PHILIPPINES

TRADE SUMMARY

The U.S. trade deficit with the Philippines was $3.7 billion in 2002, an increase of $50 million from 2001. U.S. goods exports in 2002 were $7.3 billion, down 5.1 percent from the previous year. Corresponding U.S. imports from the Philippines were $11.0 billion, down 3.0 percent. Philippines is currently the 19th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to the Philippines were $1.6 billion in 2001 (latest data available), and U.S. imports were $1.4 billion. Sales of services in the Philippines by majority U.S.-owned affiliates were $888 million in 2000 (latest data available), while sales of services in the United States by majority Philippines-owned firms were $20 million.

The stock of U.S. foreign direct investment (FDI) in the Philippines in 2001 was $2.8 billion, up from $2.7 billion in 2000. U.S. FDI in the Philippines is concentrated largely in manufacturing, finance and banking sectors.

IMPORT POLICIES

Tariffs

Imported manufactured goods that are not locally produced generally face low tariffs, while imports that have local competition face tariffs of up to 30 percent. Under the Philippine Government's comprehensive tariff reform program, set out in Executive Orders (E.O.) 264 in 1995 and 288 in 1996, most-favored-nation (MFN) tariff rates applied to all goods (except sensitive agricultural products) were to be gradually reduced to the following target rates: 3 percent for raw materials by January 2003; 10 percent for finished products by January 2003; and a uniform 5 percent tariff rate for all remaining products by January 2004.

On January 3, 2001, during the final days of the Estrada Administration, rates were set out for the period from 2001 to 2004, which maintained 2000 tariffs for 2001 and proposed gradual rate reductions in 2002 and 2003 to meet the goal established under the Ramos Administration for a uniform 5 percent tariff rate for all products by January 2004. Exceptions to this plan included some raw materials that would face a 3 percent tariff rate for 2004, as well as finished automobiles and some agricultural goods, which would face higher rates. On April 17, 2001, the Arroyo Administration issued an order, which among other changes, lowered the tariff on automotive vehicle components from 10 percent to 3 percent under the Philippine Government's Commercial Vehicle Development Program, a program design to rationalize the auto industry and transform the Philippines into a regional hub for automotive production.

To promote local assembly under the Philippine Motor Vehicle Development Program, imports of finished automobiles (completely built-up units) are subject to the highest duty rate applied to nonagricultural products. By executive order, tariff rates for finished automobiles will remain at 30 percent and rates for completely knocked down vehicles will remain at 10 percent until the end of 2003. In 2004, the rates for both are scheduled to drop to 5 percent. A 3 percent tariff is imposed on crude oil and most refined petroleum products.

The Safeguard Measures Act, effective August 10, 2000, authorizes the Commissioner of Customs to raise a tariff or, in the case of an agricultural good, impose a quantitative restriction, to protect a domestic industry from an import surge. The U.S. Government has expressed reservations concerning the Philippine safeguards legislation, noting in particular that the five days afforded to foreign industry to comment on proposed safeguards is not a reasonable period of time as provided for in the WTO Agreement on Safeguards. The U.S. Government has requested that the Philippines lengthen the statutorily mandated period. The Philippines Government has responded that, under certain circumstances, the time to comment can be extended to 21 days. The United States will continue to urge the Philippines to address its concerns on this issue.

The Common Effective Preferential Tariff (CEPT) Agreement for the ASEAN Free Trade Area (AFTA) requires that tariff rates among ASEAN members on a broad range of products be reduced to between zero percent and 5 percent, while quantitative restrictions and other non-tariff barriers are to be eliminated. ASEAN members agreed on a firm timetable leading up to the full realization of AFTA in 2003.

Philippine Government announcements in January 2003 indicate that it intends to slow down its tariff reduction process. Signaling a reversal in policy, President Arroyo signed an executive order on January 9, 2003, which temporarily suspends the AFTA tariff reduction schedule on petrochemical resins and certain plastic products. As allowed for under AFTA, other ASEAN countries are seeking compensation from the Philippines for failing to lower its petrochemical tariffs.

Agriculture Tariffs and Import Licensing

The Philippines maintains high tariff rates on sensitive agricultural products, including grains, livestock and meat products, sugar, potatoes, onions, and coffee. Among these, 15 items (at the four-digit HS level) are subject to a minimum access volume (MAV) and tariff-rate quotas (TRQs). Several products with significant market potential for the United States are subject to TRQs, including corn (with an in- quota tariff rate of 35 percent and for 2003/2004 an out-of-quota tariff rate of 50 percent), poultry meat (in-quota and out-of-quota tariff rates equalized at 40 percent on July 1, 2003), and pork (in-quota rate of 30 percent through 2004, out-of-quota at 40 percent through 2004).

The Philippine Government established rules for implementing the 15 TRQs and allocating import licenses. In the past, the United States has expressed concerns that TRQs for pork and poultry meat were administered in a manner that allocated a vast majority of import licenses to domestic producers who had no interest in importing. Following intensive consultations, the Governments of the United States and the Philippines concluded a Memorandum of Understanding in February 1998 that resolved the United States' primary concerns over the Philippine TRQ system. The U.S. Government continues to closely monitor the operation of the Philippines TRQ system and the allocation and distribution of import licenses.

The Philippines issued an executive order in January 2001 that will reduce tariffs on most agricultural goods during the next several years. For example, tariffs for prepared meats, corn meal and pellets, and coffee would be reduced to 30 percent by 2004. Tariffs on other, less-sensitive goods, will be reduced to 5 percent.

The Philippine Fisheries Code permits importation of fresh, chilled, or frozen fish and fish products only when certified as necessary by the Secretary of Agriculture and upon issuance of an import permit by the Department of Agriculture. One of the criteria the Secretary is mandated to consider in determining whether to approve importation is whether there is serious injury or threat of injury to a domestic industry that produces like or directly competitive products.

Excise Tax on Distilled Spirits

Current Philippine law discriminates against many imported distilled spirits by subjecting them to a higher excise tax than applied to many common domestic spirits. Distilled spirits produced from indigenous materials (such as coconut palm, cane, and certain root crops) are subject to a specific tax of 8.96 pesos per proof liter. Distilled spirits produced from other raw materials (which would apply to most imports) are subject to a specific tax ranging from 84 pesos to 336 pesos per proof liter (depending on the net retail price per 750 ml bottle). Wines with an alcohol content of 14 percent or less by volume are assessed an excise tax of 13.44 pesos per liter, while wines with an alcohol content greater than 14 percent but less than 25 percent alcohol content by volume are charged an excise tax of 26.88 pesos per liter. Fortified wines (containing greater than 25 percent alcohol content) are taxed as distilled spirits. Depending on the net retail price per bottle, an excise tax of 112 pesos per liter for wines or 336 pesos per liter for sparkling wines is assessed.

A bill pending in the Lower House at the end of 2002 would revert the tax rates to more equitable levels through indexation. The bill would also reclassify alcohol and tobacco products based on their net retail prices in order to ensure that the appropriate tax rate is applied. Most importantly, the bill is expected to address the inherent bias of the present structure in favor of locally manufactured brands of distilled spirits produced from native materials.

The important features of the bill include: (a) restructuring the excise tax on distilled spirits through adoption of a single structure of tax rates for all distilled spirits regardless of the raw material used; (b) indexation of the tax brackets and tax rates using cumulative inflation of 37.3 percent from 1997 to 2001 to restore the real value of the unit taxes applied to "sin" products to their January 1, 1997 levels; (c) indexation of the tax brackets and tax rates two years thereafter by the amount of cumulative inflation for the two preceding years to ensure that the excise tax rates track changes in price; and (d) immediate reclassification of alcohol and tobacco products based on their current net retail price and reclassification of these products again in two years. The U.S. Government is monitoring developments on this issue closely.

Excise Tax on Automotive Vehicles

The excise tax for automotive vehicles is currently based on engine displacement, as opposed to vehicle value, generally discouraging imported vehicles, including those from the United States, with larger engine displacement. Current tax rates for motor vehicles with gasoline engines are: 15 percent for engines up to 1600 cubic centimeters (cc); 35 percent for those between 1601-2000cc; 50 percent for those between 2001-2700cc; and 100 percent for those 2701cc and above. For motor vehicles with diesel engines, excise rates are 15 percent for engines of up to 1800cc; 35 percent for those 1801-2300cc; 50 percent for those 2301-3000cc; and 100 percent for those 3001cc and above. Large utility vehicles with seating for ten or more, commonly referred to as Asian Utility Vehicles (AUVs), are exempt from this excise tax. U.S. industry raised concerns about this policy. In October 2002, the Department of Finance submitted to the Philippine Congress legislation to base the auto excise tax on value rather than on engine size, a more equitable means of assessment. The bill that would remove the tax exemption for AUV's is pending in the House of Representatives. While the U.S. Government supports revisions to the Philippines automotive tax structure, it has raised concerns that this tax cut will be accompanied by increases in duties on auto imports, despite the Philippines Government's commitment to tariff reductions on autos in 2004.

Quantitative Restrictions

The National Food Authority administers quantitative restrictions on rice imports. The minimum access volume (quota) for rice is 164,265 metric tons for 2002 and 194,135 metric tons for 2003. Rice import demand is expected to continue growing in the Philippines due to persistent shortfalls in local production and rapid population growth (2.3 percent annually). Due to this restriction, rice is frequently and commonly smuggled into the country from such countries as Vietnam.

The Philippine Department of Agriculture is in the process of opening up the importation of rice to the private sector. Currently, only the National Food Authority may legally import rice. While the opening to private sector participation is a welcome development, the U.S. Government has raised concerns that the plan to transfer import rights to domestic rice farmers ("Farmers as Importers" and "Farmers as Distributors") may result in discriminatory treatment toward imports.

Other Import Restrictions

The Philippines maintains import restrictions on a range of products. Since April 15, 1999, the National Telecommunications Commission (NTC) has required cellular telephone service providers or authorized equipment dealers to obtain an import certification prior to importation of cellular phone handsets. Imports of used automotive vehicles sales of which almost equal annual sales of new vehicles (about 80,000 per year) had been subject to government review and approval. The majority of these used vehicles come from Japan and Korea, and many of them do not meet environmental or safety standards. The U.S. Government raised concerns over this issue with the Philippines. In December 2002, President Arroyo signed an executive order banning the importation of used vehicles (except buses and special purpose vehicles). The order also permits only new original equipment manufacture parts and components to be imported for assembly purposes.

Customs Barriers

All importers or their agents must file import entries with the Bureau of Customs (BOC), which then processes these entries through its Automated Customs Operating System (ACOS). ACOS uses a computer system to classify shipments as low-risk (green lane), moderate risk (yellow lane) or high risk (red lane). The BOC requires a documentary review of shipments channeled through the yellow lane, while red lane shipments require physical inspection at the port. Green lane shipments are not subject to any documentary or inspection requirements. The BOC has also added a "Super Green Lane" for the largest importers. To date, only about 55 companies have made use of this customs facility, which was intended to serve 1,000 companies.

A 1996 law and series of 1999 regulations issued by the BOC were intended to implement transaction value as the basis of customs valuation on January 1, 2000, consistent with Philippine's WTO commitments. However, the law and regulations contained many deficiencies, and a new customs valuation law was passed in April 2001 to clarify the hierarchy of valuation methods to be used by the BOC. The law eliminated the requirement that the BOC maintain a price reference database for valuation purposes and authorized the BOC to conduct post-entry audits. The administrative order implementing this law was approved by the Department of Finance on November 16, 2001 and further clarifications on valuation methodology, post-entry audit, and appeals procedures were made in January 2002. Notably, the law eliminated private sector involvement in the valuation process and clarified that reference values may be used as a risk management tool, but not as a substitute value for valuation purposes. The U.S. Government remains concerned, however, about reported private sector involvement in the valuation process. The U.S. Government raised this issue during bilateral trade discussions in November 2002 and will continue to closely monitor implementation of the law and related measures. The United States has repeatedly requested that the Philippine Government improve administration of its customs regime and minimize import harassment. Under the preshipment inspection regime (PSI) operated until March 31, 2000, by Societe Generale de Surveillance, there were frequent abuses reported, including arbitrary and unjustified increases or "uplifts" of the invoice value of imports, often on the basis of inappropriate or questionable information. In late 2001, the Philippine Government announced it would consider returning its customs administration to a PSI system. The U.S. Government noted the problematic history of PSI and urged the Philippines to continue reforming its current customs regime without resorting to PSI. The Philippines Government made improvements to the valuation system, but periodic procedural irregularities continue to occur, including requests by customs officials for the payment of unrecorded facilitation fees. The U.S. Government repeatedly has raised concerns over hubless pipe, imports of which have been detained or denied by Philippines Customs authorities since 1993. The Philippine Government revised its National Plumbing Code effective March 2000, specifically permitting the use of hubless pipe in the Philippines. As of early 2003, longstanding obstacles to imports of this product appear to have been resolved by the Philippine judiciary. The U.S. Government continues to monitor this issue.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Industrial Goods

Local inspection for compliance with mandatory Philippine national standards is required for 75 products, including cosmetics, medical equipment, lighting fixtures, electrical wires and cables, cement, pneumatic tires, sanitary wares, and household appliances. For goods not subject to mandatory standards, U.S. manufacturers' self-certification of conformity is accepted. Labeling is mandatory for textile fabrics, ready-made garments, household and institutional linens, and garment accessories. Mislabeling, misrepresentation, or misbranding may subject an entire shipment, rather than just the offending goods, to seizure and disposal. The "Generic Act" of 1988 aims to promote the use of generic drugs by requiring that the generic name of a particular pharmaceutical appear above its brand name on all packaging.

Agricultural Goods

The Philippine Department of Agriculture (DA) established plant health regulations in 1995, which allow the import of U.S. apples, grapes, oranges, potatoes, onions, and garlic, provided these products do not originate from Florida or Texas. Importation of Florida grapefruit, oranges, and tangerines into the Philippines is permitted under a March 2000 protocol between the Philippines and the United States. However, fresh fruit imports from Texas are prohibited because of concerns regarding the possible presence of fruit flies. Similar protocols are being negotiated for a range of other fruits and vegetables, including cherries, broccoli, lettuce, and cauliflower.

The DA continues to use Veterinary Quarantine Certificates (VQCs) and import inspections to limit poultry meat imports. U.S. industry reports delays of up to one month in DA issuance of VQCs and DA limits on the issuance of VQCs for purchases outside the Minimum Access Volume (MAV) system to holders of MAV licenses. The U.S. Government will continue to urge the Philippines Government to address U.S. concerns on this issue.

In September 2002, DA announced plans to introduce mandatory third-party Hazard Analysis and Critical Control Point (HAACP) inspections for all meat and dairy plants exporting to the Philippines as of April 1, 2003. On February 24, 2003, however, the Philippine government postponed indefinitely implementation of this new regulation. The order would have required a third-party quarterly audit of all foreign meat and milk plants exporting to the Philippines for their compliance with internationally recognized standards of the HACCP program. The United States and other countries raised serious concerns about the consistency of this new requirement with the Philippines SPS commitments. U.S. industry estimated the proposed new requirement would result in losses of $55 million, roughly the dollar value of U.S. trade to the Philippines in the affected commodities.

The Philippine Government maintains a zero-tolerance policy for methanol in wine products. This policy requires that manufacturers submit a report on the manufacturing process to the Philippine Bureau of Food and Drug for evaluation before they can obtain a product registration and obtain an operating license.

GOVERNMENT PROCUREMENT

The Philippines is not a signatory to the WTO Government Procurement Agreement (GPA). In awarding contracts, the Philippine Government provides preferential treatment to local suppliers of pharmaceuticals, rice, corn, and iron/steel materials for use in government projects, and in locally funded government consulting requirements. Contractors for infrastructure projects that require a public utility franchise (i.e., water and power distribution, telecommunications, and transport systems) must be at least 60 percent Filipino-owned.

In 1993, the Philippine Government mandated a countertrade requirement for procurements by government agencies and government-owned or -controlled corporations that entail the payment of at least $1 million in foreign currency. Implementing regulations set the level of countertrade obligations at a minimum of 50 percent of the import price and set penalties for nonperformance of countertrade obligations.

The Philippine Government has taken some steps to reform its procurement process. In July 2000, it issued an executive order shifting emphasis from bidder's pre-qualification to an eligibility check and strengthened the post-qualification check by changing the criterion for award from lowest evaluated responsive bid to lowest calculated responsive bid. The bidder's available budget serves as the ceiling in evaluating bid price.

On January 10, 2003, President Arroyo signed the "Government Procurement Reform Act" into law. The law calls for public monitoring of the procurement process to promote greater transparency and competition, enhance the flow of information, and lessen discretion among agencies. It also establishes an electronic procurement system to serve as the single portal for all government procurement and requires that all bidders use standard forms. The law provides for goods to be obtained from domestic or foreign sources with two caveats, both of which appear to favor domestic suppliers. The law allows, in the interest of availability and timeliness, for the procuring entity to give preference to the purchase of domestically produced and manufactured goods, supplies and materials. Consulting services and infrastructure projects are exempt from this provision, putting foreign firms on equal footing with local firms in these sectors. For infrastructure projects, the law provides that, for the next five years, contractors whose head office is located in the province where the project will take place have the right to match the lowest offer made by a non-province based bidder. The U.S. Government will continue to monitor implementation of this law.

EXPORT SUBSIDIES

Enterprises and exporters engaged in activities under the Philippine Government's "Investment Priorities Plan" may register with the Board of Investments (BOI) for fiscal incentives, including four- to six-year income tax holidays, a tax deduction equivalent to 50 percent of the wages of direct-hire workers, and tax and duty exemptions for the importation of breeding stock and genetic materials. BOI-registered firms that locate in less developed areas may be eligible to claim a tax deduction of up to 100 percent of outlays for infrastructure works and 100 percent of incremental labor expenses. Firms in government-administered export processing zones, free trade zones, and other special industrial estates registered with the Philippine Economic Zone Authority (PEZA) enjoy similar incentives, as well as tax and duty-free imports of capital equipment and raw materials, and exemption from customs inspection. In lieu of national and local taxes, PEZA-registered firms are subject to a 5 percent tax on gross income. Firms that earn at least 50 percent of their income from exports may register with BOI or PEZA for certain tax credits under the Export Development Act, including a tax credit on incremental annual export revenue.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The development of comprehensive protection of IPR in the Philippines has been marked by uneven progress. Legislation to fully implement the WTO TRIPS Agreement commitments has been slow to develop, while enforcement agencies perennially have been hampered by a lack of resources and support from the judiciary. In April 2002, for the second consecutive year, the U.S. Government named the Philippines to the Special 301 Priority Watch List. USTR identified lax copyright enforcement, especially with regard to a booming illicit industry in optical disk piracy, as a particular area of concern. The U.S. Government has welcomed the progress made by the Philippines Government and President Arroyo's commitment to strengthening the Philippines' IPR regime, but raised concerns at the Ministerial level about the need for further significant progress. The United States has cited, in particular, the failure of the Philippine Government to pass and implement an optical disc law, the rampant production of optical media, the failure to pass bills on online commerce and e-commerce piracy, and the failure to improve the judiciary to prosecute IPR cases.

In addition to its commitments under the WTO TRIPS Agreement, the Philippines is a party to the Paris Convention for the Protection of Industrial Property, the Berne Convention for the Protection of Literary and Artistic Works, the Berne Treaty on the International Recognition of the Deposit of Microorganisms, Patent Cooperation Treaty, and the Rome Convention. The Philippines, as a member of the World Intellectual Property Organization (WIPO), ratified the WIPO Performances and Phonograms Treaty and the Copyright Treaty in March 2002. The treaties took effect in October 2002.

The Intellectual Property Code

The 1997 Intellectual Property Code provides the legal framework for IPR protection in the Philippines. The 2000 Electronic Commerce Act, extends this framework to the Internet. However, deficiencies in the Intellectual Property Code remain a source of concern, including ambiguous provisions on the rights of copyright owners over broadcast, rebroadcast, cable retransmission, or satellite retransmission of their works; burdensome restrictions affecting contracts to license software and other technology; and the judiciary's lack of authority to order the seizure of pirated material as a provisional measure without notice to the suspected infringer.

The Philippines Government took several positive steps to strengthen its IPR regime in recent years. In January 2002, the Philippines Supreme Court adopted rules establishing ex parte authority in civil cases of IPR infringement. On June 7, 2002, President Arroyo enacted legislation to comply with its TRIPS Article 27.3 (b) requirements on the protection of the exclusive rights of breeders with respect to their new plant varieties. In addition, in 2001, the Philippines enacted a new law to protect layout designs (topographies) of integrated circuits.

The Philippines has yet to enact legislation to regulate the import, export, and production of optical disks, and the tools and materials involved in the replication of optical disks. The House of Representatives passed an optical disk bill in October 2002, but the Senate has not acted on it. To date, Congress has also failed to adopt amendments that would extend further IPR protection to the Internet by accommodating e-commerce and outlawing online piracy. The U.S. will continue to urge the Philippines to strengthen its legislative and regulatory regime relating to IPR.

Status of IPR Enforcement

Under the Intellectual Property Code of the Philippines, the Intellectual Property Office (IPO) has jurisdiction to resolve certain disputes concerning alleged infringement and licensing. It is charged with coordinating IPR enforcement efforts, although its ability to do so has been limited to date. The IPO's administrative complaint mechanisms, established in April 2001, have yet to be fully tested. In addition to the IPO, agencies with IPR enforcement responsibilities include the Department of Justice, National Bureau of Investigation, Videogram Regulatory Board (covering for piracy involving cinematographic works), the Bureau of Customs, and the National Telecommunications Commission (for piracy involving satellite signals and cable programming). The Presidential Interagency Committee on Intellectual Property Rights, which was composed of representatives from these and other agencies, was tasked with coordinating enforcement efforts, but was dissolved in 2002 due to budgetary constraints.

Significant problems remain in ensuring consistent, effective and sustained IPR protection. U.S. industry estimates the annual losses due to piracy in the Philippines in 2002 at $116 million, not including losses to the entertainment software industry. U.S. distributors report high levels of pirated optical disks of cinematographic, musical works, and computer games, business software, and widespread unauthorized transmissions of motion pictures and other programming on cable television systems.

The Philippine Government has made some efforts to strengthen enforcement. It enacted a customs administrative order in September 2002 strengthening the ability of the Bureau of Customs (BOC) to prohibit the importation of pirated products, and creating an Interim Intellectual Property Unit within the BOC to oversee IPR violations at ports of entry. In addition, it increased raids on suspected counterfeit products resulting in the seizure and destruction of pirated goods valued in the millions of dollars. Joint efforts between the government and private sector have led to some successful enforcement actions. Nonetheless, serious problems continue to hamper the effective operation of agencies tasked with IPR enforcement. Resource constraints, already a problem, have been exacerbated by general government budgetary shortfalls. Enforcement agencies generally are not proactive in targeting infringement. The designation of 27 courts to handle IPR violations has done little to streamline judicial proceedings, as these courts have not received additional resources and continue to handle a heavy non-IPR workload. Delays in the issuance of warrants also are a problem and arrests are infrequent. In addition, IPR cases are not considered serious crimes and take a lower precedence in court proceedings.

There have been very few successful cases leading to prosecution and imprisonment. Companies spend significant resources on investigations and litigation, with many cases remaining unresolved for as long as a decade after the original complaint. Moreover, the Philippines has failed to establish punitive sanctions that are sufficiently strict to serve as a deterrent to IPR violators. For example, the nominal damage awarded by the Philippine courts in most IPR cases amounts to the cost of doing business, with no risk of imprisonment. Such penalties do not have a deterrent effect.

SERVICES BARRIERS

Basic Telecommunications

The Philippine Constitution limits foreign ownership of telecommunications firms to 40 percent. During the WTO negotiations on basic telecommunications services, the Philippines made commitments on most basic telecommunications services and adopted some procompetitive regulatory principles contained in the WTO Reference Paper. It did not provide market access or national treatment for satellite services and made no commitments regarding resale of leased circuits/closed user groups. The Philippine Government has yet to ratify the Fourth Protocol to the WTO General Agreement on Trade in Services (GATS), embodying its proposed obligations under the WTO Basic Telecommunications Agreement.

Financial Services

The Philippines also has yet to ratify the Fifth Protocol to GATS, embodying its obligations under the WTO Financial Services Agreement.

Insurance

Although current practice permits up to 100 percent foreign ownership in the insurance sector, the Philippines only committed in the GATS to a maximum of 51 percent equity participation and grandfathered existing insurers with more than 51 percent foreign equity. Under current regulations, minimum capitalization requirements increase with the degree of foreign equity. As a general rule, only the state-owned government insurance system may provide coverage for government-funded projects. A 1994 administrative order extended this policy to public and private build-operate-transfer projects. Private insurance firms, both domestic and foreign, regard this as a significant trade barrier. Current regulations require all insurance/professional reinsurance companies operating in the Philippines to cede to the industry-owned National Reinsurance Corporation of the Philippines at least 10 percent of outward reinsurance placements.

Banking

Pursuant to 1994 legislation, 10 foreign banks were permitted to open full service branches in the Philippines or to own up to 60 percent of a new or existing local subsidiary. Foreign branch banks are limited to six branches each. Four foreign-owned banks that had been operating in the Philippines prior to 1948 were each allowed to operate up to six additional branches. The Philippines only committed to foreign ownership at 51 percent in its 1997 WTO financial services offer and included a reciprocity test for authorization to establish a commercial presence. The General Banking Law of 2000 (signed in May 2000 to succeed the 1948 General Banking Act) created a seven-year window during which foreign banks may own up to 100 percent of one locally incorporated commercial or thrift bank (up from the previous 60 percent foreign equity ceiling). However, for the first three years, such foreign investment may be made only in existing banks, reflecting the current emphasis of the Bangko Sentral ng Pilipinas (BSP, the central bank) on banking sector consolidation. Current regulations mandate that majority Filipino-owned domestic banks should, at all times, control at least 70 percent of total banking system assets. Rural banking remains completely closed to foreigners.

Securities and Other Financial Services

Membership in the Philippine Stock Exchange is open to foreign-controlled stock brokerages that are incorporated under Philippine law. Foreign equity in securities underwriting companies is limited to 60 percent. Securities underwriting companies not established under Philippine law may underwrite Philippine issues for foreign markets, but not for the domestic market. Although there are no foreign ownership restrictions governing acquisition of shares of mutual funds, current law restricts membership on a board of directors to Philippine citizens. The Philippines took an MFN exemption on foreign equity participation in securities firms, stating that Philippine regulators would approve applications for foreign equity only if Philippine companies enjoy similar rights in the foreign investor's country of origin.

Advertising

The Philippine Constitution limits foreign ownership of advertising agencies to 30 percent. All executive and managing officers of advertising agencies must be Philippine citizens.

Public Utilities

The Philippine Constitution specifically limits the operation of certain utilities (water and sewage, electricity transmission and distribution, telecommunications, public transport) to firms with at least 60 percent ownership by Philippine citizens. All executive and managing officers of such enterprises must be Philippine citizens.

The June 2001 Electric Power Industry Reform Act provides for the privatization of the transmission and distribution assets of the National Power Corporation. Transmission and distribution require a public utility franchise under the Act, which would be subject to a 40 percent foreign-ownership ceiling (1986 Constitution). Legislation to allow for the privatization of the national transmission grid, known as Transco, continues to languish in the Senate. The privatization and modernization of the sector is considered critical to attracting additional foreign investment.

Practice of Professions

As a general rule, the Philippine Constitution reserves the practice of licensed professions (e.g., law, medicine, nursing, accountancy, engineering, architecture, customs brokerage) to Philippine citizens. Philippine law (R.A. 8182) also requires that preference be given to Philippine citizens in the hiring of consultants and other professionals necessary for the implementation of projects funded by foreign assistance. Legislation signed in February 1998 (R.A. 8555) gives the Philippine President the authority to waive this and other preferences applicable to the procurement of goods and services funded with foreign assistance.

Shipping

The Maritime Industry Authority prohibits foreign-flagged vessels from engaging in the provision of domestic carriage services. The country's bareboat chartering laws stipulate that Philippine-flagged vessels should be manned by a Filipino crew and disallows foreign crew/officers, except as supernumeraries.

Express Delivery Services

Foreign air express couriers and airfreight forwarding firms must either contract with a 100 percent Filipino-owned business to provide delivery services or establish a domestic company with a minimum of 60 percent Philippine-owned equity.

INVESTMENT BARRIERS

The 1991 Foreign Investment Act contains two "negative lists" enumerating areas where foreign investment is restricted. The restrictions stem from a constitutional provision that permits the Philippine Congress to reserve to Philippine citizens certain areas of investment. The scope of these lists was updated on August 24, 2000, and again on October 22, 2002. The list will be reviewed by the Executive again in 2004.

List A restricts foreign investment in certain sectors because of constitutional or other constraints. For example, the practice of licensed professions such as engineering, medicine, accountancy, environmental planning, and law is fully reserved for Filipino citizens. Also reserved for Filipino citizens are enterprises engaged in retail trade (with paid-up capital of less than $2.5 million, or less than $250,000 for retailers of luxury goods), mass media, small-scale mining, private security, cock fighting, utilization of marine resources, and manufacture of firecrackers and pyrotechnic devices. Up to 25 percent foreign ownership is allowed for enterprises engaged in employee recruitment and for public works construction and repair (with the exception of build-operate-transfer and foreign-funded or -assisted projects, that is, foreign aid, where there is no upper limit). Foreign ownership of 30 percent is allowed for advertising agencies, while 40 percent foreign participation is allowed in natural resource extraction (although the president may authorize 100 percent foreign ownership), educational institutions, public utilities, commercial deep sea fishing, government procurement contracts, rice and corn processing (after 30 years of operation, before which time 100 percent foreign participation is allowed), and ownership of private lands. Retail trade enterprises with paid-up capital of more than $2.5 million but less than $7.5 million were limited to 60 percent foreign ownership until March 2002, after which 100-percent foreign ownership was allowed. Enterprises engaged in financing and investment activities, including securities underwriting, also are limited to 60 percent foreign ownership.

List B restricts foreign ownership (generally to 40 percent) for reasons of national security, defense, public health, safety, and morals. Sectors covered include explosives, firearms, military hardware, massage clinics, and gambling. This list also seeks to protect local small- and medium-sized firms by restricting foreign ownership to no more than 40 percent in nonexport firms capitalized at less than $200,000.

In addition to the restrictions noted in the "A" and "B" lists, the Philippines generally imposes a foreign ownership ceiling of 40 percent on firms seeking incentives with the Board of Investment (BOI) under the annual investment priorities plan. While there are exceptions to the ceiling, divestment to reach the 40 percent level is required within 30 years of the initial investment, or longer as allowed by the BOI. As a general policy, the Philippine Department of Labor and Employment allows the employment of foreigners provided there are no qualified Philippine citizens who can fill the position. However, the employer must train Filipino understudies and report on such training periodically. The positions of elective officers (i.e., president, general manager and treasurer) are exempt from the labor market test and understudy requirements.

The 1987 Constitution bans foreigners from owning land in the Philippines. The 1994 Investors' Lease Act allows foreign companies investing in the Philippines to lease land for 50 years, renewable once for another 25 years, for a maximum 75 years.

Trade-Related Investment Measures (TRIMS)

The BOI imposed industry-wide local content requirements under its Motor Vehicle Development Program. Local content requirements in the motor vehicle sector are based on a point system, which translates to 40 percent for passenger cars and 45 percent for commercial vehicles of less than three tons. These requirements are to be eliminated by July 2003.

The program also requires an investment of $10 million in parts and components manufacturing for export and domestic markets to establish a vehicle assembly facility ($8 million for trucks/commercial vehicles). This program authorizes the BOI to create a mandatory parts list as part of the local content requirement for manufacturers.

In 1995, pursuant to the WTO TRIMS Agreement, the Philippines notified the WTO of its maintenance of local content and foreign exchange balancing requirements to promote investment. Proper notification allowed the Philippines to maintain such measures for a five year transitional period, ending January 1, 2000. In October 1999, the Philippines requested a five year extension for the measures in the motor vehicle sector. After extensive consultations on this issue, the United States and the Philippines agreed in November 2001 that the Philippines would discontinue the exchange balancing requirements immediately and remove all local content requirements in the motor vehicle sector by July 1, 2003, following the implementation of a phase-out program begun in January 2002. The final phase out of the local content requirements is July 1, 2003. The U.S. Government is continuing to closely monitor Philippine implementation of this agreement.

Under a 1987 executive order, the soap and detergent industry is required to use a minimum of 60 percent of raw materials that do not endanger the environment, and prohibits imports of laundry soap and detergents containing less than 60 percent of such raw materials. The law is intended to require soap and detergent manufacturers to use coconut-based surface active agents of Philippine origin. In 1999, the Philippine Department of Justice stated that this executive order conflicts with the Philippines' obligations under the WTO TRIMS Agreement and since then, while not repealed, the order has not been enforced.

The United States continues to monitor other TRIMS. Regulations governing the provision of BOI- administered incentives impose a higher export performance for foreign owned enterprises (70 percent of production should be exported) than for Philippine owned companies (50 percent). A 1987 executive order requires that pharmaceutical firms purchase semisynthetic antibiotics from a specific local company, unless they can demonstrate that the landed cost of imports is at least 20 percent less than that produced by the local firm. A 1984 measure, which requires mining firms to prioritize the sale of copper concentrates to the then government-controlled Philippine Associated Smelting and Refining Company (PASAR), has yet to be repealed despite PASAR's privatization in 1998. In addition, there appear to be unwritten "trade balancing" requirements for firms applying for approval of ventures under the ASEAN Industrial Cooperation scheme.

TRIMS and Retail Trade

Legislation passed by the Philippine Congress in February 2000 requires that foreign retailers, for 10 years after the bill's enactment, source at least 30 percent (for retail enterprises capitalized at no less than $2.5 million) and 10 percent (for retail enterprises specializing in luxury goods) of their inventory, by value, in the Philippines. In addition, prospective investors in the retail sector face a reciprocity requirement. The Retail Trade Act states that only nationals from, or juridical entities formed or incorporated in countries that allow the entry of Filipino retailers, shall be allowed to engage in retail trade in the Philippines.

Public Utilities

The Philippine Government's most recent privatization effort, the June 2001 Electric Power Industry Reform Act, requires the National Power Corporation (NPC) to privatize at least 70 percent of its generating assets within three years. Seventy-five percent of the funds used to acquire NPC assets must be inwardly remitted and registered with the Philippine Central Bank. However, foreign participation may be restricted pursuant to a constitutional provision regarding utilization of certain natural resources (such as water and geothermal resources) and power generation as well as provisions requiring a minimum 60 percent Filipino ownership to obtain water rights for hydropower generation under the implementing rules of the 1976 Water Code of the Philippines.

Licensing of Technology

Technology transfer arrangements are defined as contracts involving the transfer of systematic knowledge for the manufacture of a product, the application of a process, or rendering of a service including management contracts, and the transfer, assignment, or licensing of all forms of intellectual property rights, including computer software (except for software developed for the mass market). The Intellectual Property Office requires that all technology transfer arrangements comply with provisions outlined in R.A. 8293, including the prohibition of the use of certain clauses in such arrangements. The scope of these provisions is extremely broad and serves to obstruct the normal contracting process between unrelated parties or as part of intra-company business.

ANTICOMPETITIVE PRACTICES

The 1987 Constitution provides the Philippine Government with the authority to regulate or prohibit monopolies, and it also bans combinations in restraint of trade and unfair competition. However, there is no comprehensive competition law to implement this constitutional provision. Instead, there are a number of laws dealing with competition, including the 1930 Revised Penal Code, the 1961 Act to Prohibit Monopolies and Combinations in Restraint of Trade , 1949 Civil Code, the 1980 Corporation Code , the 1991 Price Act, and the 1932 Consumer Act. Enforcement agencies do not adequately enforce these laws, as they do not have the resources or capability to challenge well-entrenched economic and political interests.

ELECTRONIC COMMERCE

On June 19, 2000, the Electronic Commerce Act took effect. The Electronic Commerce Law provides that business transactions entered into through an automated electronic system such as the Internet are functional and legal, equivalent to a written document protected under existing laws on commerce. Business-to-business transactions include domestic and international exchange of information, arrangements and contracts for procurement, payments, supply management, transportation, and facility operations. An Internet service provider (ISP) generally is not criminally liable if the ISP does not directly commit any infringement or other unlawful activities or does not cause another party to commit any unlawful act. The act includes provisions to penalize, among other offenses, hacking or cracking (unauthorized access into or interference in a communications system) and piracy (or the unauthorized reproduction, distribution, importation, use, removal, alteration, and downloading, or broadcasting of copyrighted works including legally protected sound recordings). Electronic transactions are not currently subject to any tax measures. However, a reciprocity clause specifies that all benefits, privileges, and advantages established under the act will be enjoyed only by parties whose country of origin grants the same benefits and privileges or advantages to Philippine citizens.

OTHER BARRIERS

Corruption is a pervasive and longstanding problem in the Philippines. The Philippine Revised Penal Code, the Anti-Graft and Corrupt Practices Act, and the Code of Ethical Conduct for public officials are intended to combat suspected corruption and related anticompetitive business practices. The Office of the Ombudsman investigates cases of alleged graft and corruption involving public officials. The Sandiganbayan (anti-graft court) prosecutes and adjudicates cases filed by the Ombudsman. In addition, a Presidential Commission Against Graft and Corruption is tasked with prosecuting corruption cases linked to the former Marcos regime.

Soliciting/accepting and offering/giving a bribe are criminal offenses, punishable with imprisonment of between six and 15 years, a fine and/or disqualification from public office or business dealings with the government. As with many other laws, enforcement of this provision has been inconsistent. An initiative to strengthen public and private governance, including anticorruption efforts, was launched in cooperation with bilateral and multilateral aid donors, particularly the World Bank, in May 2000. To date, results of this initiative have been limited.

An October 2000 USAID-funded survey of more than 600 randomly-selected Philippine and foreign- invested enterprises in the capital region suggests that graft remains a serious problem at many levels in all branches of the Philippine Government. Almost three-fourths of the enterprises surveyed had extensive or moderate personal knowledge of public-sector corruption on matters directly related to their sector of business. Nearly one-half believed companies need to give bribes to win public sector contracts, whether local or national. The Bureau of Customs; Bureau of Internal Revenue; Department of Public Works and Highways; Department of Education, Culture and Sports; and the Philippine National Police were rated as the most corrupt agencies. The Philippines is not a signatory of the OECD Convention on Combating Bribery.

Both foreign and domestic investors have expressed concern about the propensity of courts and regulators to stray beyond matters of legal interpretation into policymaking functions and about the lack of transparency in these decisionmaking processes. Investors complain that these officials rarely have any background in economics, business, or a competitive economic system and that entrenched economic interests are able to manipulate the legal system and regulatory process to protect market position. For example, spectrum allocation and licensing in the telecommunications sector is well guarded by incumbent firms, despite regulations that require transparent distribution of these rights.