent Decree may be examined at the office of the United States Attorney, District of Massachusetts, 1107 John W. McCormack, Post Office and Courthouse, Boston, Massachusetts 02109, and at the Office of Regional Counsel, United States Environmental Protection Agency, Region I, John F. Kennedy Federal Building, Rm. 2203, Boston, Massachusetts 02203. Copies of the Modified Consent Decree may also be examined at the Environmental Enforcement section, Land and Natural Resources Division, Department of Justice, Room 1647(D), Ninth Street and Pennsylvania Avenue NW., Washington, DC 20530. A copy of the proposed Modified Consent Decree may be obtained in person or by mail from the Environmental Enforcement section, Land and Natural Resources Division, Department of Justice. In requesting a copy, please refer to the referenced case name and D.J. Ref. number and enclose a check in the amount of \$5.00 (ten cents per page reproduction cost) payable to the Treasurer of the United States.

George W. Van Cleve,

Acting Assistant Attorney General, Land and Natural Resources Division.

[FR Doc. 90-7655 Filed 4-3-90; 8:45 am]

BILLING CODE 4410-01-M

Antitrust Division

United States v. The Gillette Co., et al.; Proposed Final Judgment and Competitive Impact Statement

Notice is hereby given pursuant to the Antitrust Procedures and Penalties Act, 15 U.S.C. 16(b)-(h), that a proposed Final Judgment, Stipulation, and Competitive Impact Statement have been filed with the United States District Court for the District of Columbia in *United States v. The Gillette Company, Wilkinson Sword, Inc., Stora Kopparbergs Bergslags AB, and Eemland Management Services BV*, Civil Action No. 90-0053-TFH.

The Complaint of the United States, filed January 10, 1990, alleged that the acquisition by The Gillette Company ("Gillette") of the Wilkinson Sword wet shaving razor blade businesses of Eemland Management Services BV ("Eemland") outside the 12-nation European Community ("E.C.") violated section 7 of the Clayton Act, 15 U.S.C. 18. The non-E.C. businesses included the wet shaving razor blade business of

APPENDIX C
CALENDAR OF PUBLIC HEARING

CALENDAR OF PUBLIC HEARING

Those listed below appeared as witnesses at the United States International Trade Commission's hearing on:

Subject : The Effects of Greater Economic
Integration within the European
Community on the United States

Inv. No. : 332-267

Date and Time : June 21, 1990 - 9:30 a.m.

Sessions were held in connection with the investigation in the Main Hearing Room 101, United States International Trade Commission, 500 E Street, S.W., in Washington, D.C.

WITNESS AND ORGANIZATION:

National Forest Products Association,
Washington, D.C.

John Mentis, Director,
International Trade Council

Ward C. Hatchings, National Forest
Products Association

Motion Picture Association
of America, Incorporated
Washington, D.C.

Fritz E. Attaway, Senior Vice President
of the Motion Picture Export Association of
America

North American Telecommunications
Association
Washington, D.C.

Edwin B. Spievack, President

-end-

APPENDIX D
LIST OF EC 92 INITIATIVES ADDRESSED IN
THIS INVESTIGATION

Key to Abbreviations and Symbols Used in Appendix D

EC initiative:

- Dir = Directive (binding on member states as to the result to be achieved and requires national implementing measures)
- Rec = Recommendation (a nonbinding request to member states or individuals)
- Dec = Decision (binding on and applicable to member states or persons addressed and generally requires no national implementing measures)
- Reg = Regulation (binding and directly applicable throughout the EC without any national implementing measures)
- * = Initiative listed in *Fifth Progress Report of the Commission to the Council and the European Parliament Concerning the Implementation of the White Paper on the Completion of the Internal Market*. Certain non-White Paper measures are being considered because of their importance in a single EC market.
- ✓ = Initiative considered in preparation of this report; initiatives introduced in 1990 that are not checkmarked will be considered in preparation of the next follow-up report; other initiatives in appendix were considered in either the original or first follow-up report.

Member-state implementation:

- | | | |
|------------------|--------------|---------------------|
| B = Belgium | FR = France | L = Luxembourg |
| G = West Germany | GR = Greece | NL = Netherlands |
| DK = Denmark | IT = Italy | P = Portugal |
| S = Spain | IR = Ireland | UK = United Kingdom |
- I = Initiative implemented by member state into national law.
- N = Initiative not implemented by member state.
- F = EC Commission infringement proceeding under way for failure to implement.
- D = Derogation (e.g., exemption from implementation deadline).
- = National implementation measure is not required or applicable.

Note. — The implementation status of adopted initiatives was obtained mostly from the *Fifth Report of the Commission to the Council and Parliament Concerning the Implementation of the White Paper on the Completion of the Internal Market*, COM(90)90, Mar. 28, 1990, and the *Seventh Annual Report to the Parliament on Commission Monitoring of the Application of Community Law, 1989*, COM(90) 288, May 22, 1990. Not all adopted initiatives are listed in these reports and, thus, their status is not readily known (columns in appendix table on member-state implementation are blank). Implementation of the initiatives may not be reflected because the specified deadline for implementation has not arrived, member states may not have completed implementation processes or reported on implementation, or efforts by EC and internal institutions to achieve implementation may be ongoing.

Table D-1.
List of EC initiatives considered in this investigation

Initiative	Description	Relevant U.S. Member state implementation													Comment
		B	G	DK	S	FR	GR	IT	IR	L	NL	P	UK		
Public procurement															
Enacted:															
88/295-Dir*	Revises procedures for awarding public-supply contracts.	I	I	I	D	I	D	I	I	F	I	I	D	I	Implementation 1/1/89. Derogation to 3/1/92.
89/364-Dec.....	Improve efficiency of electricity use.....														Applicable 3/4/90.
89/440-Dir*....	Coordinates procedures for awarding public-works contracts (annex I updated by 90/380-Dec).														Implementation 7/19/90. Derogation to 3/1/92.
89/665-Dir*....	Review procedures for the award of public supply and public works contracts.														Implementation 12/1/91.
√90/377-Dir.....	Transparency of gas and electricity prices.....														Implementation 7/1/91.
Proposed:															
(89)334-Dir.....	Transit of natural gas through the major systems.....														Natural gas
(89)335-Reg....	Investment in petroleum, natural gas, and electricity.														Energy
(89)380-Dir*....	Procurement procedures of entities in water, energy, transport, and telecommunications.														Energy, water, transport, telecom
(89)400.....	Public procurement--regional and social aspects.....														Potentially all
√(90)207-Dir....	Transit of electricity through transmission grids.....														Electricity
Financial sector															
Enacted:															
85/583-Dir*....	Liberalization of movement of units of collective investment undertakings in transferable securities.	I	I	I	I	I	I	I	I	I	I	I	D	I	Implementation 10/1/89. Derogation to 12/31/90.
85/611-Dir*....	Undertakings for collective investment in transferable securities.	N	I	I	I	D	N	I	I	N	D	I			Implementation 10/1/89. Derogation to 4/1/92.
86/566-Dir*....	Liberalization of capital movements.....	I	I	I	D	I	I	I	I	I	D	I			Implementation 2/28/87. Implementation 12/31/90.
86/635-Dir*....	Accounting practices for financial institutions.....	N	N	N	I	N	N	N	N	N	N	N			Implementation not required
87/62-Rec*....	Monitoring large exposures of credit institutions.....	N	N	N	N	N	N	N	N	N	N	N			Implementation not required
87/63-Rec*....	Deposit-guarantee schemes for financial institutions.....	N	N	N	N	N	N	N	N	N	N	N			Implementation not required
87/343-Dir*....	Investment in direct non-life insurance.....														Implementation 7/1/90.
87/344-Dir*....	Legal-expenses insurance.....														Implementation 7/1/90.
87/345-Dir.....	Requirements for official stock exchange listing.....														Implementation 1/1/90.
87/598-Rec*....	European code of conduct for electronic payment.....														Addressed to enterprises.
88/220-Dir*....	Undertakings for collective investments in transferable securities.	N	I	I	I	D	N	I	I	N	D	I			Implementation 10/1/89. Derogation to 4/1/92.
88/357-Dir*....	Direct non-life insurance services.....														Implementation 6/29/90.
88/361-Dir*....	Implementation of article 67 of the treaty regarding freedom of capital flows.														Implementation 7/1/90. Derogation to 12/31/92.
88/590-Rec.....	Payment systems - card holders and issuers.....														Implementation 1/1/91.
88/627-Dir*....	Public-disclosure requirements for changes in major stock holdings of publicly held companies.														
88/1969-Reg....	Single facility providing medium-term financial assistance for member states' balance of payments.														

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Relevant U.S. Sector/Industry	Member state implementation	Comment
			P G DK S FR GR IT IR L NL P UK	
Financial sector--Continued				
Enacted--Continued:				
89/117-Dir*	Annual reporting by branches of credit and financial institutions outside member state of head office.	Banking		Implementation 1/1/91.
89/298-Dir*	Requirements for public offer prospectus.	Securities		Implementation 4/17/89.
89/299-Dir*	Harmonizes the concept of own funds.	Banking		Implementation 1/1/93.
89/592-Dir*	Coordinates regulations on insider trading.	Securities		Implementation 6/1/92.
89/646-Dir*	Regulation and authorization of credit institutions.	Banking		Implementation 1/1/93.
89/647-Dir*	Solvency ratio for credit institutions.	Banking		Implementation 1/1/91.
90/88-Dir	Consumer credit.	Banking		Implementation 12/31/92.
90/109-Rec.	Transparency of banking conditions regarding cross-border financial transactions.	Banking		
90/211-Dir*	Mutual recognition of public offer prospectuses.	Securities		Implementation 4/17/91.
90/232-Dir*	Third directive on motor vehicle liability insurance.	Insurance		Implementation 12/31/92.
Proposed:				
(80)854-Dir*	Insurance contracts.	Insurance		
(87)255-Dir*	Mortgage credit.	Banking		
(88)4-Dir*	Reorganization and winding-up of credit institutions and deposit-guarantee schemes.	Banking		
(88)805-Reg.	Guarantees of credit institutions or insurance firms.	Banking		
(89)394-Dir*	Bankruptcy regulations for insurance firms.	Insurance		
(89)474-Dir*	Accounting requirements for insurance firms.	Insurance		
(89)629-Dir*	Investment services.	Securities		
(89)641-Reg.	Application of article 85(3) to insurance.	Insurance		
(90)106-Dir	Money laundering.	Banking		
(90)141-Dir	Capital adequacy of investment and credit firms.	Banking		
(90)46-Dir*	Second directive on life insurance services.	Insurance		
(90)278-Dir*	Motor vehicle liability insurance; non-life insurance.	Insurance		
Customs				
Free movement of goods				
Enacted:				
85/347-Dir*	Duty-free allowance for fuel in bus tanks.	Travel, tourism		Implementation 10/1/85.
85/1900-Reg*	Introduces EC export and import forms.	Potentially all		Applicable 1/1/88.
85/1901-Reg*	Single Administrative Document.	Potentially all		Applicable 1/1/88.
86/1797-Reg*	Abolishes certain postal fees.	Mail order		Applicable 1/1/88.
86/3690-Reg*	Eliminates customs formalities under TIR Convention.	Potentially all		Applicable 7/1/87.
88/4283-Reg*	Introduction of common border posts.	Potentially all		Applicable 7/1/89.
89/526-Dec.	International Convention on the Harmonization of Frontier Controls of Goods.	Potentially all		Treaty entered into force 9/12/87.
89/604-Dir*	Exemption for permanent imports of personal property.	Potentially all		Implementation 7/1/90.
89/617-Dir	Units of measurement.	Potentially all		

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Relevant U.S. Sector/Industry	Member state implementation											Comment	
			B	G	DK	S	FR	GR	IT	IR	L	NL	P		UK
<u>Free movement of goods--Continued</u>															
<u>Enacted--Continued:</u>															
89/1292-Reg....	Movement of goods from one member state for temporary use in one or more other member states.	Potentially all													Applicable 5/15/89.
89/4046-Reg....	Security to ensure payment of a customs debt.....	Potentially all													Applicable 1/1/91.
√90/474-Reg*....	Abolishes lodgement of the transit advice note.....	Potentially all													Applicable 7/1/90.
√90/1715-Reg....	Information provided by customs concerning classification of goods in the customs nomenclature.	Potentially all													Enters into force on 6/29/90.
√90/1716-Reg....	Persons liable for payment of a customs debt.....	Potentially all													Applicable 6/29/90.
<u>Proposed:</u>															
(85)224-Dir*....	Easing of border controls on intra-EC borders.....	Potentially all													
(85)467-Reg....	Correct application of customs and agricultural laws..	Agriculture													
(86)383-Dir*....	Duty-free admission of fuel in commercial vehicles....	Potentially all													
(87)383-Dir*....	Control of the acquisition and possession of weapons..	Weapons													
(88)297-Dir*....	Temporary importation of motor vehicles.....	Motor vehicles													
(88)298-Dir*....	Permanent imports of personal property.....	Potentially all													
(89)446-Dir*....	Control of the acquisition and possession of weapons..	Weapons													
√(89)384.....	Autonomous suspension of customs duties.....	Potentially all													
√(90)71-Reg.....	EC customs code and temporary importation arrangements with total relief from duties (2 proposals).	Potentially all													
√(90)74-Dir.....	Release of goods for free circulation.....	Potentially all													Will be superseded by Common Customs Code.
√(90)xx-Reg.....	Statistical classification of economic activities.....	Potentially all													
√(90)177-Reg*....	Statistics for intra-EC trade in goods.....	Potentially all													
√(90)203-Reg....	EC use of TIR and ATA carnets.....	Potentially all													
<u>Free movement of persons</u>															
<u>Enacted:</u>															
85/348-Dir*....	Increases exemption from turnover and excise taxes on imports in intra-EC travel (amended by 88/664).	Potentially all	I	I	I	I	I	I	I	I	I	I	I	I	Implementation, as amended, 7/1/89.
85/368-Dec*....	Comparability of vocational training qualifications...	Potentially all	-	-	-	-	-	-	-	-	-	-	-	-	
85/432-Dir*....	Coordinates provisions in the field of pharmacy.....	Healthcare	F	I	I	N	I	I	F	I	-	I	I	I	Implementation 10/1/87.
85/433-Dir*....	Mutual recognition of diplomas in pharmacy.....	Healthcare	F	I	I	N	I	I	F	I	F	I	I	I	Implementation 10/1/87.
85/434-Dec*....	Advisory committee on pharmaceutical training.....	Healthcare	-	-	-	-	-	-	-	-	-	-	-	-	
86/365-Dec*....	Cooperation in training in technology (COMETT).....	Potentially all	-	-	-	-	-	-	-	-	-	-	-	-	
86/457-Dir*....	Specific training in general medical practice.....	Healthcare	I	F	I	I	I	I	F	I	-	I	I	I	Impl. 1/1/88-1/1/90.
86/653-Dir*....	Self-employed commercial agents.....	Potentially all	N	I	N	N	N	N	N	N	D	N	I	N	Derogation to 1/1/94. Implementation 1/1/90. Implementation 1/3/91.
89/48-Dir*....	Mutual recognition of higher education diplomas.....	Potentially all													
89/438-Dir.....	Mutual recognition of diplomas for goods haulage and road passenger operators.	Transport													
89/594-Dir.....	Mutual recognition of diplomas in medicine.....	Potentially all													Implementation by 5/8/91.
89/595-Dir.....	Mutual recognition of diplomas for nurses.....	Potentially all													Implementation by 10/13/91.

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Relevant U.S. Sector/Industry							Comment					
		B	G	DK	S	FR	GR	IT		IR	L	NL	P	UK
<u>Free movement of persons--Continued</u>														
<u>Enacted--Continued:</u>														
89/601-Rec.....	Training of health personnel in the matter of cancer...												Potentially all	Action program launched.
89/657-Dec.....	Vocational training/technological change (Eurotecnet).												Potentially all	Applicable 1/1/91.
89/663-Dec.....	Mobility of university students (Erasmus).....												Education	Applicable 1/1/91.
√89/684-Dir.....	Vocational training for drivers with dangerous goods...												Transport	Multiple effective dates.
89/2332-Reg.....	Social security benefits (for persons moving in EC)...												Potentially all	Multiple effective dates.
89/3427-Reg.....	Social security benefits (residence of families).....												Potentially all	Applicable 1/15/86.
√90/233-Dec.....	Trans-European mobility for university studies.....												Education	Applicable 7/1/90.
√90/267-Dec.....	Continuing vocational training (FORCE).....												Potentially all	Applies 1/1/91-12/31/94.
√90/364-Dir*.....	Right of residence.....												Potentially all	Implementation 6/30/92.
√90/365-Dir*.....	Right of residence for employees and retired persons..												Potentially all	Implementation 6/30/92.
√90/366-Dir*.....	Right of residence for students.....												Potentially all	Implementation 6/30/92.
90/1360-Reg.....	European Training Foundation.....												Potentially all	Applicable 1 day after site chosen for Foundation.
<u>Proposed:</u>														
(89)372-Dir*.....	Recognition of professional education and training.....												Potentially all	
√(89)612-Dec.....	Vocational training (Eurotecnet II).....												Potentially all	
(89)640-Dir.....	Blood alcohol concentration for vehicle drivers.....												Potentially all	
√(90)76-Dir*.....	Increase in tax paid allowances for intra-EC travel...												Potentially all	
√(90)108-Reg*.....	Freedom of movement for workers within the EC.....												Potentially all	
√(90)132-Dec.....	Vocational training in audiovisual sector.....												Potentially all	
<u>Protection of workers</u>														
<u>Enacted:</u>														
88/364-Dir.....	Protection from certain chemicals and work activity...												Potentially all	Implementation 1/1/90.
88/383-Dec.....	Information on safety, hygiene, and health at work....												Potentially all	Adopted 2/24/88.
89/391-Dir.....	Improvements in safety and health of workers at work..												Potentially all	Implementation 12/31/92.
89/654-Dir.....	Safety and health requirements at work.....												Potentially all	Implementation 12/31/92.
														Derogation to 12/31/94.
89/655-Dir.....	Use of work equipment at work.....												Potentially all	Implementation 12/31/92.
89/656-Dir.....	Use of personal protective equipment at work.....												Potentially all	Implementation 12/31/92.
√90/326-Rec.....	European schedule of occupational diseases.....												Potentially all	Implementation 12/31/92.
√90/269-Dir.....	Handling heavy loads and risk of back injury.....												Potentially all	
√90/270-Dir.....	Work with visual display units.....												Potentially all	
√90/394-Dir.....	Exposure to carcinogens at work.....												Potentially all	
<u>Proposed:</u>														
√(89)376-Dir.....	Protection from ionizing radiation												Potentially all	
(89)404-Dir.....	Risks related to exposure to biological agents.....												Potentially all	
(90)184-Dir.....	Risks related to exposure to asbestos at work.....												Potentially all	
√(90)228-Dir.....	Atypical work (3 separate proposals).....												Potentially all	
√(90)317-Dir.....	Organization of working time.....												Potentially all	

D

Customs--Continued

Member state implementation
B G DK S FR GR IT IR L NL P UK

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Member state implementation													Comment
		B	G	DK	S	FR	GR	IT	IR	L	NL	P	UK		
<u>Customs--Continued</u>															
<u>Social dimension</u>															
<u>Enacted:</u>															
90/238-Dec.....	"Europe against cancer" program for 1990-94.....													Potentially all	
<u>Proposed:</u>															
(89)471.....	EC charter of fundamental social rights.....													Potentially all	
(89)568.....	EC charter of basic social rights for workers.....													Potentially all	
<u>Transport</u>															
<u>Enacted:</u>															
86/4055-Reg*	Maritime transport.....													Shipping	Applicable 1/1/87.
86/4056-Reg*	Maritime transport.....													Shipping	Applicable 7/1/87.
86/4057-Reg*	Maritime transport.....													Shipping	Applicable 7/1/87.
86/4058-Reg*	Maritime transport.....													Shipping	Applicable 7/1/87.
87/601-Dir*	Air fares between member states.....													Airlines	Implementation 12/31/87.
87/602-Dec*	Passenger capacity rates and access to scheduled air service routes.													Airlines	Applicable 1/1/88. F for UK suspended.
87/1674-Reg*	Amends regulations regarding EC transit operations.....													Trucking	Applicable 7/1/88.
87/3975-Reg*	Rules on competition in air transport.....													Airlines	Applicable 1/1/88.
87/3976-Reg*	Application of article 85(3) to air transport (as amended by 90/2344-Reg).													Airlines	Applicable 1/1/88; amendment 8/12/90.
88/1841-Reg*	Market access for carriage of goods by road.....													Trucking	Applicable 7/1/88.
89/463-Dir.....	Scheduled inter-regional air services for transport of passengers, mail, and cargo.													Airlines	Implementation 11/1/89.
89/629-Dir.....	Noise emission from civil subsonic jet planes.....													Airlines	Implementation 9/30/90.
89/684-Dir.....	Vocational training for certain drivers of vehicles...													Transport	Implementation 1/1/95.
89/2299-Reg*	Code of conduct for computerized reservation systems...													Airlines	Applicable 8/1/89.
89/4038-Reg*	Rates for intra-EC carriage of goods by road.....													Trucking	Applicable 1/1/90.
89/4059-Reg*	Conditions under which non-resident carriers may operate national road haulage services.													Transport	Applicable 7/1/90.
89/4060-Reg*	Controls in road and inland waterway transport.....													Transport	Applicable 7/1/90.
90/398-Dir.....	Vehicles hired without drivers for carriage of goods...													Transport	Implementation 12/31/90.
90/1053-Reg*	International carriage of goods by road.....													Transport	Applicable 5/1/90.
90/2342-Reg*	Fares for scheduled air services.....													Airlines	Applicable 11/1/90.
90/2343-Reg*	Market access and passenger capacity.....													Airlines	Applicable 11/1/90.
<u>Proposed:</u>															
(85)90-Reg*	Rules applicable to maritime transport.....													Shipping	
(85)610-Reg*	Conditions under which nonresident carriers may transport goods or passengers by inland waterway.													Shipping	
(88)596-Reg*	Conditions under which nonresident carriers may operate national road passenger-transport services.													Passenger carriage	

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Member state implementation													Comment
		B	G	DK	S	FR	GR	IT	IR	L	NL	P	UK		
<u>Transport--Continued</u>															
<u>Proposed--Continued:</u>															
(88)770-Reg*	International carriage of passengers by coach and bus.													Passenger carriage	
(89)238-Reg	Transport infrastructure and transport market in 1992.													Transport	
(89)266-Reg	Definition of EC shipowner													Maritime	
(89)417-Reg	Amends 87/3975-Reg on competition in air transport													Airlines	
(89)417-Reg	Amends 87/3976-Reg on application of article 85(3) to air transport.													Airlines	
(89)417-Reg	Application of article 85(3) to air transport													Airlines	
(89)472-Dir*	Personnel licenses for functions in civil aviation													Aviation	
(89)490-Reg*	Community transit													Transport	
(89)564-Dir	Development of EC railways													Railroads	
(89)564-Reg	Public service obligation in rail, road, and waterway.													Transport	
(89)564-Dec	Network of high speed trains													Railroad	
(89)564-Dir	Combined carriage of goods between states													Transport	
(90)17-Dec	Commercial aviation agreements with third countries													Aviation	
(90)63-Reg	Operation of air cargo services													Air freight	
(90)64-Reg	Organization of market for carriage of goods by road													Transport	
(90)99-Reg	Denied boarding compensation system in air transport													Airlines	
(90)100-Reg	Consultation between airports and airport users													Airlines	
(90)167-Reg	Amends 87/3975-Reg on competition in air transport													Airlines	
(90)219-Reg	Transfer of ships from one register to another													Maritime	
(90)260-Reg	Application of article 85(3) to shipping companies													Maritime	
<u>Enacted:</u>															
85/2137-Reg*	Regulation of European Economic Interest Groups													Potentially all	Applicable 7/1/89.
88/301-Dir	Competition in telecommunications terminal equipment													Telecom.	Implementation by 6/30/90.
89/666-Dir*	Disclosure requirements for branches of certain firms													Potentially all	Implementation 1/1/92.
89/667-Dir	Company law for single-member private limited firms													Potentially all	Implementation 1/1/92.
89/4064-Reg	Controls concentration between undertakings													Potentially all	Applicable 9/21/90.
90/388-Dir	Competition in markets for telecommunication services													Telecom.	Adopted 6/28/90.
<u>Proposed:</u>															
(83)185-Dir*	Structure of public limited firms and their powers													Potentially all	
(84)727-Dir*	Cross-border mergers of public limited companies													Potentially all	
(86)238-Dir*	Annual and consolidated accounts													Potentially all	
(88)823-Dir*	Company law on takeover and other general bids													Potentially all	
(89)268-Reg*	Statute for a European company													Potentially all	
(89)561-Dir	Annual and consolidated accounts - exemption for small and medium-sized companies.													Potentially all	
(90)58-Rec	Administrative simplification favoring small and medium-sized companies.													Potentially all	

I I I N I N I N I N I
I I I N I N I N I N I
I I I N I N I N I N I
I I I N I N I N I N I

Competition policy

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Relevant U.S. Sector/Industry	Member state implementation													Comment
			P	G	DK	S	FR	GR	IT	IR	L	NL	P	UK		
Tax systems																
Enacted:																
85/349-Dir*	Increases tax relief on small consignments of noncommercial value (as amended by 88/663-Dir).	Potentially all	I	I	I	I	I	I	I	I	I	I	I	I	Implementation, as amended, 7/1/89.	
85/362-Dir*	VAT exemption for temporary imports of goods other than means of transport (as amended by 90/237-Dir).	Potentially all	I	I	F	I	D	I	I	I	I	I	I	I	Implementation 1/1/86.	
86/560-Dir*	VAT refund to persons not established in the EC.	Potentially all	I	I	I	I	I	F	I	I	I	I	I	I	Amendment 7/1/90.	
88/245-Dec*	Authorizes France to apply reduced duty on consumption of "traditional" rum.	Rum	-	-	-	-	-	-	-	-	-	-	-	-	Implementation 1/1/88.	
88/331-Dir*	VAT exemption on final importation of certain goods.	Potentially all	I	I	I	I	I	N	F	I	I	I	I	I	Implementation not required.	
89/465-Dir*	Turnover taxes for common VAT scheme - abolition of certain derogations.	Potentially all	N	N	I	N	N	N	N	N	N	N	N	N	Implementation 1/1/89.	
89/683-Dec*	Derogation for France regarding turnover taxes.	Potentially all	I	I	I	I	I	N	F	I	I	I	I	I	Implementation 1/1/90;	
90/434-Dir*	Taxation applicable to mergers, divisions, transfers of assets, and exchange of shares.	Potentially all	N	N	I	N	N	N	N	N	N	N	N	N	P partial derogation.	
90/435-Dir*	Taxation applicable to parent firms and subsidiaries.	Potentially all	I	I	I	I	I	N	F	I	I	I	I	I	Implementation 1/1/89.	
90/463*	Convention on the elimination of double taxation on adjustment of profits of associated enterprises.	Potentially all	I	I	I	I	I	N	F	I	I	I	I	I	Implementation 1/1/90.	
Proposed:																
(72)225*	Excise duties on alcoholic drinks.	Beverages														
(73)1234*	Excise duties on mineral oils.	Potentially all														
(79)737-Dir*	Income tax provisions regarding movement of workers.	Potentially all														
(79)794-Dir*	VAT and excise duty on the stores of vessels, aircraft, and international trains.	Potentially all														
(80)69-Dir*	Taxes, except turnover tax, on manufactured tobacco.	Tobacco														
(84)84-Dir*	Turnover taxes for the common VAT scheme - deduction eligibility.	Potentially all														
(85)150-Dir*	Indirect consumption taxes and excise duties on alcoholic drinks.	Beverages														
(85)151-Dir*	Excise duties on fortified wine and similar products.	Beverages														
(85)319-Dir*	Tax arrangements for carryover of undertakings.	Potentially all														
(86)742-Reg*	Regulates fees payable to the EC trademark office.	Potentially all														
(87)139-Dir*	Abolishes indirect taxes on securities transactions.	Securities														
(87)315-Dir*	Turnover taxes for common VAT scheme - abolition of certain derogations.	Potentially all														
(87)321-Dir*	Approximates common VAT rates.	Potentially all														
(87)324-Dir*	Process for converging VAT and excise duty rates.	Potentially all														
(87)324-Dir*	Turnover taxes for common VAT scheme for small and medium-sized business.	Potentially all														
(88)846-Dir*	Completion of common VAT system.	Potentially all														
(89)60-Dir*	Mutual assistance on direct taxation and VAT; common system of withholding tax on interest income.	Potentially all														
(89)525-Dir*	Taxes on cigarettes.	Tobacco														
(89)525-Dir*	Taxes on manufactured tobacco other than cigarettes.	Tobacco														

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Relevant U.S. Sector/Industry	Member state implementation	Comment
			E G DK S FR GR IT IR L NL P UK	
TAX SYSTEMS--Continued				
Proposed--Continued:				
(89)526-Dir*	Rates of excise taxes on mineral oils.....	Mineral oil		
(89)527-Dir*	Excise taxes on alcoholic beverages and on alcohol contained in other products.	Beverages		
√(90)94-Dir.....	Indirect taxes on the raising of capital.....	Financial		
√(90)102-Dir*	Abolishes fiscal frontiers.....	Potentially all		
Residual quantitative restrictions				
Enacted:				
89/3365-Reg.....	Liberalization of certain products subject to national quantitative restrictions.			
Proposed:				
√(89)xxx-xxx.....	A single EC motor-vehicle market.....	Motor vehicles		
Intellectual property				
Enacted:				
87/54-Dir*	Legal protection of semiconductor products.....	Semiconductors		Implementation 11/7/87.
89/104-Dir*	Harmonizes laws relating to trademarks.....	Potentially all		Implementation 12/28/91. Derogation to 12/31/92.
Proposed:				
(84)470-Reg*	Regulates EC trademarks.....	Potentially all		
(85)844-Reg*	Implements trademark regulations.....	Potentially all		
(86)731-Reg*	Procedural rules for Boards of Appeal on EC trademark.	Potentially all		
(88)172-Dir.....	Green Paper on copyright and challenge of technology..	Potentially all		
(88)496-Dir*	Legal protection of biotechnological inventions.....	Biotechnology		
(88)816-Dir*	Legal protection of computer programs.....	Software		
√(90)101-Reg.....	Supplementary protection certificate for medicines....	Pharmaceuticals		
Standards				
Agriculture - farm based				
Enacted:				
85/179-Dir.....	Prohibition of organisms harmful to plants.....	Agriculture		Implementation 1/1/86.
85/320-Dir*	Classical swine fever and African swine fever.....	Swine		Implementation 1/1/86.
85/321-Dir*	African swine fever.....	Pork products		Implementation 1/1/86.
85/322-Dir*	Classical swine fever and African swine fever.....	Fresh pork		Impl. date not yet fixed.
85/323-Dir*	Health inspections of meat-production plants.....	Meat		

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Relevant U.S. Member State Implementation													Comment
		D	G	DK	S	FR	GR	IT	IR	L	NL	P	UK		
Agriculture - farm based--Continued															
Standards--Continued															
85/324-Dir*	Health inspection of poultry-production plants.....	N	N	N	N	N	N	N	N	N	N	N	N	N	Impl. date not yet fixed.
85/325-Dir*	Medical certification of people handling fresh meat....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/86.
85/326-Dir*	Medical certification of people handling poultry meat....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/86.
85/327-Dir*	Medical certification of people handling fresh meat....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/86.
85/328-Dir*	Testing for prohibited hormone growth promoters.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/87.
85/397-Dir*	Production and sale of heat-treated milk.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/89.
85/511-Dir*	Control of foot-and-mouth disease.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/87.
85/574-Dir*	Organisms harmful to plants or plant products.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/87.
86/355-Dir*	Prohibits ethylene oxide as a pesticide (expiry date of exceptions extended by 89/365-Dir).	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 7/1/87.
86/362-Dir*	Pesticide residues on cereals.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 6/30/88.
86/363-Dir*	Pesticide residues on edible animal products.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 6/30/88.
86/469-Dir*	Examination of animals and fresh meat for residues....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 12/31/88.
86/649-Dec*	African swine fever in Portugal (amended by 89/577)....	-	-	-	-	-	-	-	-	-	-	-	-	-	Applicable 12/16/86.
86/650-Dec*	African swine fever in Spain.....	-	-	-	-	-	-	-	-	-	-	-	-	-	Applicable 12/16/86.
87/58-Dec*	Eradicating brucellosis, tuberculosis, and leukosis....	I	I	I	I	I	I	I	I	I	I	I	I	I	Compulsory for S and P.
87/64-Dir*	Health and veterinary inspections on EC imports of bovine animals, swine and fresh meat.	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/88.
87/153-Dir*	Guidelines to assess additives in animal nutrition....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 12/31/87.
87/202-Dec*	Accelerates plan for eradication of swine fever.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Applicable 1/1/87.
87/230-Dec*	Eradicating classical swine fever.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Applicable 12/31/87.
87/231-Dec*	Measures relating to swine fever.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/89.
87/328-Dir*	Purebred animals of bovine species for breeding.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Derogation to 1/1/92.
87/486-Dir*	Measures to control classical swine fever.....	F	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 12/31/87.
87/487-Dir*	Render and keep EC free from classical swine fever....	-	-	-	-	-	-	-	-	-	-	-	-	-	Implementation 9/22/87.
87/488-Dec*	Financial means for eradicating classical swine fever....	F	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 12/31/88.
87/489-Dir*	Certain measures relating to swine fever.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/88.
87/491-Dir*	Animal health problems in trade in meat products.....	F	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/88.
87/519-Dir*	Pesticide residues on animal feedings.....	F	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 12/31/90.
88/146-Dir*	Prohibits hormone growth promoters in livestock.....	F	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/88.
88/288-Dir*	Health problems in trade in fresh meat.....	F	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/89.
88/289-Dir*	Imports of bovine animals, swine, and fresh meat....	F	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/89.
88/298-Dir*	Pesticide residues on fruit, vegetables, and cereals....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 7/1/88.
88/380-Dir*	Marketing of seeds and catalog of plant species.....	N	I	N	N	N	N	N	N	N	N	N	N	N	Implementation 7/1/90.
88/407-Dir*	Frozen bovine semen (as amended by 90/120-Dir).....	N	I	N	N	N	N	N	N	N	N	N	N	N	Implementation 1/1/89.
88/572-Dir*	Organisms harmful to plants or plant products (wood)....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/89.
88/657-Dir*	Health rules for minced meat and similar preparation....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/92.
88/658-Dir*	Health rules for intra-EC trade in meat products.....	I	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 7/1/90.
88/661-Dir*	Zootechnical standards for porcine breeding animals....	I	I	I	I	I	I	I	I	I	I	I	I	I	Derogation to 12/31/92.
															Derogation to 1/1/93.

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Member state implementation											Comment		
		B	G	DK	S	FR	GR	IT	IR	L	NL	P		UK	
Agriculture - farm based--Continued															
Enacted--Continued:															
89/145-Dec*	Contagious bovine pleuropneumonia in Portugal.....													Livestock	
89/214-Dec*	Inspecting fresh meat establishments.....													Meat	Implementation 6/30/90.
89/227-Dir*	Health rules for imports of meat products.....													Meat	
89/359-Dir*	Organisms harmful to plants or plant products (seed)...													Agriculture	Implementation 1/1/91.
89/361-Dir*	Purebred breeding sheep and goats.....													Sheep and goats	Implementation 3/31/89.
89/366-Dir*	Marketing of seed potatoes.....													Agriculture	
89/437-Dir*	Hygiene and health problems regarding egg products....													Poultry and eggs	
89/439-Dir*	Organisms harmful to plants or plant products.....													Agriculture	Implementation 1/1/90.
89/455-Dec*	Pilot projects for the control of rabies.....													Wildlife	
89/536-Dir*	Trade in embryos of domestic bovine animals.....													Agriculture	
89/575-Dec*	Inspections in third countries on seed-producing crops (amends 85/355-Dec. as do 88/322 and 89/532).													Agriculture	
89/608-Dir*	Application of legislation on veterinary matters.....													Agriculture	To be re-examined before 1/1/91.
89/610-Dec*	Reference methods and list of national reference laboratories for detecting residues.													Agriculture	Implementation 12/31/91.
89/662-Dir*	Veterinary checks in intra-EC trade.....													Agriculture	Implementation 1/1/91.
90/113-Dir*	Organisms harmful to plants and plant products.....													Agriculture	Applies only to IT.
90/168-Dir*	Organisms harmful to plants and plant products.....													Agriculture	Required of FR/GR/IT/S/P.
90/208-Dec*	Contagious bovine pleuropneumonia in Spain.....													Livestock	Impl. 7/1/90 and 10/1/90.
90/217-Dec*	Eradication of African swine fever in Sardinia.....													Swine	Implementation 1/1/92.
90/242-Dec*	Eradication of brucellosis in sheep and goats.....													Livestock	Adopted 6/26/90.
90/422-Dir*	Enzootic bovine leucosis.....													Livestock	Implemented 1/1/91.
90/423-Dir*	Control of foot-and-mouth disease.....													Livestock	Implemented 1/1/91.
90/424-Dec*	Expenditure in the veterinary field.....													Livestock	Implemented 1/1/91.
90/425-Dir*	Veterinary and zootechnical checks in intra-EC trade...													Agriculture	Implemented 1/1/91.
90/426-Dir*	Animal health - third country imports of horses.....													Horses	Implemented 1/1/91.
90/427-Dir*	Zootechnical rules regarding horses.....													Horses	Implementation 7/1/91.
90/428-Dir*	Trade in horses intended for competition.....													Horses	Implementation 12/31/91.
90/429-Dir*	Semen of porcine species animals.....													Semen	
Proposed:															
(81)504-Dir*	Personnel responsible for inspecting meat products.....													Meat	
(82)529-Dir*	Intra-EC trade in live cattle and pigs.....													Livestock	
(82)883-Dir*	Maximum levels for pesticide residues for fruit and vegetables (ethoxyquin and diphenylamine).													Agriculture	
(83)655-Dir*	Fixes the weight of uncastrated male pigs.....													Swine	
(84)288-Dir*	Timetable for harmonizing health matters in veterinary, plant health, and legislation.													Agriculture	
(85)678-Dir*	Health rules for intra-EC trade in meat products.....													Meat	
(86)170-Dir*	Organisms harmful to plants or plant products.....													Agriculture	
(88)598-Dir*	Zootechnical and pedigree rules for purebred animals..													Agriculture	
(88)742-Reg*	Intra-EC trade in ovine and caprine species animals...													Livestock	

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Member state implementation							Comment				
		B	G	DK	S	FR	GR	IT		IR	L	NL	P
Agriculture -- farm based--Continued													
Proposed--Continued:													
(88)798-Dir*	Pesticide residues for fruit and vegetables.....												Agriculture
(88)836-Reg*	Health problems regarding trade in dogs and cats (rabies) (partially adopted; see 89/455-Dec).												Domestic animals
(89)9-Reg*	Trade in poultry and hatching eggs.....												Poultry, eggs
(89)34-Dir*	Standards for plant protection products.....												Agriculture
(89)379-Dec*	Administration of Bovine Somatotrophin (BST).....												Pharmaceuticals
(89)428-Reg*	Marketing fresh fish and fish products (nematodes)....												Fish
√(89)490-Reg*	Health rules for melted animal fat, greaves, and by-products of rendering for human consumption.												Animal fat
√(89)492-Reg*	Health rules for products of animal origin not covered by existing legislation.												Agriculture
√(89)493-Dec*	Safeguard measures in the veterinary field.....												Agriculture
√(89)496-Reg*	Game meat and rabbit meat.....												Agriculture
√(89)500-Reg*	Animal health conditions for marketing of rodents....												Agriculture
√(89)507-Reg*	Fresh poultry meat and fresh meat of reared game bird.												Meat
√(89)509-Reg*	Pathogens in feedstuffs.....												Agriculture
√(89)645-Reg*	Health conditions regarding fishery products.....												Seafood
√(89)646-Dir*	Organisms harmful to plants or plant products.....												Agriculture
√(89)647-Dir*	Organisms harmful to plants or plant products.....												Agriculture
√(89)648-Reg*	Health conditions regarding mollusks.....												Seafood
√(89)649-Reg*	Marketing of young plants.....												Agriculture
√(89)650-Reg*	Ornamental plant propagating material and plants.....												Agriculture
√(89)651-Dir*	Marketing of fruit plants.....												Agriculture
√(89)655-Reg*	Health conditions regarding aquaculture animals.....												Seafood
√(89)658-Reg*	Products of animal origin (other species).....												Agriculture
√(89)667-Reg*	Health conditions for milk products.....												Dairy
√(89)668-Reg*	Health rules for fresh poultry meat.....												Poultry
√(89)669-Reg*	Health rules for meat products.....												Meat
√(89)670-Dec*	Derogation regarding application of health standards..												Agriculture
√(89)671-Reg*	Health rules for minced meat and meat preparations...												Meat
√(89)672-Reg*	Health rules for heat-treated milk.....												Dairy
√(89)673-Reg*	Health rules for fresh meat.....												Meat
√(90)134-Dir*	Marketing of seed potatoes (micro-propagated).....												Vegetables
√(90)175-Dir*	Health and inspection problems with imports of bovines, swine, and meats.												Meat, livestock
√(90)222-Dec*	Eradication of infectious hemopoietic necrosis (IHN)...												Fish
√(90)238-Dir*	Protection of animals during transport.....												Animals

Standards--Continued

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Relevant U.S. Sector/Industry													Comment
		B	G	DK	S	FR	GR	IT	IR	L	NL	P	UK		
<u>Pharmaceuticals and medical devices--Continued</u>															
<u>Enacted--Continued:</u>															
89/105-Dir*	Price transparency of medicines and their inclusion in national health insurance.	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 12/31/89.	
89/341-Dir*	Approximates provisions for proprietary medicines.....													Implementation 1/1/92.	
89/342-Dir*	Immunological medicine of vaccines, toxins or serums..													Implementation 1/1/92.	
89/343-Dir*	Radio-pharmaceuticals.....													Implementation 1/1/92.	
89/381-Dir*	Proprietary medicine and medicine of human plasma.....													Implementation 1/1/92.	
90/385-Dir*	Active implantable medical equipment.....													Implementation 1/1/93.	
90/2377-Reg*	Tolerances for residues of veterinary medicines.....													Adopted 6/25/90.	
<u>Proposed:</u>															
(88)669-Dir*	Proprietary medicines (amends and restates (87)697; partially adopted under 89/341, 342, 343, and 381).														
(89)302-Dec....	European Convention for the protection of vertebrate animals for experimental and scientific purposes.														
√(89)607-Dir*	Distribution, legal status, and labeling of medicine..														
√(90)101-Dir....	Supplementary protection certificate for medicines.....														
√(90)172-Dir....	Medicines and homeopathic medicines.....														
√(90)172-Dir....	Veterinary medicines and homeopathic medicines.....														
√(90)135-Dir*	Veterinary medicines.....														
√(90)135-Dir*	Immunological veterinary medicines.....														
(90)212-Dir....	Advertising of medicines.....														
(90)xxx-Dir....	Free movement of medicines (four proposals).....														
<u>Motor vehicles</u>															
<u>Enacted:</u>															
87/358-Dir*	Certification procedures for vehicles and trailers....	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 10/1/88.	
88/76-Dir*....	Air pollution by gases from engines of vehicles.....	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 7/1/88. IT partial impl.	
88/77-Dir*....	Gaseous pollutants from diesel engines.....	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 7/1/88.	
88/194-Dir....	Braking devices of vehicles and their trailers.....	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 10/1/88.	
88/195-Dir....	Engine power of motor vehicles.....	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 4/1/88.	
88/218-Dir....	Weights, dimensions for refrigerated road vehicles....	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/89.	
88/321-Dir....	Rear view mirrors of motor vehicles.....	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/89.	
88/366-Dir....	Diver field of vision.....	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 10/1/88.	
88/436-Dir*....	Emission of particle pollutants from diesel engines....	N	I	I	I	I	I	I	I	I	I	I	I	Implementation 10/1/88.	
88/449-Dir....	Road worthiness tests (see (89)6-Dir below).....	N	I	I	I	I	I	I	I	I	I	I	I	Implementation 7/27/90.	
89/235-Dir*....	Sound level and exhaust systems of motorcycles.....	N	I	I	I	I	I	I	I	I	I	I	I	Implementation 10/1/89.	
89/277-Dir....	Direction indicator lamps.....	N	I	I	I	I	I	I	I	I	I	I	I	Implementation 9/30/89.	
89/278-Dir....	Installation of lighting and light-signaling devices....	N	I	I	I	I	I	I	I	I	I	I	I	Implementation 9/30/89.	
89/297-Dir*....	Side guards of certain vehicles and their trailers....	I	I	I	I	I	I	I	I	I	I	I	I	Implementation 10/30/89.	
89/458-Dir*....	Gaseous emissions from motor vehicles below 1,400 cc..	N	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/90.	
89/459-Dir....	Tread depth of tires of vehicles and their trailers....	N	I	I	I	I	I	I	I	I	I	I	I	Implementation 1/1/92.	

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Relevant U.S. Sector/Industry											Member state implementation	Comment
		B	G	DK	S	FR	GR	IT	IR	L	NL	P		
Standards--Continued														
Motor vehicles--Continued														
Enacted--Continued:														
89/460-Dir	Derogation for IR and UK regarding vehicle size													Derogation to 12/31/98.
89/461-Dir	Authorized dimensions for articulated vehicles													Implementation 1/1/91.
89/491-Dir	Vehicles' use of leaded or unleaded gasoline													Implementation 1/1/90.
89/516-Dir	End-outline marker lamps and front, rear, stop lamps													Implementation 12/31/89.
89/517-Dir	Headlamps and incandescent electric filament lamps													Implementation 12/31/89.
89/518-Dir	Rear fog lamps													Implementation 12/31/89.
Proposed:														
(76)701-Dir*	Weights and dimensions of certain vehicles													
(76)712-Dir*	Tires of vehicles													
(89)6-Dir	Amends 88/449-Dir regarding road worthiness tests													
(89)377-Dir	Spray-suppression devices for vehicles and trailers													
√(89)453-Dir	Masses and dimensions of vehicles of category M1													
√(89)573-Dir	Maximum authorized dimensions for road trains													
√(89)-xxx	A single EC motor-vehicle market													
√(89)653-Dir	Pneumatic tires for vehicles													
√(89)653-Dir	Safety glazing and glazing materials on vehicles													
√(89)662-Dir	Air pollution by emissions from vehicles													
Other machinery														
Enacted:														
86/217-Dir*	Requirements for tire-pressure gauges													Implementation 11/30/87.
86/594-Dir*	Labeling household appliances for noise emissions													Implementation 12/3/89.
86/662-Dir*	Noise from hydraulic diggers													Implementation 12/24/88.
87/402-Dir*	Rollover protection structures (see (89)582 below)													Implementation 6/25/89.
87/404-Dir*	Simple pressure vessels (see (89)636-Dir below)													Implementation 7/1/90.
87/405-Dir*	Permissible sound power level of tower cranes													Implementation 6/25/89.
88/180-Dir*	Permissible sound-power levels of tower cranes													Implementation 7/1/91.
88/181-Dir*	Permissible sound-power levels of lawnmowers													Implementation 7/1/91.
88/297-Dir*	Type-approval of wheeled tractors													Implementation 12/31/88.
88/465-Dir	Driver's seat on wheeled tractors													Implementation 9/10/88.
89/173-Dir*	Certain standards for tractors													Implementation 12/31/89.
89/240-Dir	Self-propelled industrial trucks													Implementation 1989.
89/392-Dir*	Safety requirements for machines (see (89)624-Dir)													
√89/686-Dir*	Personal protective equipment													Implementation 7/1/92.
√89/680-Dir	Roll-over protection structures of wheeled tractors													Implementation 1/2/91.
√89/681-Dir	Roll-over protection structures in front of driver's seat on narrow-track wheeled tractors													Implementation 1/2/91.
√89/682-Dir	Rear-mounted roll-over protection on narrow-track wheeled tractors													Implementation 1/2/91.
90/384-Dir*	Non-automatic weighing instruments													Implementation 1/1/93.
90/396-Dir*	Gas appliances													Implementation 1/1/92.

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Member state implementation													Comment	
		B	G	DK	S	FR	GR	IT	IR	L	NL	P	UK			
Standards--Continued																
Other machinery--Continued																
Proposed:																
√(89)454-Dir....	Batteries and accumulators with dangerous substances..														Potentially all	
√(89)582-Dir*...	Roll-over protection structures on tractors.....														Tractors	
√(89)624-Dir*...	Amends 89/392-Dir on mobile machinery.....														Machinery	
√(89)636-Dir*...	Amends 87/404-Dir on simple pressure vessels.....														Pressure vessels	
√(90)274-Dir....	Electrically operated lifts.....														Machinery	
√(90)13-Dir....	Electrical equipment used in explosive atmospheres.....														Machinery	
Telecommunications																
Enacted:																
86/361-Dir.....	Initial stage of the mutual recognition of type approval for telecommunications terminal equipment.														Telecom.	Implementation within 1 year following adoption.
86/659-Rec.....	Integrated Services Digital Network (ISDN); strengthened by resolution of 7/18/89 (89/C196/04).														Telecom.	Applicable 2/7/88.
87/95-Dec.....	Information technology and telecommunications.....														Telecom.	Member state to inform EC Commission of progress in implementation.
87/371-Rec*...	Public pan-European cellular digital land-based mobile communications.														Mobile phones	Implementation 12/25/88.
87/372-Dir*...	Frequency bands for pan-European mobile telephones....														Mobile phones	Applicable 7/26/88.
88/524-Dec*...	Development of information services market.....														Telecom.	Implementation 1/1/92.
89/336-Dir*...	Electromagnetic compatibility (radio interferences)...														Broadcasting	
89/552-Dir*...	Pursuit of television broadcasting activities.....														Broadcasting	
90/387-Dir*...	Open network provisions (ONP).....														Telecom.	Implementation 1/1/91.
Proposed:																
(88)588-Dec....	Information technology and telecommunications for health care - advanced informatics in medicine.														Potentially all	
(89)289-Dir*...	Telecommunications terminal equipment, including mutual recognition of their conformity.														Telecom.	
(89)452-Dec....	Standard European-wide emergency call number.....														Potentially all	
√(90)32-Rec.....	Pan-European land-based public radio paging.....														Communications	
√(90)32-Dir.....	Frequency bands for pan-European land-based public radio paging.														Communications	
Environment																
Enacted:																
86/279-Dir.....	Transfrontier shipment of hazardous waste.....														Potentially all	Implementation 1/1/97.
89/369-Dir.....	Pollution from new municipal waste incineration plants.														Waste	Implementation 12/1/90.
89/427-Dir.....	Air quality limit values and guide values for sulphur dioxide and suspended particulates.														Potentially all	Implementation 1/10/91.
√90/313-Dir.....	Access to information on the environment.....														Potentially all	Implementation 12/31/92.
√90/1210-Reg....	Establishes the European Environment Agency.....														Potentially all	Effective day after site of agency decided.

Table D-1.
List of EC initiatives considered in this investigation--Continued

Initiative	Description	Member state implementation											Comment	
		B	G	DK	S	FR	GR	IT	IR	L	NL	P		UK
Standards--Continued														
Environment--Continued														
Proposed:														
(89)7-Dir.....	Vessels entering or leaving EC ports carrying dangerous or polluting goods.													
(89)282-Dir.....	Civil liability for damage caused by waste.													
(89)478-Dir.....	Drinking, bathing, and surface water.													
(89)518-Dir.....	Municipal waste water treatment.													
(89)544-Dir.....	Protects fresh, coastal, and marine waters against pollution caused by nitrates from diffuse sources.													
(89)559-Dir*....	Shipment of radioactive waste.													
(89)560-Dir.....	Amended proposals on waste and hazardous waste.													
(90)3-Reg.....	Substances that deplete the ozone layer.													
(90)9-Dir.....	Pollution from dangerous substances discharged into the aquatic environment.													
(90)85-Dir.....	Sewage sludge in agriculture - limits for chromium....													
Agriculture														
Building products														
Enacted:														
89/106-Dir*....	Construction products.....													
Miscellaneous:														
Enacted:														
86/665-Rec.....	Standardized information in existing hotels.....													
86/666-Rec*....	Protection of hotels against fire.....													
86/378-Dir*....	Safety of toys.....													
90/314-Dir.....	Package travel, package holidays, and tours.....													
Proposed:														
(90)95-Dir.....	Child-resistant fastenings.....													
Generic														
Enacted:														
85/374-Dir.....	Liability for defective products.....													
87/357-Dir*....	Mislabeled products that endanger health and safety....													
88/182-Dir*....	Information on technical standards and regulations....													
88/314-Dir*....	Labeling of prices for nonfood products.....													
90/352-Dec.....	Exchange of information on dangers of consumer goods..													
Proposed:														
(90)284-Dec.....	Modules for conformity assessment procedures for use in technical harmonization directives.													
(90)55-Dec.....	Consumers' Consultative Council.....													
(90)259-Dir.....	General product safety.....													

APPENDIX E
INDEX OF INDUSTRY/COMMODITY ANALYSES
CONTAINED IN REPORT CHAPTERS 4 THROUGH 12

Note. — The industries listed in this index are those industries found to be potentially the most significantly affected by each of the various categories of EC 1992 directives. This listing is not a comprehensive listing of all U.S. industries.

INDEX OF INDUSTRY/COMMODITY ANALYSES

<i>Industry/Commodity</i>	<i>Directive category</i>	<i>Page</i>
Agriculture	Standards	4-46
Air Transport Sector	Transport	8-6
Automobiles	Standards	4-64
Banking	Financial Sector	5-3
Biotechnology	Standards	4-49
Bovine Semen, Deep-Frozen	Standards	4-47
Cellular Digital Mobile Communications	Standards	4-68
Chemicals	Standards	4-58
Cigarettes	Standards	4-56
Construction Products	Standards	4-71, 4-72
Dangerous Substances	Standards	4-60
Energy	Government Procurement	6-8
Foodstuffs, Labeling	Standards	4-53
Food, Materials in Contact With	Standards	4-57
Hormones	Standards	4-48
Insurance Services	Financial Sector	5-5
Investment/Securities Services	Financial Sector	5-4
Machinery	Standards	4-65
Meat: Hormones, Inspecting	Standards	4-48
Medical Equipment	Standards	4-62
Ocean Transport Sector	Transport	8-12
"Organic" Foods	Standards	4-52
Pharmaceuticals	Standards	4-61
Processed Foods	Standards	4-51
Radio Paging	Standards	4-69
Road- and Rail-Transport Services	Transport	8-9
Telecommunications	Standards	4-67
Terminal Equipment	Standards	4-67
Tobacco Products	Standards	4-54, 4-55, 4-56
Toys, Safety of	Standards	4-28