THE PHILIPPINES

TRADE SUMMARY

The U.S. goods trade deficit with the Philippines was $1.7 billion in 2007, a decrease of $383 million from $2.1 billion in 2006. U.S. goods exports in 2007 were $7.7 billion, up 1.3 percent from the previous year. Corresponding U.S. imports from Philippines were $9.4 billion, down 3.0 percent. The Philippines is currently the 29th largest export market for U.S. goods.

U.S. exports of private commercial services (*i.e.*, excluding military and government) to the Philippines were $1.9 billion in 2006 (latest data available), and U.S. imports were $1.8 billion. Sales of services in Philippines by majority U.S.-owned affiliates were $1.9 billion in 2005 (latest data available), while sales of services in the United States by majority Philippines-owned firms were $18 million.

The stock of U.S. foreign direct investment (FDI) in the Philippines was $7.0 billion in 2006 (latest data available), up from $6.4 billion in 2005. U.S. FDI in the Philippines is concentrated largely in the manufacturing and finance sectors.

The United States and the Philippines meet regularly under their Trade and Investment Framework Agreement to discuss outstanding issues and possible initiatives to further deepen trade and investment relations as well as to coordinate on regional and multilateral issues.

IMPORT POLICIES

Tariffs

The Philippines simple average bound tariff was 25.6 percent in 2006, while its simple average applied tariff was 6.3 percent. However, only two-thirds of the Philippines' tariff lines are bound under WTO rules. The Philippine government reviewed its tariff program and released a 5 year (2006 to 2010) tariff program schedule, which took effect in April 2007. To meet its commitments under the ASEAN Free Trade Area, the Philippines has reduced duties to 5 percent or below on 99 percent of total ASEAN Harmonized Tariff Nomenclature tariff lines.

The average tariff on agricultural products remained at 11.8 percent in 2006. 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.

Automobile Sector Tariffs

The Motor Vehicle Development Program (MVDP) is intended to rationalize the automotive industry and transform the Philippines into a regional hub for automotive production. To promote local assembly under the program, tariffs on automotive vehicle components have been reduced while imports of finished automobiles and motorcycles have been subject to the highest duty rates applied to nonagricultural products. The importation of used vehicles is prohibited.

Under the tariff schedule that took effect in April 2007, tariffs on high engine displacement vehicles are set at 30 percent until 2010. A 1 percent duty is applied on all Completely Knocked down Kit (CKD) importations by MVDP-registered participants, except for CKD intended for the assembly of alternative fuel vehicles, which are duty free. In addition, tariffs for imported finished automobiles that qualify under the Automotive Export Program, with certification from the Board of Investments, are levied a preferential rate of 10 percent.

Under ASEAN Free Trade Agreement-Common Effective Preferential Tariffs (AFTA-CEPT), tariffs on automobile components are set at 3 percent for CKD and 5 percent for completely built-up units. A subsequent executive order further reduced these preferential rates to zero under the ASEAN Framework Agreement for the Integration of Priority Sectors of the AFTA-CEPT.

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. Under the revised excise tax scheme, vehicles are divided into four brackets based on their price: (1) for vehicles with a manufacturer's/importer's selling price of 600,000 pesos and below, the tax is 2 percent; (2) for those priced over 600,000 pesos 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 pesos 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

In response to concerns raised by the United States and other governments in 2007, the Philippines lengthened the 5 day period afforded to foreign industry to comment on proposed safeguards, granting stakeholders a period of several weeks to present comments. The Philippines has drafted amendments to the Safeguards Measures Act extending the period to file answers by interested parties from 5 days to 30 days, but these changes have not yet been enacted.

Import Licensing

The U.S. Government continues to monitor the operation of the Philippine tariff-rate quota (TRQ) or Minimum Access Volume (MAV) 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. The Philippine Department of Agriculture maintains a VQC import licensing scheme for imported meat and poultry. A VQC is valid for 60 days from the date of issuance, within which time the meat or meat products must be shipped from the country of origin. Each VQC must be surrendered upon arrival of a shipment of a covered product, creating the appearance of discretionary licensing.

On October 14, 2007, the Philippine government announced that it would defer the application and distribution for the 2008 Beginning Year Pool for MAV licenses, including for poultry, while it reviews its current MAV procedures. Philippine meat importers have requested that the Philippine Department of Agriculture continue the issuance of licenses while the review continues so trade remains uninterrupted. As of late 2007, the review had not been concluded.

The Philippine Department of Agriculture Bureau of Plant Industry (BPI) regulates imports of fresh fruits and vegetables, requiring phytosanitary clearances from BPI 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 imports are 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.

Excise Tax on Distilled Spirits and Tobacco Products

In 2004, under Republic Act 9334, the Philippine government raised taxes on alcohol and tobacco products and stipulated further biennial increases until 2011. The law maintains the imposition of significantly lower excise taxes on locally produced spirits made from indigenous raw materials than it does on imports. The U.S. Government continues to urge the Philippines to address this issue.

Quantitative Restrictions

Among sensitive agricultural products, 15 items are subject to a MAV administered through 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 negotiated at the WTO.

In 2004, the Philippine government applied for the extension of Quantitative Restrictions on rice under Annex 5 of the WTO Agreement of Agriculture until 2012. The National Food Authority, a state trading enterprise, controls rice imports and administers the import quota. In 2006, the request for extension of its WTO waiver was approved by WTO members subject to certain concessions. Accordingly, in June 2007, the Philippine government lowered tariff rates on rice and various other agricultural products including mechanically separated or deboned turkey meat from 30 percent to 5 percent and deboned chicken meat from 40 percent to 5 percent. The minimum market access (quota) for rice was increased from 239,000 MT to 350,000 MT for the extension period. Annual rice imports are much higher, usually over a million metric tons, and they are expected to continue growing.

Several other products with significant market potential for the United States are 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; turkey meat, with an in-quota tariff of 30 percent and out-of-quota tariff of 35 percent to 40 percent; pork, with an in-quota rate of 30 percent and out-of-quota rate of 40 percent; and chicken meat, with an equalized in-quota and out-of-quota tariff rate of 40 percent. Moreover, since 2002, the Philippines has imposed a special safeguard on out-of-quota chicken imports, which has effectively doubled the protection rate for chicken meat.

Other Import Restrictions

The Philippines maintains import restrictions on a number of goods, basing the restrictions on grounds of morals, national security, and meeting international treaty obligations regulating certain products. Clearances and permits are required for a range of products, including 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.

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, including implementation of the WTO Agreement on Customs Valuation, but corruption and other irregularities remain commonplace.

The Philippine government has taken steps to eliminate private sector involvement in the valuation process and to clarify 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 the Customs Bureau'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 also 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 and is supporting reform and modernization of the customs regime 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 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. Florida grapefruit and U.S. cherries are permitted, but the United States and the Philippines are still negotiating the import protocols for broccoli, cauliflower, lettuce, carrots, cabbage, and celery. The Agriculture Department's target date for completion of the pest risk analysis for these vegetables is undetermined. 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.

On September 28, 2007, the Philippine government lifted import restrictions on beef and beef products from the United States and Canada. Following the World Organization for Animal Health (OIE) decision in May 2007 recognizing the controlled risk classification status of the United States for Bovine Spongiform Encephalopathy, U.S. beef and beef products derived from cattle of all ages, including bone-in and boneless beef; processed beef; and beef offal (*i.e.*, tongue, tripe, hearts, liver, cheek meat, and collagen casings) may now be exported to the Philippines, provided that the products come from healthy ambulatory animals and are free of specified risk materials.

On December 23, 2006 the Agriculture Department 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 still eligible to export meat and poultry to the Philippines.

GOVERNMENT PROCUREMENT

The Philippines is not a signatory to the WTO Agreement on Government Procurement. However, the Philippine government has taken some steps to reform its procurement process. In January 2003, the Government Procurement Reform Act consolidated procurement laws and issuances and standardized guidelines, procedures, and forms across Philippine government agencies, government-controlled corporations, and local governmental units. The Act simplified prequalification procedures, introduced more objective, nondiscretionary 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 greater transparency of the procurement process to promote competition, enhance the flow of information, and lessen discretion among agencies.

Nevertheless, the Government Procurement Reform Act's Implementing Rules and Regulations for locally funded government projects continue to favor purchases from Philippine and Philippine-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 Philippine-controlled entities. For infrastructure projects, the Law also provides that 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 nonprovince-based bidder, though this provision is set to expire in January 2008.

The Philippine government has not yet issued implementing rules and regulations covering procurement for projects with 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 waived the preference for local suppliers for projects involving ODA. Foreign donors have been able to apply their procurement regulations in accordance with the ODA Act. The build-operate-transfer law allows investors in build-operate-transfer (BOT) projects to engage the services of either Philippine firms or foreign firms for the construction of BOT infrastructure projects.

The Philippines also provides for preferential treatment of Philippine consultants in public sector infrastructure projects. Where foreign funding is indispensable, foreign consultants are required to enter into joint ventures with Philippine partners. U.S. companies also continue to raise concerns about corruption in government procurement.

The Philippine government issued an executive order 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 countertrade 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 (IPP) may register with the Board of Investments (BOI) for fiscal incentives, including 4 year to 6 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 Philippine-owned and, if export-oriented, export at least 50 percent of its production to qualify for BOI incentives. Enterprises with less than 60 percent Philippine 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, the Philippine government launched the Philippine Automotive Export Program (AEP) in 2003 and modified it in 2004. The export incentives program offers automobile manufacturers registered under the AEP preferential tariff rates in the 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 3, declining to $100 by year 5, will be credited. Export performance is required to take advantage of preferential tariff rates. 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.

INTELLECTUAL PROPERTY RIGHTS (IPR)

In February 2006, the United States moved the Philippines from the Special 301 “Priority Watch List” (where it had been listed for 5 consecutive years) to the “Watch List” to acknowledge steps the Philippines has taken to strengthen its IPR regime. Following the announcement, President Arroyo and other senior government officials pledged continued momentum and increased effort on IPR initiatives. However, there has been limited progress since and there are some signs that the IPR climate may be deteriorating. 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. In addition, there are widespread unauthorized transmissions of motion pictures and other programming on cable television systems. The Intellectual Property Office (IPO) and the National Telecommunications Commission have brought criminal charges against cable companies that distribute programming without the consent of copyright holders, but the Department of Justice has experienced difficulties in prosecuting the cases.

While the Philippines has made progress in combating optical media piracy through passage of the 2004 Optical Media Act (OMA), it has generally failed to improve the prosecution and conviction of IPR violators. Print piracy and end-user piracy of business and entertainment software also are serious problems. The United States has urged the Philippines to further improve and sustain enforcement efforts and to take steps to enhance judicial capacity.

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 handed down a decision with respect to *ex parte* seizure authority in civil cases of IPR infringement (seizure without notice to the suspected infringer).

The Philippines is a member of the World Intellectual Property Organization (WIPO) and is party to the following international IP agreements: the Berne Convention for the Protection of Literary and Artistic Works; the Budapest Treaty on the International Recognition of the Deposit of Microorganisms for the Purposes of Patent Procedure; the Paris Convention for the Protection of Industrial Property; the Patent Cooperation Treaty; and Rome Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organizations. Most recently, the Philippines acceded to the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty (known collectively as the WIPO Internet Treaties), which took effect in the Philippines in October 2002. However, the Philippine government has not yet enacted necessary amendments to its Intellectual Property Code that would fully implement the requirements of these two WIPO treaties into domestic law. The U.S. Government continues to urge the Philippines to enact this needed legislation.

As of January 2008, the Philippine Congress is in the process of working on the passage of legislation to amend the Intellectual Property Code with respect to patent registration for pharmaceuticals, placing additional and more burdensome requirements on pharmaceuticals vis-à-vis other products. If passed, this legislation would weaken some patent protection provisions in the Intellectual Property Code related to pharmaceutical products and increase uncertainty in the market for U.S. pharmaceutical companies.

Enforcement

The United States continues to have serious concerns regarding the lack of consistent, effective and sustained IPR enforcement in the Philippines. In 2007, U.S. distributors continued to report high levels of piracy of optical discs 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 merchandise openly available from both legitimate and illegitimate vendors.

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 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. To support Philippine efforts, the U.S. Government continues to provide technical assistance and training to the Philippine agencies responsible for IPR protection.

Serious problems nonetheless continue to hamper the effective operation of agencies tasked with IPR enforcement. Interagency coordination within the Philippine government is generally weak, though improving. 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 three years. The Optical Media Board (OMB), created to enforce the OMA, continues to work towards full operational capability in its efforts to combat domestic production of pirated optical media, despite persistent inadequate funding. The OMB continues to conduct numerous raids against optical media production lines and retail outlets, resulting in increasing seizures of production equipment and finished products. The legal system in the Philippines remains inadequate, however, and courts often release suspects picked up in OMB raids and drop their cases on technical grounds.

The Philippine government has taken some administrative steps intended to strengthen enforcement. The Intellectual Property Code of the Philippines stipulates that the IPO has jurisdiction to resolve disputes concerning alleged infringement. The IPO has implemented a more robust leadership role on enforcement issues in the Philippines, and, in February 2006, was granted oversight authority over IPR-related law enforcement efforts. A November 2006 directive from President Arroyo assigned the IPO the responsibility for coordinating intellectual property protection among executive agencies. 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 and counterfeit products and created an Intellectual Property Unit within the BOC. The BOC maintains an IPR registry where rights holders may record relevant information regarding their products in order to facilitate enforcement. However, the Intellectual Property 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, limited 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. Over the past year, those judges and several of the prosecutors received training from the U.S. Patent and Trademark Office. The Task Force was reorganized in July 2006 and is composed of entirely new personnel. In 2006, 15 judges were identified for specialized IPR training. While these judges handle other commercial and criminal cases such as money laundering, their primary responsibility is IPR cases. Frequent changes in personnel and structure have limited the effectiveness of this mechanism. If appealed, IPR cases continue to go through the current appellate system, which permits numerous interlocutory appeals and can result in long delays. There continue to be proposals to create special courts to deal with IP cases exclusively.

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 for as long as two decades after the initial complaint. The Philippines has failed to establish punitive sanctions sufficient to serve as a deterrent to IPR infringement. The nominal damages awarded by the Philippine courts in IPR cases add little to the cost of doing business for IPR infringers, and thus far there has been no risk of imprisonment for offenders.

SERVICES BARRIERS

Basic Telecommunications

The Philippine Constitution of 1987 limits the operation of certain utilities to firms with at least 60 percent ownership by Philippine citizens and defines telecommunications services as a public utility, thereby limiting foreign ownership to 40 percent. This restricts market entry, particularly 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 of telecommunications companies and the number of foreign directors in telecommunications 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 Philippine nationals.

Financial Services

The Philippines 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

Under the Foreign Bank Liberalization Act of 1994, a maximum of 10 additional foreign banks were permitted to open full service branches in the Philippines within 5 years from the effective date of the Act. All slots have been filled. Without time limit, the Foreign Bank Liberalization Act allowed foreign banks to own up to 60 percent of a new or existing local subsidiary. Foreign branch banks were 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 created a seven-year window (which closed in June 2007) during which foreign banks could acquire up to 100 percent of one locally incorporated commercial or thrift bank (up from the previous 60 percent foreign equity ceiling). Since September 1999, foreign investments have been allowed only in existing banks because of a central bank moratorium on the issuance of new bank licenses to encourage consolidation in the banking system. Current laws mandate that majority Philippine-owned domestic banks should, at all times, control at least 70 percent of total banking system assets. Rural banking remains completely closed to foreigners.

Existing laws require financial institutions to set aside loans for certain preferred sectors. The Agr-Agra Law requires banks to earmark at least 25 percent of their loan portfolios for agricultural credit in general, with at least 10 percent dedicated to agrarian reform program beneficiaries. The Magna Carta for Small Enterprises requires banks to set aside at least 8 percent of their loan portfolios for small and medium-sized enterprises (SMEs). Although these mandatory lending requirements lapsed in August 2007, a pending bill seeks to continue mandatory lending for SMEs. In the interim, the central bank has issued a circular letter encouraging banks to maintain their present level of lending to the SME sector on the request of the Small and Medium Development Council (the lead government agency for SME promotion and development). The mandatory lending provisions are more burdensome for foreign branches because of their limited branch networks and because constitutionally-mandated foreign land ownership restrictions impede their ability to accept land as collateral.

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. A 60 percent foreign ownership ceiling applies to financing companies and a 30 percent cap applies to pawnshops. The Lending Company Regulation Act – signed into law in May 2007 to establish a regulatory framework for credit enterprises that do not clearly fall under the scope of existing laws – requires majority Philippine ownership.

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.

Practice of Professions

As a general rule, the Philippine Constitution reserves the practice of licensed professions (*e.g.,* law, medicine, nursing, accountancy, 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 Philippine 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 manned by Philippine crews.

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.

The Civil Aeronautics Board (CAB) expanded international nonscheduled or chartered services for specific airports based on a 2005 resolution to allow unlimited flight frequencies over and above the existing entitlement provided in bilateral air services agreements. This resolution applies to Diosdado Macapagal International (Clark) 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" (list A and List B), 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 signed in December 2006.

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 Philippine 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 nonexport 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 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 need to be clarified for domestic landowners.

Trade Related Investment Measures

Under a 1987 Executive Order, the soap and detergent (surfactant) 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 Agreement on Trade-Related Investment Measures. Subsequent to the ruling, the order has not been enforced, but it has not been repealed. Moreover, a 2000 law 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 other of the Philippines' trade-related investment measures. 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. A 1982 executive order with guidelines issued by the Bureau of Foods and Drugs, which 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, is currently dormant as the said local company has closed and there is no other local company that manufactures semi-synthetic antibiotics.

Retail Trade

The Retail Trade Liberalization Act of 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 8 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 Philippine 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) was aimed at privatizing at least 70 percent of its generating assets located in Luzon and Visayas within 3 years. Thus far, some 39 percent of generating assets have been sold. By the end of 2007, the Power Sector Assets and Liabilities Management Corporation expects to have privatized 50 percent of these assets. 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 Philippine 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 Republic Act 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 Philippine nationals. 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 exploration permits to only 25 companies as of end July 2007 covering 81,820 hectares 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 ruled in June 2005 that the Bases Conversion Development Act of 1992 did not explicitly provide incentives for the Clark Special Economic Zone, as it did for the Subic Special Economic and Freeport Zone. Unforeseen taxes, including retroactive taxation, threatened the operations of more than 350 investors in Clark, including 10 U.S. firms. In March 2007, President Arroyo signed amendatory legislation restoring incentives for Clark locators and also a law granting a one time tax amnesty to shield Clark investors from having to pay back taxes.

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. However, 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 2000 Electronic Commerce Law 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 has been recognized as 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 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 6 years 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 anticorruption laws has been inconsistent. The Philippine government launched an initiative to strengthen public and private governance, including anticorruption efforts, in cooperation with bilateral and multilateral aid donors in May 2000. The Philippine government has worked in recent years to reinvigorate its anticorruption drive. In November 2004, the Philippines became eligible for the Millennium Challenge Account Threshold Program. In June 2006, the Millennium Challenge Corporation approved a 2 year $21 million grant to implement the Philippines Threshold Country Plan which focuses on strengthening the anticorruption capabilities of the Office of the Ombudsman and tax collection agencies.

Both foreign and domestic investors express concern over the propensity of Philippine courts and regulators to stray beyond matters of legal interpretation into policymaking 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.