PHILIPPINES

TRADE SUMMARY

The U.S. goods trade deficit with Philippines was $2.1 billion in 2006, a decrease of $277 million from $2.4 billion in 2005. U.S. goods exports in 2006 were $7.6 billion, up 10.5 percent from the previous year. Corresponding U.S. imports from Philippines were $9.7 billion, up 4.8 percent. Philippines is currently the 26th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Philippines were $1.7 billion in 2005 (latest data available), and U.S. imports were $1.7 billion. Sales of services in Philippines by majority U.S.-owned affiliates were $1.8 billion in 2004 (latest data available), while sales of services in the United States by majority Philippines-owned firms were $19 million.

The stock of U.S. foreign direct investment (FDI) in Philippines in 2005 was $6.6 billion (latest data available), up from $6.0 billion in 2004. U.S. FDI in Philippines is concentrated largely in the manufacturing, finance, and non-bank holding companies sectors.

The United States and the Philippines concluded a bilateral Trade and Investment Framework Agreement (TIFA) in 1989. In recent years, the United States and the Philippines have held regular meetings under the TIFA. The United States has used the TIFA to discuss and seek resolution of many issues that threaten to inhibit bilateral trade and investment. The United States-Philippines TIFA is a component in the Enterprise for ASEAN Initiative, which was launched by President Bush in October 2002.

IMPORT POLICIES

Tariffs

In January 2003, the Philippine government announced that it would undertake a comprehensive review of all tariff lines. The Tariff Commission issued recommendations for increased tariffs in several sectors and a slowdown of its tariff reduction plans in others. While the increased tariffs, which took effect in 2004, remain below the WTO bound rates, they represent a reversal of the hard fought reforms of successive previous Philippine administrations during the 1990s. According to the WTO, in 2005 the Philippines simple average bound tariff for all goods was 25.6 percent, while its simple average applied tariff for all goods was 6.3 percent.

Previous progress on tariff liberalization took shape through a series of reform programs beginning in 1995. Normal trade relations/most favored nation tariff rates on all goods (except sensitive agricultural products) were to be gradually reduced to the following target rates: 3 percent for raw materials and 10 percent for finished products by January 2003, and a uniform 5 percent tariff rate for all remaining products by January 2004. Executive Orders 241 and 264, signed by Philippine President Arroyo in October and December 2003, respectively, raised tariff rates on more than 1,000 product lines and maintained 2002 rate levels for an even greater number of product lines. Affected products include industrial goods produced domestically, such as chemical fertilizers, cement, and consumer products, including apparel and footwear. The orders raised rates on these products from the previous rates of between 3 percent and 10 percent to between 5 percent and 20 percent.

The Philippine government is currently reviewing the tariff program and had expected to publish a five-year (2006 to 2010) tariff program schedule via executive order before the end of 2006, though it had not done so as of March 2007. With regard to the classification of products within tariff codes, at least one major U.S. company has reported inconsistency by the Bureau of Customs in the application of tariff classifications.

The Common Effective Preferential Tariff (CEPT) Agreement for the ASEAN Free Trade Area (AFTA) requires that tariff rates among the original six ASEAN members, including the Philippines, on a broad range of products be reduced to between zero percent and 5 percent or below by end-2003, while quantitative restrictions and other non-tariff barriers were to be eliminated. ASEAN members agreed on a firm timetable leading up to the full realization of this initial stage of AFTA by the end of 2003. The Philippines has reduced duties to 5 percent or below on 99 percent of all tariff lines under the AFTA-CEPT. Moreover, as a result of the November 2004 ASEAN Summit, members agreed to implement the ASEAN Sectoral Integration Protocols, which legally bind them to undertake accelerated integration measures in 11 priority sectors. In January 2007 ASEAN leaders added Information and Communications Technology as the 12th priority sector for liberalization. These sectors account for 71 percent of 2003 intra-ASEAN trade and include electronics, E-ASEAN (electronic commerce/usage/connectivity among ASEAN countries), health care, wood-based products, automotive products, rubber-based products, textiles and apparel, agri-based products, fisheries, air travel, and tourism.

Automobile Sector Tariffs

Executive Order 264 in 2003 specifically lowered the tariff on automotive vehicle components from 10 percent to 3 percent under the Philippine government's Motor Vehicle Development Program (MVDP), a program meant to rationalize the automotive industry and transform the Philippines into a regional hub for automotive production. To promote local assembly under the program, imports of finished automobiles (completely built-up units) and motorcycles have been subject to the highest duty rate applied to non-agricultural products, resulting in a high rate of effective protection in the automotive sector. Under the MVDP, completely-knocked down (CKD) kits can be imported at preferential tariff rates if they "promote efficiency in the domestic industry." increase value-added, create jobs, and transfer technology. The tariff rate on CKD ranges between 1 percent and 3 percent.

Executive Orders 418 and 419 of April 2005 increased the tariff rates on certain types of automobiles. Executive Order 418 imposed a specific duty of 500,000 pesos (approximately $10,000 per vehicle) on top of the *ad valorem* duty on used vehicles. However, the high tariff imposed on the importation of used vehicles has yet to be implemented since a temporary restraining order was initiated shortly after the passing of EO 418. EO 419 increased from 30 percent to 35 percent the duties on high engine displacement vehicles under a stated pretext as an energy conservation and environmental measure. Under AFTA-CEPT, the tariffs on automobile components are set at 3 percent and 5 percent on passenger cars.

Excise Tax on Automotive Vehicles

In August 2003, the Philippine Congress passed legislation changing the automotive excise tax structure from one based on engine displacement to a system based on vehicle value. The old system generally discouraged imported vehicles with large engine displacement, including those from the United States. The August 2003 law covers most types of imported and locally manufactured vehicles, except for some trucks defined as motor vehicles designed for cargo and buses, which are classified by their tonnage. Vehicles that had been tax-exempt under the "10-seater rule" that applied to vehicles containing at least

10 seats including Asian utility vehicles (AUVs, a small version of the sport utility vehicle sold in Asian countries including the Philippines), are now taxed under the new system.

Under the revised excise tax scheme, vehicles are divided into four brackets based on their price: (1) for vehicles with a manufacturer's price of 600,000 pesos and below, the tax is 2 percent; (2) for those priced over 0.6 million to 1.1 million pesos, the tax is 12,000 pesos plus 20 percent of the amount in excess of 600,000 pesos; (3) for those priced over 1.1 million to 2.1 million pesos, the tax is 112,000 pesos plus 40 percent of the amount in excess of 1.1 million pesos; and (4) for those over 2.1 million pesos, the tax is 512,000 pesos plus 60 percent of the amount in excess of 2.1 million pesos.

Safeguards

The Safeguard Measures Act (Republic Act 8800), enacted in 2000, authorizes the Secretary of Trade and Industry or the Secretary of Agriculture to impose safeguard measures in order to remedy injury due to a sudden and sharp increase in imports and facilitate the structural adjustments for domestic industry to be competitive with other markets. 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 has drafted amendments to the Safeguards Measures Act extending the period to file answers by interested parties from five days to 30 days. The said draft was submitted to Congress for approval, but Congress had not acted as of March 2007.

In November 2001, the Philippine government put in place a safeguard to protect local cement producers from imports. The Secretary of Trade and Industry imposed the safeguard duty despite the finding of the interagency Tariff Commission that there was no merit to the cement producers' case. This decision was brought to the Philippine Supreme Court and in July 2004, the Court ruled that the safeguard duty was illegal and overturned the safeguard. The Philippine government continues to levy safeguard duties on imported ceramic floor and wall tiles, float glass, figured glass and glass mirrors, and provisional safeguard duties on sodium tripolyphosphates (technical grade).

Agriculture Tariffs and Import Licensing

The average nominal tariffs on agricultural products remained at 11.3 percent in 2005. High tariffs are still maintained on politically sensitive agricultural products, such as grains, livestock, poultry and meat products, sugar, frozen and processed potatoes, onions, coffee, and fresh citrus, including oranges, lemons, and grapefruit.

In 2002, the Philippines issued several executive orders that provided for tariff reductions for most agricultural products through 2004. However, in January 2003, the Philippines reversed this policy by issuing Executive Order 164, which set tariff rates for most agricultural products at their generally higher 2002 levels with the exception of pork, poultry, processed meats, corn, coffee and vegetables. Executive Order 264, issued in 2003, raised tariff rates on some product lines. These rates have been extended to an even greater number of food and agricultural products, including those for which the United States has a substantial market share.

The U.S. Government continues to monitor the operation of the Philippine tariff-rate quota (TRQ) system closely, including the allocation and distribution of import licenses. In particular, the U.S. Government is monitoring the Philippine government's application of its Veterinary Quarantine Clearance (VQC) certificates for meat and poultry imports, as well as its import permit system for fresh vegetables. In response to pressure from domestic producers to limit imports as well as to crack down on illegal importation of meat and poultry into the country, the Philippine Department of Agriculture (DA) maintains a VQC import-licensing scheme for imported meat and poultry. The amended meat import regulation under the Administrative Order (AO) 26 series of 2005 (AO26) reiterates the need for an accredited importer to obtain a VQC certificate prior to the importation of meat and meat products. A VQC will now be valid for 60 days from the date of issuance, within which the meat or meat products are to be shipped from the country of origin, and may no longer be extended beyond that. The regulation still requires a one-time use of a VQC, meaning that each VQC must be surrendered upon arrival of a shipment of a covered product. When the quantity allowed on a VQC is insufficient to cover the amount in a container, the importer must supply an additional VQC to cover the difference. Any remaining tonnage from that second VQC is subsequently forfeited rather than the importer being given credit for the unused tonnage. This practice creates the appearance of discretionary licensing and fosters imprecision in this statistical tracking of import volumes.

Although the U.S. Government has registered its concern with the Philippine government regarding the VQC process and has requested that its application be made more flexible, transparent and WTO consistent, these concerns have not been addressed. The DA Bureau of Plant Industry (BPI) also regulates imports of fresh fruits and vegetables. All imports of fresh produce require phytosanitary clearances from BPI which also serve as import licenses. These permits are applied for by the Philippine importer for each shipment. Like meat and meat products, import permits for fruits and vegetables need to be secured prior to exportation from the United States. The date of shipment cannot be earlier than that of the import permit.

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. The Secretary issues a certificate of necessity when he deems import is essential for achieving food security and the import will not cause serious injury or threat of injury to a domestic industry that produces like or directly competitive products. This process appears to be a discretionary application of import licensing.

Excise Tax on Distilled Spirits and Tobacco Products

Republic Act 9334 of December 2004 raised the taxes on alcohol and tobacco products and stipulated further biennial increases until 2011. The law maintained the preferential treatment the Philippines gives to distilled spirits produced from indigenous raw materials in its excise tax regime, which is a tiered tax structure based on net retail price. This tax regime continues to impede access to the Philippine market for U.S. exports of higher-value distilled spirits and is a primary reason why U.S. exports to this potentially significant market remain quite small.

The December 2004 legislation increased the excise tax by 30 percent for distilled spirits produced from indigenous sources, raising the tax from 8.96 pesos to 11.65 pesos on every liter of distilled spirits made from raw materials such as coconut palm, cane, and certain root crops. It also increased the excise tax by 50 percent on distilled spirits made from other materials (which would apply to most imports) and on fortified wines (wines containing more than 25 percent alcohol content) from a range of 84 pesos to 336 pesos per 750 ml bottle to a range of 126 pesos to 504 pesos per bottle. The legislation also increased the excise tax on fermented liquor by 20 percent to a range of 8.27 pesos to 16.33 pesos per liter of volume capacity. Still wines with an alcohol content of 14 percent or less by volume were assessed an excise tax of 17.47 pesos per liter of volume capacity, while still wines with an alcoholic content greater than 14 percent but less than 25 percent alcohol content were charged an excise tax of 34.94 pesos per liter of volume capacity. Depending on the net retail price per bottle, an excise tax ranging from 145.60 pesos to

436.80 pesos per liter of volume capacity was assessed on sparkling wines and champagnes. Republic Act 9334 increases these rates on alcohol products by 8 percent every other year until 2011. In 2007, excise taxes therefore will rise to 12.58 pesos per proof liter of distilled spirits made from indigenous ingredients; to between 136.08 pesos to 544.32 per 750 ml bottle for other distilled spirits and fortified wines; to between 8.93 pesos to 17.64 pesos per liter of volume capacity for fermented liquors; to between 18.87 pesos to 37.74 pesos per liter of volume capacity for still wines; and, to 157.25 pesos per liter of volume capacity for sparkling wines and champagnes.

The Philippines also maintains a multi-tiered excise tax system based on the retail prices of cigarettes, with Republic Act 9334 stipulating biennial increases until 2011. Low-priced machine-packed cigarettes with a retail price below 5 pesos per pack and hand-rolled cigarettes were assessed a tax of 2 pesos in 2005, rising every other year to 2.72 pesos by 2011. Medium-priced machine-packed cigarettes with a net retail price between 5 pesos and 6.50 pesos per pack were assessed a tax of 6.35 pesos in 2005, rising every other year to 7.16 pesos by 2011. High-priced cigarettes with net retail prices above 6.50 pesos up to 10 pesos per pack were charged a tax of 10.35 pesos in 2005, rising every other year to 12 pesos by 2011. Premium cigarettes with net retail prices above 10 pesos per pack were charged a tax of 25 pesos in 2005, rising every other year to 28.30 pesos by 2011. In 2007, the excise tax on cigarettes increases to 2.23 pesos per pack for hand-rolled and low-end machine-packed cigarettes; 6.74 pesos per pack for medium-priced cigarettes; 10.88 pesos per pack for high-priced cigarettes; and, 26.06 pesos per pack for premium cigarettes. The legislation assessed an *ad valorem* tax of 10 percent per cigar with a net retail price of 500 pesos or lower, and a tax of 50 pesos plus 15 percent of net retail prices in excess of 500 pesos.

Republic Act 9334 also provides that alcohol and cigarette brands sold in the domestic market as of October 1996 be classified according to their 1996 net retail prices for excise tax purposes. Brands introduced between January 1997 and December 2003 are classified according to their net retail prices as of the end of 2003. This provision effectively provides existing (mostly domestic) brands with preferential excise tax treatment relative to new brands/entrants.

U.S. firms have noted that the Documentary Stamp Tax involves a denial of national treatment with respect to cigarettes. Although the National Internal Revenue Code requires that tax stamps be affixed to all cigarettes sold in the Philippines, it is only effectively enforced on imported cigarettes. Because of lax enforcement, domestically-produced cigarettes are often shipped to outlets without the stamps and without paying the connected taxes.

Quantitative Restrictions

The National Food Authority, a state trading enterprise, controls rice imports and administers an import quota. It imports any shortfall in rice production under the import quota. The 2006 minimum access volume (quota) for rice was set at 238,000 metric tons, unchanged from the previous year's level. The tariff on imported rice, whether in or out of quota, is 50 percent. Rice import demand is expected to continue growing in the Philippines due to persistent shortfalls in local production and a high population growth rate (1.95 percent annually). Rice is illegally imported into the country on a regular basis from various rice-producing countries in the region.

Among sensitive agricultural products, 15 items are subject to a minimum access volume administered through tariff-rate quotas (TRQs). The Philippines' 10-year minimum access commitments under the Uruguay Round expired in June 2005. Final-year TRQ commitments are being maintained until such time as the products are liberalized or new commitments are negotiated under the Doha Development Agenda. For rice, a commodity for which the Philippines receives special treatment under Annex 5 of the

Uruguay Round Agricultural Agreement, the Philippine government petitioned WTO Members for an extension until 2012. In return for various agricultural concessions, nine countries (Thailand, Pakistan, Egypt, China, Argentina, the United States, Canada, India, and Australia) have provisionally accepted the Philippines' extension. Several other products with significant market potential for the United States are also subject to TRQs. These include: corn, with an in-quota tariff rate of 35 percent and an out-of-quota tariff rate of 50 percent for 2006; chicken meat, with an equalized in-quota and out-of-quota tariff rate of 40 percent; turkey meat, with an in-quota tariff of 30 percent and out-of quota tariff of 35 percent to 40 percent; and pork, with an in-quota rate of 30 percent and out-of-quota rate of 40 percent.

Other Import Restrictions

The Philippines maintains import restrictions on a number of goods on the grounds of public health, morals, national security, and meeting international treaty obligations regulating certain products. Imports require clearances and permits from appropriate government agencies. Among the regulated commodities are essential and precursor chemicals included in the U.N. Convention Against Illicit Drug Trafficking; penicillin and its derivatives; sodium cyanide, chlorofluorocarbons and other ozone depleting substances; coal and its derivatives; color reproduction machines; various chemicals for the manufacture of explosives, fireworks and firearms; pesticides including agricultural chemicals; used motor vehicle parts and motorcycle components; warships of all kinds; radioactive materials; used clothing and rags; used tires; toy firearms and explosives; laundry and industrial detergents containing hard surfactants; all government importation; and Philippine currency in amounts exceeding P10,000,000 coin blanks and bank notes. Also subject to government regulation are industrial products subject to mandatory standards: aircraft; telecommunications; video tapes, VCDs, DVDs, tobacco, cigars and cigarettes.

Customs Barriers

The Philippine government has made some progress during the last several years toward bringing its customs regime into compliance with its WTO obligations, but corruption and other irregularities remain commonplace. Republic Acts 8181 (1996) and 9135 (2001), with supporting regulations, implemented the WTO Agreement on Customs Valuation. The Philippines discontinued the use of Home Consumption Value and adopted transaction value for the purpose of calculating *ad valorem* rates of duty. Supporting regulations also provided the Bureau of Customs (BOC) with the authority to create a post-entry audit unit, a risk management unit and a border control unit charged with enforcement of intellectual property rights.

Currently, all importers or their agents must file import declarations with the BOC, which it then processes through its Automated Customs Operating System (ACOS). ACOS uses its selectivity system to classify shipments as low-risk (green lane), moderate-risk (yellow lane), or high-risk (red lane). All shipments channeled through the yellow lane require a documentary review, while red lane shipments require both documentary review and physical inspection at the port. Green lane shipments are not subject to any documentary or inspection requirements. In early 2002, the BOC also announced the addition of a "Super Green Lane" facility for importers acknowledged as the lowest risk. The import transactions of Super Green Lane importers are not covered by the selectivity system and are exempt from documentary and physical examination. Because of low use during implementation which took place in December 2003, the BOC lowered the cost to companies of accessing the facility. By the end of 2004, 86 firms were using these facilities.

Republic Act 9135 eliminated private sector involvement in the valuation process. It also clarified that reference values may be used as a risk management tool, but not as a substitute for valuation. The U.S. Government remains concerned, however, about reports of continued private sector involvement in the valuation process, particularly in the activities of BOC's Import Specialist Team, which has the authority to review all green lane entries for possible valuation-related offenses. The Philippines has 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 has raised this issue during bilateral trade discussions during the past several years.

The U.S. Government continues to have concerns about inconsistent application of customs rules and procedures, undue and costly processing delays, and corruption. The United States has regularly urged the Philippine government to improve the administration of its customs regime. Customs administration could be strengthened by improving classification of entries and providing precise descriptions of imported articles to reduce discretionary authority of customs officials. Reform and modernization within the BOC is being supported through technical assistance by USAID and several other donor organizations, including the Millennium Challenge Account Threshold Program.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Industrial Goods

Local inspection for compliance with mandatory Philippine national standards is required for 91 products, including automotive and motorcycle batteries, cosmetics, medical equipment, lighting fixtures, fire extinguishers, electrical wires and cables, cement, pneumatic tires, sanitary wares, and household appliances. For goods not subject to such 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 encourage the use of generic drugs by requiring that the generic name of a pharmaceutical appear above its brand name on all packaging.

Agricultural Goods

The Philippine Department of Agriculture (DA) established plant health regulations in 1995 that allow the import of U.S. apples, grapes, oranges, potatoes, onions, and garlic, provided these products, when necessary, undergo a specified cold treatment to control targeted pests. Importation of Florida grapefruit, oranges, and tangerines into the Philippines is permitted under a March 2000 protocol between the Philippines and the United States. Similarly, under a July 2004 protocol, importation of cherries from the United States is permitted.

The United States and the Philippines are currently negotiating the import protocols for broccoli, cauliflower, lettuce, carrots, cabbage, and celery produced in the United States. The target date for completion of the pest risk analysis for the vegetables is in early 2007. In the interim, the Philippines has continued to allow these products to enter into the country provided that they are intended for “high-end markets” only.

In January 2004, the DA issued Memorandum Order No. 33 (MO 33), which imposed new requirements for beef and beef products imported from the United States. This was in response to the detection of Bovine Spongiform Encephalopathy in a single imported dairy cow in the State of Washington in December 2003. Only deboned and deglanded beef and beef products derived from cattle 30 months of age or less are allowed entry into the country. Other specified requirements include certification that the beef comes from healthy and ambulatory cattle and is devoid of nerve tissue and any specified risk materials. Moreover, the production or slaughter date of the cattle must be provided on the packaging label. On December 19, 2006, the Bureau of Animal Industry of the Philippine Department of Agriculture formally allowed the importation of heart, liver and cheek meat of U.S. beef cattle subject to requirements stated in DA Memorandum Order No. 33.

On December 23, 2006 the DA issued new regulations on the accreditation of foreign meat establishments (FMEs) from which meat and meat products are sourced for exports to the Philippines. The new guidelines would require all exporting countries or individual FMEs to obtain either systems or individual accreditation to be eligible as legitimate suppliers. At present, all U.S. meat establishments that are regulated and inspected by the USDA Food Safety and Inspection Service are eligible to export meat and poultry to the Philippines. Countries including the United States that have traditionally exported to the Philippines under a systems accreditation approach will be subject to an audit within one year of implementation of the new regulation, which took effect on January 7, 2007.

GOVERNMENT PROCUREMENT

Although the Philippines is not a signatory to the WTO Agreement on Government Procurement (GPA), the Philippine government has taken some steps to reform its procurement process. The Government Procurement Reform Act of 2003 consolidated numerous procurement laws and issuances and standardized guidelines, procedures, and forms across Philippine government agencies, government-controlled corporations, and local government units. The law simplified pre-qualification procedures, introduced more objective, non-discretionary criteria in the selection process, and established an electronic procurement system to serve as the single portal for government procurement activities. The Government Procurement Reform Act also mandated public monitoring of the procurement process to promote greater transparency and competition, enhance the flow of information, and lessen discretion among agencies.

Nevertheless, the Government Procurement Reform Act's Implementing Rules and Regulations (IRRs) for locally funded government projects continue to favor purchases from Filipinos and Filipino-controlled companies. As a general rule, goods and supplies for locally funded projects must be purchased from enterprises that are at least 60 percent Philippine-owned, infrastructure services from enterprises with at least 75 percent Philippine ownership, and consulting services with at least 60 percent Filipino-controlled entities. For infrastructure projects, the law also provides that, for five years from the effective date of the law, contractors whose head office is located in the province where the project will take place have the right to match the lowest offer by a non-province-based bidder.

The Philippine government, in consultation with foreign donors, has yet to issue implementing rules and regulations covering procurement for projects involving foreign financing or assistance, reportedly because of strong pressure to favor local suppliers (which may contradict donor procurement policies). The Official Development Assistance (ODA) Act (Republic Act 8182, as amended in February 1998 by Republic Act 8555) waived the preference for local suppliers for projects involving ODA. Foreign donors have been able to implement their procurement regulations under the provisions of the ODA Act. The Build Operate Transfer (BOT) Law (Republic Act 6957 of July 1990, as amended in May 1994 by Republic Act 7718) allowed investors in BOT projects to engage the services of Philippine or foreign firms for the construction of BOT infrastructure projects.

In 2004, President Arroyo issued Executive Order 278, which provides for preferential treatment for Filipino consultants in public sector infrastructure projects. The Executive Order stipulates that, as much as possible, the government should fund consultancy services for its infrastructure projects with local funds, using local resources and expertise. When Filipino capability is determined to be insufficient, Filipino consultants may hire or work with foreign consultants, but must be the lead consultants. Where foreign funding is indispensable, foreign consultants are required to enter into joint ventures with Filipinos. Foreign donors have so far been able to comply with their respective procurement guidelines without violating Executive Order 278. However, because an executive order has the force of law, the specter of problems arising in the future remains. In addition to concerns about discriminatory treatment against foreign firms, U.S. companies continue to raise concerns about corruption in government procurement.

The Philippine government issued Executive Order 120 in 1993 mandating 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 counter trade obligations at a minimum of 50 percent of the import price and set penalties for nonperformance of countertrade obligations.

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. As a general rule, an enterprise must be at least 60 percent Filipino-owned and, if export-oriented, export at least 50 percent of its production to qualify for BOI incentives. Enterprises with less than 60 percent Filipino equity may qualify provided they engage in projects listed as “pioneer” under the IPP or they export at least 70 percent of production. 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 Philippines’ Export Development Act, including a tax credit on incremental annual export revenue.

Automotive Export Subsidies

With the intention of promoting the local assembly and export of vehicles from the Philippines, President Arroyo signed Executive Order 244 in October 2003, which launched the Philippine Automotive Export Program (AEP), subsequently modified by Executive Order 312, issued in 2004. The export incentives program offers automobile manufacturers registered under the AEP preferential tariff rates in their importation of finished automobiles on the basis of equivalent net foreign exchange earnings (NFEE) from their finished vehicle exports. An equivalent NFEE, $400 per unit exported for year one to two of the program, $300 for year three, phased down to $100 by year five, will be credited. The benefit of availing of preferential tariff rates is contingent upon export performance. The net foreign exchange earning chargeable against imports is on a per unit basis and continues until the credit has been exhausted, after which the manufacturer pays the normal tariff rates on its imports. The reduced tariff rates are: MFN rates of 30 percent will become to 20 percent of the CIF value of importation; MFN rates of 20 percent will become 10 percent of the CIF value of importation; and, the ASEAN Common External Preferential Tariff (CEPT) rate of 5 percent will become 4 percent of the CIF value for imports from the other ASEAN countries.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

In February 2006, the United States moved the Philippines from the Special 301 "Priority Watch List" (where it had been listed for five consecutive years) to the "Watch List" to acknowledge the steps the Philippines has to take to strengthen its IPR regime. Following the announcement, President Arroyo and other senior government officials pledged continued momentum and increased effort on IPR initiatives.

Despite the general improvement in the IPR protection regime, the U.S. Government continues to have serious concerns about the consistency and effectiveness of IPR protection in the Philippines. Significant problems remain in ensuring consistent and effective IPR protection. U.S. distributors continued to report high levels of pirated optical discs as well as widespread unauthorized transmissions of motion pictures and other programming on cable television systems. Counterfeit goods such as brand name and designer clothing, handbags, cigarettes, and other consumer goods are widely available. Optical media piracy, including piracy of DVDs and CD-Rs, also continues to be a problem. Although some improvement is visible in select shopping malls, it is unclear yet whether this represents a long-term trend.

President Arroyo signed into law the Optical Media Act (OMA) on February 10, 2004. The OMA is intended to regulate the import, export and production of optical discs, including tools and materials involved in their manufacture. In addition, the OMA created the Optical Media Board as a replacement for the Videogram Regulatory Board. On February 1, 2005, the Congressional Oversight Committee approved implementing regulations for the Optical Media Act. Full implementation and enforcement of this law and regulations, including prosecution of IPR violators, will be critical to strengthening the Philippines' IPR regime.

While the Philippines has made progress in combating optical media piracy through passage of the OMA, it has generally failed to improve the prosecution and conviction of IPR violators to create a credible deterrent. Print piracy and end-user piracy of business and entertainment software also are serious problems. The United States has encouraged the Philippines to further improve and sustain enforcement efforts and to take steps to enhance judicial capacity.

IPR protection is a special concern for the textile and apparel sectors. U.S. apparel companies spend large amounts of money on brand protection and vigorously engage the Philippines on IPR enforcement. Clothing with counterfeit brand labels is routinely available in Philippine shopping areas, much of which is reportedly imported.

Intellectual Property Laws

The 1997 Intellectual Property Code provides the basic legal framework for IPR protection in the Philippines. The 2000 Electronic Commerce Act extends this framework to the Internet. However, the Code contains ambiguous provisions relating to the rights of copyright owners over broadcast, rebroadcast, cable retransmission, or satellite retransmission of their works, and burdensome restrictions affecting contracts to license software and other technology. The Philippine government has nonetheless taken positive steps in recent years to address legislative deficiencies in its IPR regime. In 2001, the Philippines enacted a new law to protect layout designs (topographies) of integrated circuits. In January 2002, the Philippine Supreme Court adopted rules establishing *ex parte* seizure authority in civil cases of IPR infringement (*i.e.,* seizure without notice to the suspected infringer).

In June 2002, President Arroyo approved legislation designed to comply with WTO Trade Related Aspects of Intellectual Property Rights (TRIPS) Article 27.3(b) requirements on the protection of the exclusive rights of breeders with respect to their new plant varieties. However, U.S. seed company representatives have expressed concern about the vagueness of key provisions of the law, particularly relating to a provision exempting local farmers from licensing requirements.

In addition to adhering to the TRIPS Agreement, the Philippines is a party to the Paris Convention, the Berne Convention, the Budapest Treaty, the 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 WIPO Copyright Treaty in March 2002. The treaties took effect in October 2002. However, the Philippine government has not yet enacted necessary amendments to its copyright law that would fully implement the requirements of these WIPO treaties into domestic law. The U.S. Government continues to urge the Philippines to enact this needed legislation.

As of December 2006, the Philippine Congress was considering legislation to reduce patent protection for pharmaceutical products. If passed, this legislation could weaken some patent protection provisions in the Intellectual Property Code related to pharmaceutical products.

IPR Enforcement

The United States continues to have serious concerns regarding the lack of consistent, effective and sustained IPR enforcement in the Philippines. U.S. industry estimated the annual losses due to copyright piracy in the Philippines in 2005 at around $123.6 million. In 2006, U.S. distributors continued to report high levels of piracy of optical disks of films and musical works, computer games, and business software, as well as widespread unauthorized transmissions of motion pictures and other programming on cable television systems. Trademark infringement in a variety of product lines is also widespread, with counterfeit or pirated merchandise openly available in both legitimate and illegitimate venues.

The U.S. Government continues to encourage effective action and full funding support for IPR enforcement efforts and judicial capacity building. The U.S. Government also has called for the closure of malls and other outlets where pirated optical discs are the primary products being offered. The U.S. Government has urged the Philippines to adopt laws that would extend further IPR protection to the Internet by accommodating electronic commerce and outlawing online piracy, and to take further steps to combat piracy of textbooks and other printed materials. The U.S. Government continues to provide technical assistance and training to strengthen capacity within Philippine agencies responsible for IPR protection.

Serious problems nonetheless continue to hamper the effective operation of agencies tasked with IPR enforcement. Interagency coordination is improving within the Philippine government, but many enforcement agencies continue to suffer from a lack of resources. Enforcement efforts such as raids and seizures have increased in frequency over the past two years. The Optical Media Board (OMB) continues to work towards full operational capability in its efforts to combat domestic production of pirated optical media. The OMB continues to conduct numerous raids against optical media production lines and retail outlets, resulting in increasing seizures of production equipment and finished product. Yet the legal system in the Philippines continues to undermine the best enforcement efforts and courts often release suspects picked up in OMB raids and drop their cases on questionable technical grounds.

The Philippine government has taken some administrative steps intended to strengthen enforcement. The Intellectual Property Code of the Philippines stipulates that the Intellectual Property Office (IPO) has jurisdiction to resolve disputes concerning alleged infringement and licensing. The IPO has implemented a more robust leadership role on enforcement issues in the Philippines, and, in February 2006, was granted oversight authority over law enforcement efforts. Components of the IPO's strategy include a greater emphasis on interagency coordination, enforcement campaigns in partnership with private industry, and sustained outreach efforts to inform the public on IPR issues.

A Bureau of Customs (BOC) administrative order in September 2002 strengthened the ability of the BOC to prohibit the importation of pirated products, and created an Intellectual Property Unit within the BOC. The BOC maintains an IPR registry where property holders may record their rights and other information to facilitate enforcement. However, the IP Unit is an *ad hoc* entity and does not have adequate institutional or resource support to fulfill its mandate effectively. The Unit is handicapped by inadequate staffing, few resources, and lack of access to critical Customs computer information systems.

In late 2005, the Supreme Court created a Task Force on Intellectual Property Rights, which identified three judges and a team of prosecutors who will focus on IPR cases and receive specialized training. The Task Force was reorganized in July 2006 and is composed of entirely new personnel. In 2006, fifteen judges were identified for specialized IPR training. These judges handle other commercial and criminal cases such as money laundering, but their primary responsibility is for IPR cases. Frequent changes in personnel and structure have limited the effectiveness of this mechanism. If appealed, IPR cases would still go through the current appellate system, which permits numerous interlocutory appeals and can result in long delays.

Among those cases that have made it to court, there have been relatively few successful prosecutions. While companies have invested significant resources in investigations and litigation, some cases remain unresolved as long as two decades after the initial complaint. The Philippines has failed to establish punitive sanctions sufficient enough to serve as a deterrent to IPR violators. The nominal damages awarded by the Philippine courts in IPR cases add little to the cost of doing business for IPR pirates, and thus far there has been no risk of imprisonment for offenders.

SERVICES BARRIERS

Basic Telecommunications

The Philippine Constitution of 1987 defined telecommunication services as a public utility and limited foreign ownership to 40 percent. This restricts market entry, especially in more capital-intensive applications, such as broadband, where foreign firms are reluctant to invest without majority control. In addition, foreigners are restricted from serving as executives or managers and the number of foreign directors in telecommunication companies must be proportionate to its aggregate share of foreign capital. Foreign equity in the private radio communications network is constitutionally limited to 20 percent. Operation of cable television and other forms of broadcasting and media are also reserved for Filipinos.

Voice-Over-Internet Protocol (VOIP) Rules

The National Telecommunications Commission (NTC) issued a ruling (Memorandum Circular No. 3-11-2005) in 2005 that removes uncertainty over the status of VoIP services, as these services were not easily categorized by the 1995 Public Telecommunications Policy Act (Republic Act 7925). This law limits the provision of traditional telephone services to "Public Telecommunications Entities" holding a congressional franchise, but exempted value added service (VAS) providers from the franchise requirement.

The Memorandum Circular defined VoIP as a value added service, removing the requirement for a legislative franchise to offer service. Any entity who wishes to offer VoIP must register as VAS provider.

The VoIP registration fee is P50,000 per year, with a filing fee of P180. There is a minimum required capital of P10,000,000 and a performance bond of P5,000,000 to register as a VAS provider.

There are two levels of VoIP service: provider and reseller. Resellers operate Public Calling Offices while VoIP providers offer access via broadband Internet connections. VoIP providers must have interconnection agreements with a public telecommunications entity providing local exchange carrier service to a fixed telephone service network operator, while a reseller simply sells access to the service of a VoIP provider. A reseller need not comply with the minimum capital requirement of P10 million. The registration fee is P5000 per year, the filing fee is P180 per year, and a performance bond of P1 million is required for a reseller.

During the WTO negotiations on basic telecommunications services, the Philippine government made commitments on most basic telecommunications services and adopted some pro-competitive regulatory principles contained in the WTO Reference Paper. It did not provide market access or national treatment for satellite services (which remain subject to discriminatory rules) and did not allow resale of private leased lines.

Digital Terrestrial Television

In November 2006, the NTC published a draft Memorandum Circular for Digital Terrestrial Television (DTT). The draft, if finalized without changes, would adopt the European Digital Video Broadcast – Terrestrial standard for the delivery of DTT services in the Philippines. If unchanged, the delivery standard will also have implications for the products designed to transmit digital broadcasts. The draft Memorandum envisions a transition period from analog transmissions to DTT transmission through December 31, 2015.

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 regulations permit 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 Service Insurance System (GSIS) may provide coverage for government-funded projects. Administrative Order 141, issued in August 1994, also required proponents and implementers of Build-Operate-Transfer projects and privatized government corporations to secure their insurance and bonding from the GSIS at least to the extent of the government's interests. 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

Per the Foreign Bank Liberalization Act of 1994, 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 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 a 51 percent level 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 acquire up to 100 percent of one locally incorporated commercial or thrift bank (up from the previous 60 percent foreign equity ceiling). Such investments can be made only in existing banks since the Bangko Sentral ng Pilipinas (the central bank) imposed a moratorium on the issuance of new bank licenses in September 1999 to encourage consolidation in the banking system. 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.

Pre-1997 legislation exempted banks' Foreign Currency Deposit Units (FCDUs) as well as Offshore Banking Units (OBUs) from certain non-income taxes (*i.e.,* gross receipts tax, documentary stamp tax, and branch profit remittance tax). In 1997, a Comprehensive Tax Reform Program (CTRP) was signed into law to broaden the tax base. The final version of the CTRP, due to faulty drafting, inadvertently withdrew these tax exemptions by leaving out the phrase "exempt from all taxes." May 2004 legislation subsequently restored the tax exemptions enjoyed by FCDUs and OBUs but the Bureau of Internal Revenue (BIR) subsequently started to assess back taxes and penalties for the intervening period (1998-2004). Even though one bank has paid the taxes assessed by the BIR, other members of the Bankers Association of the Philippines are still pursuing exemption from these taxes. Philippine legislators have indicated that there was no intention to rescind the exemptions in the CTRP.

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, and 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. These limitations also apply to the operation of public utilities under Build-Operate-Transfer and similar arrangements.

The June 2001 Electric Power Industry Reform Act mandated the privatization of the generation and transmission assets of the National Power Corporation. The privatization and restructuring of the sector is considered critical to attracting additional foreign investment, but so far few assets have been sold. Transmission and distribution require a public utility franchise under the Act, which would be subject to a 40 percent foreign ownership ceiling (1987 Constitution). After a series of failed offerings, the government decided to privatize the national transmission grid, known as Transco, by awarding a 25 year concession, renewable for another 25 years. The Philippine government will seek a congressional franchise after the concession is awarded. Though stated to be a top priority, only seven small hydroelectric generating stations have been sold, which represent a mere 3 percent of total generating assets.

Practice of Professions

As a general rule, the Philippine Constitution reserves the practice of licensed professions (*e.g.,* law, medicine, nursing, accountancy, and engineering, architecture, and customs brokerage services) to Philippine citizens.

Shipping

Under Philippine cabotage laws, foreign-flagged vessels cannot engage in the carriage of domestic trade cargoes. In specific cases, Philippine-registered ships engaged in international trade may be issued a special permit to engage temporarily in domestic trade services. These permits can only be issued if: there is no existing Philippine-flagged vessel operating on the proposed route; there is no suitable local vessel available; the vessel is contracted by private or public utilities; and it involves tourist passenger vessels, when the itinerary includes calls at domestic ports. Philippine government cargo is reserved to Philippine-flagged vessels, though exemptions are permitted if these vessels are unavailable at "reasonable" freight rates. Only Filipino nationals or locally incorporated entities authorized to engage in overseas shipping and with a maximum of 40 percent foreign equity may register a vessel. Philippine-registered vessels must be completely manned by Filipino crews, except as supernumerary for up to six months.

Express Delivery Services

Foreign air express couriers and airfreight forwarding firms must either contract with a 100 percent Philippine-owned business to provide local delivery services, or establish a domestic company with a minimum of 60 percent Philippine equity. While there has been some liberalization of international cargo services, U.S. carriers already benefited from cargo provisions in the U.S. - Philippines Air Transport Agreement that allowed them to establish hub operations in the Philippines. However, one major U.S. carrier with a cargo hub in the Philippines has announced that it is moving its Asian hub at Subic Bay to China.

The Civil Aeronautics Board (CAB) sought to expand international scheduled and chartered services for specific airports through CAB Resolution No. 23 (series of 2005) to allow unlimited flight frequencies over and above the existing entitlement provided in bilateral air services agreements. This resolution applies to Diosdado Macapagal International Airport, Subic Bay International Airport, Davao International Airport, Mactan, Cebu International Airport, Laoag International Airport, Zamboanga International Airport, and other developmental gateways.

INVESTMENT BARRIERS

The 1991 Foreign Investment Act contains two "negative lists," collectively called the "Foreign Investment Negative List" (FINL), enumerating areas where foreign investment is restricted. The Foreign

Investment Act requires the Philippine government to update and publish the FINL every two-years. The most recent FINL was released in November 2004.

List A restricts foreign investment in certain sectors by mandate of the Constitution and specific laws. For example, 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 certain marine resources, and manufacture of firecrackers and pyrotechnic devices are reserved for Filipino nationals.

The Philippine government allows up to 25 percent foreign ownership for enterprises engaged in employee recruitment and for public works construction and repair, with the exception of Build-Operate-Transfer and foreign-funded or foreign-assisted projects (that is, projects that benefit from foreign aid, for which there is no upper limit on foreign ownership). 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 for large-scale projects), educational institutions, public utilities, commercial deep sea fishing, certain government procurement contracts, ownership of condominium units, and rice and corn production and processing. Full foreign participation is allowed for retail trade enterprises with paid-up capital of $2.5 million or more, provided that investment for establishing each store is not less than $830,000, or specializing in high-end or luxury products, provided that the paid-up capital per store is not less than $250,000. Financing companies and investment houses 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 gaming activities. This list also addresses local small- and medium-sized firms by restricting foreign ownership to no more than 40 percent in non-export firms capitalized at less than $200,000.

In addition to the restrictions noted in lists "A" and "B", firms with more than 40 percent foreign equity that qualify for Board of Investment (BOI) incentives must divest to the 40 percent level within 30 years from registration date or within a longer period determined by the BOI. Foreign-controlled companies that export 100 percent of production are exempt from this divestment requirement. 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. BOI-registered companies may employ foreign nationals in supervisory, technical, or advisory positions for five years from registration, extendable for limited periods at the discretion of the BOI. The positions of elective officers of majority foreign-owned enterprises (*i.e.,* president, general manager, and treasurer or their equivalents) are not subject to this limitation.

The Philippine Constitution of 1987 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. Deeds are often difficult to establish and are poorly reported and regulated. The deeds and property infrastructure is full of ambiguities, which makes it difficult to establish clear ownership. The court system does not settle cases in a timely manner. Land ownership issues such as these need to be clarified for domestic landowners before foreign land ownership can become viable.

Trade Related Investment Measures (TRIMS)

The BOI-imposed, industry-wide local content requirements under the Motor Vehicle Development Program were eliminated in July 2003. In 1995, pursuant to the WTO TRIMS Agreement, the Philippines notified the WTO of its maintenance of local content and foreign exchange balancing requirements. 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 with the United States, the Philippines agreed in November 2001 that it 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 and foreign exchange requirements was completed in 2003. The U.S. Government is continuing to monitor Philippine implementation of this WTO commitment closely.

Under a 1987 Executive Order, the soap and detergent industry is required to use a minimum of 60 percent locally-produced raw materials that do not endanger the environment. The intent of the law is to compel soap and detergent manufacturers to use coconut-based surface-active agents (soft surfactants) of Philippine origin. In 1999, the Philippine Department of Justice determined that this Executive Order conflicts with the Philippines' obligations under the WTO TRIMS. Subsequent to the ruling, the order has not been enforced, but it has not been repealed. Moreover, a 1990 law (Republic Act 8970) prohibits manufacture, importation, distribution, and sale of laundry and industrial detergents containing hard surfactants. Only natural oleo chemicals, including those derived from coconut, palm, palm kernel, sunflower, and rapeseed oils are allowed.

The United States continues to monitor the Philippines' compliance with other TRIMS requirements. Regulations governing the provision of BOI-administered incentives impose a higher export performance requirement for foreign owned enterprises (70 percent of production should be exported) than for Philippine-owned companies (50 percent). 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. Under a 1982 executive order (EO 776), the Bureau of Foods and Drugs requires pharmaceutical firms to purchase semi-synthetic antibiotics from a specific local company, except when these firms can show that the landed cost of imports are at least 20 percent cheaper.

Retail Trade

The Retail Trade Liberalization Act (Republic Act 8762) of 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) or 10 percent (for retail enterprises specializing in luxury goods) of their inventory, by value, in the Philippines. Foreign retailers are likewise prohibited from engaging in trade outside their accredited stores. At the same time, retail enterprises with foreign ownership exceeding 80 percent of equity are required to offer 30 percent of their shares to the public within eight years after the start of operations. In addition, prospective investors in the retail sector face a reciprocity requirement. The Retail Trade Liberalization 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 important privatization effort, the June 2001 Electric Power Industry Reform Act, provided that the National Power Corporation (NPC) should privatize at least 70 percent of its generating assets located in Luzon and Visayas within three years. Privatization stalled and no asset has been privatized since December 2004 when five small hydroelectric and one large coal-fired power plant were sold. Bidding for a 225 MW Bataan thermal and a 600 MW Calaca coal-fired power plant is ongoing. Seventy-five percent of the funds used to acquire NPC assets must be inwardly remitted and registered with the BSP (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 of 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

The Philippine government defines technology transfer arrangements as: (1) contracts involving the transfer of systematic knowledge for the manufacture of a product; (2) the application of a process, or rendering of a service including management contracts; and, (3) 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.

Mining

The Philippine Supreme Court, in a decision issued in December 2004, reversed its January 2004 ruling that declared key provisions of the Mining Act of 1995 unconstitutional and prohibited majority foreign-owned firms from mining in the Philippines. The reversal opened the sector to direct foreign investment. As such, mineral exploration and processing licenses are open to full foreign equity participation for large projects valued at over $50 million; small and medium-scale mining is reserved for Filipinos. The country’s unexploited mineral wealth is estimated at $840 billion. The Philippines has some of the richest deposits of metallic and non-metallic minerals in the world (especially copper and gold). Mining output is currently about $500 million per year. There are nine million hectares where mineral deposits may be found, although the Philippine government has issued permits for only 1.4 percent of those lands. Significant barriers to investment remain, such as unresolved disputes regarding land claims and a paucity of progress in implementing key regulatory and administrative reforms.

Other Investment Issues

The Supreme Court disallowed the Clark Special Economic Zone fiscal incentives provided under the Bases Conversion Development Act, although the underlying court case has been appealed. Over 350 investors, including 10 U.S. firms, maintain investments at Clark. Nonetheless, unforeseen taxes, including retroactive taxation, may lead to investor withdrawals from Clark and discourage new investment.

ANTICOMPETITIVE PRACTICES

The Philippine Constitution provided the Philippine government with the authority to regulate or prohibit monopolies, and it also banned combinations of entities in restraint of trade and unfair competition. However, the Philippines has 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 1932 Consumer Act, the 1961 Act to Prohibit Monopolies and Combinations in Restraint of Trade, 1949 Civil Code, the 1980 Corporation Code, and the 1991 Price Act. Enforcement agencies do not effectively enforce these laws, as they do not have the resources or capability to challenge entrenched economic and political interests.

ELECTRONIC COMMERCE

The Electronic Commerce Law, signed in June 2000, provides that business transactions through an automated electronic system such as the Internet are functionally and legally equivalent to a written document governed by 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 for unlawful activities conducted using its services 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 law 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, 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 pervasive and a longstanding problem in the Philippines. The Philippines' score in Transparency International's annual Corruption Perceptions Index survey has averaged 2.5 to 2.6 (out of a best score of 10) since 2002, down from 3.6 in 1999. 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 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 Anti-Graft Commission is tasked with investigating and hearing administrative cases of presidential appointees in the executive branch and government-owned and controlled corporations.

Soliciting or accepting any offering or giving a bribe are criminal offenses, punishable by 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, however, enforcement of anti-corruption laws has been inconsistent. The Philippine government launched an initiative to strengthen public and private governance, including anti-corruption efforts, in cooperation with bilateral and multilateral aid donors in May 2000. Results of this initiative have been mixed and have not reached a critical mass to improve public perception appreciably.

The Philippine government has worked in recent years to re-invigorate its anti-corruption drive. In December 2003, the President issued an executive order creating an anti-corruption watchdog - the

Revenue Integrity Protection Service (RIPS) - in the Department of Finance that has worked closely with the Ombudsman to help curb corruption in revenue collection agencies. President Arroyo has articulated her desire to strengthen the Office of the Ombudsman to become as efficient as Hong Kong's Independent Commission Against Corruption, and each year since 2005, has made significantly higher budget requests for this office. In November 2004, the Philippines became eligible for the Millennium Challenge Account Threshold Program. In June 2006, the Millennium Challenge Corporation approved a two-year $21 million grant to implement the Philippines Threshold Country Plan which focuses on strengthening the anti-corruption capabilities of the Office of the Ombudsman and tax collection agencies, including RIPS.

Both foreign and domestic investors express concern over the propensity of Philippine courts and regulators to stray beyond matters of legal interpretation into policymaking functions and about the lack of transparency in these decision-making processes. In addition, there are many reports that courts influenced by bribery improperly issue temporary restraining orders impeding the conduct of legitimate commerce. Investors also have raised concerns that regulators rarely have any background in economics, business, or a competitive economic system, which enables entrenched interests to manipulate the legal system and regulatory process, whether by bribery or through exploiting the lack of expertise among regulators, to protect market positions.