EXPORT TRADING COMPANIES AND TRADE ASSOCIATIONS

HEARINGS

BEFORE THE

SUBCOMMITTEE ON INTERNATIONAL FINANCE

OF THE

COMMITTEE ON

BANKING, HOUSING, AND URBAN AFFAIRS

UNITED STATES SENATE

NINETY-SIXTH CONGRESS

FIRST SESSION

ON

S. 864, S. 1499, S. 1663 and S. 1744

TO INCREASE EXPORTS BY ENCOURAGING FORMATION OF EXPORT TRADING COMPANIES AND TRADE ASSOCIATIONS

SEPTEMBER 17 AND 18, 1979

Printed for the use of the
Committee on Banking, Housing, and Urban Affairs

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1—BINDERY SLIP

EXPORT TRADING COMPANIES AND TRADE ASSOCIATION

MONDAY, SEPTEMBER 17, 1979

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON INTERNATIONAL FINANCE,
Washington, D.C.

The subcommittee met at 10:30 a.m., in room 5302, Dirksen Senate Office Building, Senator Adlai E. Stevenson III, (chairman of the subcommittee) presiding.

Present: Senators Stevenson and Heinz.

OPENING STATEMENT OF SENATOR STEVENSON

Senator STEVENSON. The subcommittee will come to order.

This morning we hold hearings on export trading companies and trade associations as a part of our continuing effort to improve the competitiveness of the United States in the world.

There are four bills before the subcommittee, three of which—S. 864, S. 1499 and S. 1744—concern export trade associations, also known as Webb-Pomerene associations. S. 1663 would facilitate the operations of export trading companies. All of the bills recognize that foreign competitors are more effectively organized for export than the United States.

The Commerce Department estimates 20,000 U.S. firms could export profitably but do not. We have no export policy. We have, if anything, an antiexport policy, and the cost of our indifference to exports is growing. The dollar is weak, oil prices high, money seeks refuge from the dollar in such unproductive investments as gold. We suffer high interest rates in a futile attempt to slow the decline thereby causing inflation and recession. Inflation worsens the trade deficit and the wheel takes another turn.

Trading companies and trade associations can spread among many firms the risks and cost of exports. They can absorb exchange rate fluctuations. It may be the only way to significantly expand export participation by smaller U.S. companies which don't have the funds to invest in market development abroad or the time or personnel to master customs documentation, packaging, shipping, warehousing, and all the details associated with exporting. These companies need someone to market their products.

Witnesses appearing this morning and tomorrow afternoon will be expected to address the general subject of expanding U.S. exports as well as commenting on the bills before the subcommittee.

Our first witness this morning is the Under Secretary of Commerce, Mr. Hodges, and we welcome you. This is your first appearance I believe before the subcommittee.

Mr. HODGES. Yes, sir.

Senator STEVENSON. We are delighted to have you and we look forward to hearing your testimony. Your Department has been the one department which has faced up to all of the realities of our eroding position in the newly competitive world marketplace and has been very supportive of our efforts to improve our competitiveness. So we are especially pleased to have you here, sir, today.

[Copies of bills being considered may be found in appendix at p. 353].

STATEMENT OF LUTHER H. HODGES, JR., UNDER SECRETARY, DEPARTMENT OF COMMERCE

Mr. HODGES. Thank you, sir. I appreciate your kind comments and we do agree with you and we want to work very closely with you, and I have prepared a detailed statement which I submit to you.

I am pleased to appear this morning before the International Finance Subcommittee to give my views on S. 864, S. 1499, and S. 1663. In general these bills are pointed toward a common objective: the encouragement of joint exporting by American Industry. S. 864 extensively amends and strengthens the Webb-Pomerene Export Trade Act. S. 1499 would replace the existing Webb-Pomerene Act with an entirely new text, which includes the basic reforms of S. 864. S. 1663 is the most far-reaching of the bills, because it creates an entirely new entity, an export trading company, which would have some similarities to the Japanese trading company. This bill also provides special tax treatment for export trading companies.

SERIOUS TRADE PROBLEMS

It is gratifying to me that you are devoting special attention to legislation whose sole purpose is to assist our export effort. I am convinced our long-term trade problems are serious; finding solutions will require careful attention and cooperation by Government and business, including review of laws and regulations that form the framework for international trade. I believe the subcommittee is contributing an important step to this essential review by holding hearings on these three bills. I will state the Commerce Department views on each of these bills, but my testimony will tend to concentrate on the Webb-Pomerene act and proposed amendments to that act.

At the outset, I should say that we at the Department of Commerce feel that American firms should have the option of exporting either independently—as the large majority now do and will continue to do so—or jointly, within clear limits prescribed by law. We believe that the need to give U.S. companies the tools to compete more effectively in world markets, especially against large combinations of foreign sellers, is just as strong now as it was in 1918 when the Webb-Pomerene Act was passed. The continuing deterioration of this country's trade position underscores the need to improve the ability of our exporters to compete in foreign mar-

kets. Passage of any of these three bills would help get more firms into exporting and reduce the trade deficit.

My remarks will include: (1) a statement of the U.S. foreign trade position, (2) a discussion of our principal trading partners' attitudes toward joint exporting as compared to our own, (3) a brief review of the terms of the Webb-Pomerene Act, and (4) a discussion of the principal features of the bills including: (a) provision for joint export of services in addition to goods, (b) a stronger antitrust exemption for joint exporting, (c) administrative changes, and (d) special tax and loan treatment for export trading companies created by S. 1663. I will also provide answers to specific questions on S. 864 communicated to the Department by members of your staff.

THE U.S. FOREIGN TRADE POSITION

All of us know that U.S. exports have not grown nearly fast enough to keep pace with imports, and that the U.S. trade deficit exceed $30 billion in 1978. Let me now add some recent information and predictions to this finding. Our trade projections indicate short-term improvement in this deficit, about $4 billion for 1979, which would give a 1979 trade deficit of about $25 billion. Last month's improvement in our balance of trade, though surprising in its degree, is in our view, part of this short-term improvement. Our economic forecasts in the longer term, however, indicate that this improvement is unlikely to continue much beyond 1980, so the long-term trade picture is not bright. The major reason for this is the huge increase in oil prices which will greatly increase the total cost of U.S. imports. This rise in the world market price of crude oil will also reduce the rate of economic growth abroad, which tends to reduce the demand for U.S. exports. In addition, we anticipate that a post-1980 resurgence in U.S. economic growth and a falling off of the impact of the 1977-78 dollar depreciation will cause an increase in imports relative to exports. Furthermore, worldwide economic expansion is now forseen to be slower in the 1980's than it has been for the last two decades, so that competition for sales in export markets will probably intensify.

Thus, the outlook is that our trade problems are not going to go away, but will rather be accentuated. Many of these problems, however, are less related to fluctuations in exchange rates and macroeconomic trends than they are to the laws and regulations which form the framework for our export trade and to an increasing extent constrict it. We have noted, for example, that foreign business firms, often with government encouragement, appear better able than U.S. firms to turn to export markets when domestic markets go soft—this ability is more the product of differences in government attitudes and policies toward exports than macroeconomic imperatives. We are now just beginning to address this problem of policies and attitudes rooted in the governmental regulatory process.

POSITION OF OUR TRADING PARTNERS ON JOINT EXPORTING

Governments of other countries are well aware of the benefits of joint exporting, and currently make these benefits available to their companies. Thus, for the sole purpose of increasing their exports, our trading partners allow, and often actively encourage,

their nationals to participate in joint exporting activities that go well beyond anything allowed by the Webb-Pomerene Act. This would continue to be true even if all the amendments to the Webb-Pomerene Act proposed in S. 864 or S. 1449 became law. S. 1663, alone of these bills, would give U.S. exporters an export vehicle comparable to those available to our competitors in foreign markets.

For our businessmen, the benefits of joint exporting, and the greater freedom available to many foreign companies are vividly illustrated when they compete for business in foreign markets. They see that foreign companies are able to combine more easily to bid on large projects, that they can form export associations, and that large Japanese trading companies can sell a variety of products abroad, without the constraint of a very limited antitrust exemption.

In France, export cartels are excluded from the reach of antitrust enforcement and are not required to file notifications or reports. In the United Kingdom, Belgium, Germany, and Japan, export associations must notify the government of their formation. However, they can export thereafter without filing information on their activities, including their volume of exports. Governments of these countries collect export statistics from individual companies but are not authorized to collect statistics or other information from their export cartels.

Mr. Chairman, I might add that in 1974, the OECD Committee on Restrictive Business Practices, in a Report on Export Cartels, recommended that member countries require export cartels to register with the antitrust authorities and that member countries establish procedures by legislation if necessary, to gather enough information about export cartels to insure that their activities fall within the scope of the exemption. The United States was already adhering to those standards when the report was published, and will continue to do so in the future. On the other hand, other OECD countires have done little or nothing to follow these recommendations.

THE WEBB-POMERENE ACT NOW

The Webb-Pomerene Export Trade Act provides a limited exemption from the antitrust laws for associations of U.S. firms engaged solely in export trade. By definition, this export trade is limited exclusively to the export of "goods, wares, and merchandise" from the United States. This provision has consistently been interpreted as precluding export of services and intangible items such as blueprints, franchises, and patents. The act protects domestic competition by requiring that U.S. companies organized in Webb associations refrain from artificially or intentionally enhancing or depressing U.S. domestic prices of commodities of the class exported by the association, or from substantially lessening competition in the United States. The act also prohibits restraints on the export trade of any domestic competitor of the association.

The number of U.S. export trade associations has remained rather stable for the last 10 years, numbering between 25 and 35. The latest Federal Trade Commission count, released last May, is 33 associations. With few exceptions, these associations continue to

export a limited range of products. Basically, they export such commodities as crude sulfur, rice, phosphate chemicals, phosphate rock, soybean oil, wood chips, and various dried food products. There are also associations in motion pictures, pulp and paper, and machine tools. In our view, affording immunity to joint export of services—in addition to goods—is likely to benefit U.S. companies exporting outside this limited range of products. All three of the bills under consideration today would accomplish this basic reform.

The dollar value of U.S. exports assisted by Webb-Pomerene associations has grown slowly over this 10-year period to around $1.7 billion or $1.9 billion per year. But the percentage of U.S. exports assisted by Webb-Pomerene associations declined—and is today probably no more than 1.5 percent—because U.S. exports as a whole have grown faster than Webb association exports.

DISCUSSION OF THE BASIC REFORMS IN THE THREE BILLS

It is here in the area of government laws and regulations affecting marketing, that the Webb-Pomerene Act, appropriately amended, or a similar export vehicle, can make valuable contributions to solving our trade problems. I am convinced that passage of any of these bills would enhance the ability of U.S. exporters to join together and confidently meet competition for foreign markets.

a. Services

In my view, the growth of U.S. service industries in recent years makes it vital that services be included within the statutory coverage of any bill which may be enacted to encourage joint exporting. All three bills, I am pleased to note, recognize this basic fact. The Webb-Pomerene Act now exempts only exports of "goods, wares and merchandise." Its effect has become increasingly restrictive as the actual and potential export of services has grown. Thus, at the very least new legislation needs to take account of this changed situation, by allowing U.S. businessmen to combine to export architectural, engineering, construction, training, insurance, and project or general management services.

Experience of Webb-Pomerene Associations illustrates both the potential for increased exports if joint export of services were authorized, and the frustrations of limiting joint exporting to "goods, wares, and merchandise." So far only one Webb-Pomerene association has been able to exploit this potential for providing the quality and quantity of products demanded by large foreign buyers—something the Japanese trading companies have been so successful at doing. This Webb-Pomerene association is designed to export complete textile mills, not individual pieces of textile machinery, though such equipment may be part of a project. Statistics for this association's exports vary from year to year, because an individual order is so large, and because the number of orders varies a good deal from year to year. Nevertheless, in 1974 this association reported orders amounting to $12 million. Although data on more recent exports are not available, the association continues to export actively.

Had the Webb-Pomerene Act provided antitrust immunity for the export of services, other U.S. companies would have formed

associations to bid on large projects. We do not know how many cases there are, but one example comes readily to mind. Several years ago, the National Constructors Association attempted to form a Webb-Pomerene association from its members to compete against Government-assisted consortiums. However, the plan was dropped when the Department of Justice ruled that technology consisting of know-how, blueprints, drawings, construction plans and the like does not satisfy the statutory exemption requiring the export of only "goods, wares, and merchandise." It is to free joint exporting from such barriers to full use that we support legislation to shelter the export of services.

In this regard, it is appropriate to recount the recent history of the U.S. construction industry in competing for foreign projects. The U.S. construction industry has been losing business to foreign consortia of government-assisted firms. The U.S. heavy construction industry was once the leader in heavy construction projects around the world, but according to a recent study by Reinhardt & Hall, a New York consulting firm, the U.S. share of heavy construction projects in the Middle East has fallen to 10.3 percent of the dollar value of all contracts. European companies in the same period—1975–78—signed 51.3 percent of the work, the Japanese 16.9 percent, and the South Koreans 5.4 percent, or half the U.S. total. This development should be reviewed in terms not only of the lost construction business but the even larger losses in parts, equipment and service fees.

Accordingly, one reasonable and limited step available to help U.S. construction companies compete abroad is to authorize the joint export of goods and services. If services were covered, I believe the construction industry and other industries would respond favorably, given the rising scale of international business activity by the services sector.

Small to moderate-sized firms, which incidentally comprise most of the construction industry, now constitute the bulk of participants in the Webb-Pomerene associations. The companies I refer to typically have sales in the $500,000 to $1 million range, they are not widely known, and they are not listed in the Fortune 500. We expect that companies of this size group would tend to benefit most if the Webb Act were amended by adding services to exempted exports. Small- and medium-sized construction companies, for example, would find an expanded immunity very helpful in bidding on large foreign contracts. I emphasize this point because we believe that the high cost of individual bid preparation has hampered U.S. bidding on large-scale foreign projects. Such costs, when bids are prepared by an individual firm, can occasionally reach several hundred thousand dollars per company.

The Webb-Pomerene Act also gives U.S. exporters advantages in dealing with preferential trade practices and barriers set up by foreign companies and governments. The list of preferential trade practices and barriers is long, including special product standards, labeling requirements, and quotas. In the case of special product standards and labeling, the members of an association can often satisfy special requirements more readily and cheaply than could the individual member companies. If a foreign government sets a quota on the volume or total value of its imports, Webb-Pomerene

associations are in a position to negotiate more effectively for a larger U.S. share of the quota than could its members, if they could not proceed collectively. The Motion Picture Export Association has been particularly successful in negotiating concessions from countries with quotas on imports of motion pictures. Export Trading Companies created by S. 1663 would also confer on members the same advantages as Webb-Pomerene associations in dealing with preferential trade practices, quotas, and other barriers to trade.

I understand that in connection with S. 864 a member of the subcommittee has raised the question of what form of business organization a Webb association should take. In my view, associations should be permitted to be unincorporated or incorporated, according to the desires of the founders. At the present time there are export trade groups which have corporate status under State law and others which operate as unincorporated associations. The distinction has not been significant in terms of their effectiveness.

b. Antitrust exemption

Businessmen have often told us that one of the compelling reasons for not engaging in Webb-Pomerene association activity is the lack of certainty of the antitrust exemption. Although businessmen generally know the Justice Department has prosecuted very few—we know of only one case—Webb-Pomerene associations in the last 25 years, the nature of antitrust litigation is such that if an action is brought—whether by Justice or by a private litigant and regardless of the merits—the defendant may have a big, expensive, and long-term problem. In the last few years the Antitrust Division has investigated the two phosphate export associations, which export phosphatic fertilizers. The first ended without any suit being filed; the second is in progress. The Federal Trade Commission announced recently the investigation of the Motion Picture Export Association, which exports about one-third of all exports of Webb-Pomerene associations. Investigations also cost time and money—less than defending a lawsuit—but considerable amounts nonetheless. These risks and uncertainties are real in the minds of many businessmen and may lead them to drop the idea of forming a Webb-Pomerene association, or to use them in less than a totally effective manner to exploit export markets.

S. 864 recognizes the need to increase the certainty of the antitrust exemption, without completely absolving associations from antitrust restraints. The bill's enumeration of antitrust standards of conduct is I believe a good approach. The standards appear to be a codification of existing law, and to the extent they are, we approve their inclusion in this amendment to the Webb Act. As we interpret existing law, Webb-Pomerene associations are acting legitimately if they comply with conditions (1) through (6) as set out in section 4. The advantage of saying so is that it increases business confidence in the exemption.

Restricting enforcement actions against Webb-Pomerene associations to the Justice Department and the Federal Trade Commission may also contribute substantially to the certainty of the antitrust exemption. This restriction should not in any way hamper appropriate antitrust enforcement, since the Federal enforcement

agencies retain all the considerable powers of investigation and civil and criminal prosecution they now enjoy.

S. 1499 also recognizes the need to increase the certainty of the antitrust exemption, and in some ways goes further than S. 864 in doing so. Thus, S. 1499 gives exclusive jurisdiction to the Federal Trade Commission to investigate and take action against an export association, so that even private actions must wait until the Federal Trade Commission has made its finding, and permits private litigants to recover only compensatory damages, instead of treble damages, against an association.

S. 1663 seeks to improve the certainty of the antitrust exemption by giving the Secretary of Commerce exclusive authority to administer the act, including the making of determinations as to the noncompliance of export trading companies with the law.

Without wishing to express a preference for the language of one or the other of these bills, I strongly support the goal of strengthening the antitrust exemption. Each of these bills I believe would significantly enhance the confidence of businessmen in the certainty of the exemption. In particular, I believe that exempting export associations from not only the Sherman and Clayton Acts, but also all other antitrust laws is a good idea. This could be attained by expanding the definition of "antitrust laws," described in all three of the bills.

c. Administration

On the subject of administering the Webb-Pomerene Act or a newly designed joint export vehicle, I believe that for exporters to benefit fully from new legislation, improvements in administration are essential. There is merit in substituting the Commerce Department for the Federal Trade Commission as the agency charged with the primary responsibility for administering associations of joint exporters. I note that other antitrust exemptions, such as those for agricultural co-ops, and air, ocean, and surface transportation, are administered by agencies concerned with the subject matter of the exemption, not antitrust enforcement agencies. The Commerce Department, which helps promote U.S. foreign trade, would be a logical and appropriate choice for administering legislation affording an antitrust exemption to encourage the benefits of joint exporting.

Thus, without necessarily endorsing specific language of S. 864 and S. 1663, we do favor the approach these bills take, which is to transfer substantially all the administrative functions related to the Webb-Pomerene associations and Export Trading Companies to the Department of Commerce. This would include the collection of information about associations, the approval of applications for registration of new associations, the principal authority for drafting guidelines affecting registration, and the authority to promote use of the act. The transfer of responsibility for enforcement functions is also proposed in S. 1663. In this area, we have concluded that, there is merit to the proposed transfer of part or all of the enforcement functions to the Department, although I should note that this proposal raises cost, resource, staffing, coordination and implementation concerns that need further study.

d. Export trading companies

S. 1663, the most far-reaching and comprehensive of the three bills, includes special provisions regarding tax treatment, loan entitlements, antitrust and ownership. A licensing procedure would be established, to be administered by the Secretary of Commerce. Specific enforcement responsibilities are vested in the Secretary.

S. 1663 is intended to encourage formation of companies that would export on behalf of small- and medium-sized companies who do not possess export know/how or the financial resources necessary to carry on successful export business. The limitations in section 105 of S. 1663, Eligibility for Loans and Guarantees, indicates the large amounts of capital the drafters of S. 1663 believe export trading companies will need: credits and guarantees from government sources are limited to $10 million in a 1-year period, and $25 million during the 5-year period.

In regard to this section, I would like to add that I am concerned that loans offered at less than the prevailing market rate of interest may violate the recent MTN agreements on export subsidies.

The tax provisions are intended to attract investment necessary to create viable export trading companies. These provisions should help make investment in an export trading company profitable enough to attract investment. However, I should note that S. 1663 provides an opportunity to obtain 100 percent deferral for the profits of a qualifying export trading company. This new deferral benefit needs to be analyzed in relation to the antisubsidy code which was concluded in the multilateral trade negotiations. There is also a question as to the need for special tax provisions for export trading companies so long as DISC remains in effect and its benefits are available to such companies.

Trading companies would help to fill a vacuum which now hampers our national export effort. I refer to the lack of export know-how and adequate finance for many of our industries.

In the part of industry with which I am most familiar—textile and apparel—there are literally hundreds of sound companies that could be contributing to our export total. These people do tremendous domestic trade. They have goods for which a large demand exists by foreign buyers. Their prices are right. They are competitive. Their products are manufactured in highly efficient modern factories. But they do not—many of them—sell abroad. When foreign orders are received they are likely to be handled through the very large factoring firms, but these firms have neither the people nor the facilities to make exporters out of the many converters and jobbers whose domestic needs they service.

Here is when trading companies enter the picture. They could provide the needed skill and financial resources to handle the business, if they were given the incentives set forth in S. 1663. The tax incentives and the antitrust protection provided would, I believe, lead to the formation of such trading companies with support from banks, factors, companies now exporting and others knowledgeable in foreign marketing who possess the skills requisite to conducting export business. This would take time, however, because American firms have to develop their own paths to joint export ventures and trade intermediaries. Up to now there has

been little in the way of institutional frameworks and a lot of legal and financial roadblocks.

What is true of textiles and apparel is true of other industries in this country. Here again as in so many aspects of our foreign trade we can learn important lessons from our competitors. Right now in this country Japanese trading companies and British confirming houses are carrying on a thriving business in just this manner, and on their terms. But Japanese trading companies finance their trade through Japanese financial institutions, use Japanese forwarders, Japanese shipping, Japanese insurers.

The U.S. service industries are rightly concerned over foreign restrictions on their international business. What a gain for them and for domestic employment and economic activity if all this business could be handled by U.S. banks, U.S. forwarders, U.S. shipping lines and U.S. marine insurance companies. Both our merchandise trade and our invisible earnings would benefit from this development.

SENATOR INOUYE'S BILL

Mr. Chairman, I have reviewed also Senator Inouye's letter to you of August 31 and the enclosed draft of a bill to amend the Webb-Pomerene Act which he expects to introduce.

Senator Inouye's bill makes the minimal changes necessary to make the Webb Act an effective tool for export promotion. In addition to adding services to the exemption's coverage and strengthening the exemption, it would transfer administration of the act to the Department of Commerce.

Based on my review of the bill, and again speaking only for the Department, it is our opinion that this proposal would go far to eliminate the existing uncertainties surrounding the legal position of export associations and restore business confidence in them. Because Senator Inouye's bill has much in common with S. 864 and S. 1499, I believe that it can fairly easily be reconciled with them. Of course, we would be happy to work with you in adjusting the differences in order to arrive at a mutually satisfactory version.

CONCLUSION

Mr. Chairman, before concluding, I would like to note that these proposals to enhance U.S. exports contain in more than one instance, provisions to prevent foreign-owned or controlled entities from being a member of the export association or trading company. Although we can conceive of possible abuses these provisions are intended to remedy, we question whether they are necessary. In each of the bills, the entity loses its exemption from antitrust liability as to its activities which substantially restrain trade or create unreasonable price consequences in the domestic economy or restrain or unfairly compete with domestic competitors. Given this condition, and in light of the fact that the purpose of the Webb-Pomerene Act is to assist U.S. exports, it is immaterial whether such exports are made by a U.S.-owned or foreign-owned company. Also, if foreign-owned companies are denied access to the benefits proposed in these bills, several existing Webb associations will be obliged to expel foreign-owned members.

To summarize the major points of my testimony:

One: Joint export associations are an important export resource which is largely undeveloped in the United States. Our principal trading partners understand the benefits of joint exporting, and permit or actively encourage their nationals to engage in activities going beyond those allowed by the Webb-Pomerene Act, even if amended by one of the three bills under review.

Two: U.S. trade problems are not going to go away, but will probably be accentuated in the 1980's. A review of U.S. policies and regulations affecting international trade is needed to remove some of the restrictions on exporters. One area needing examination is Government policy as regards joint exporting, and the Webb-Pomerene Act at the very least.

Three: The Webb-Pomerene Act needs to be amended to permit associations to include services among the exempted exports. Other important amendments include making the antitrust exemption more clear and certain, and streamlining of the act's administration.

Four: S. 1663 is the most far-reaching bill introduced in the last several years to authorize joint exporting by U.S. companies, and should receive serious consideration as a potentially very useful means to assist U.S. exports.

Senator STEVENSON. Thank you, sir, for a positive and helpful statement. The amendments to the Webb-Pomerene Act and S. 1663 are compatible. That is to say, they address different problems and in no way are inconsistent with each other. Right?

Mr. HODGES. Yes, sir.

Senator STEVENSON. Now with respect to those amending Webb-Pomerene, which remove a disincentive in the antitrust laws by providing for formation of Webb-Pomerene associations, do you think those amendments, if approved, would significantly increase U.S. exports? The Commerce Department has identified some 20,000 potential exporters. Would those amendments go far toward enabling those potential exporters to become actual exporters? What would the actual effect of these amendments, if approved, be on our trade balance?

IMPACT OF AMENDMENTS

Mr. HODGES. I could probably be more specific in the service area. I think it would definitely have an immediate impact. Frankly, I think one thing that the passing of the legislation along with some other things we are doing would be a signal to American business and the world that in the reorganization of our Government and in amending certain legislation, we are going to be serious about exporting. I think it's an attitudinal problem as much as anything else, getting people to think internationally, but certainly these amendments will facilitate the entire process.

Senator STEVENSON. Now. S. 1663 doesn't just remove the disincentive. It takes a large positive step. I believe it would give U.S. exporters a vehicle comparable to those of their competitors in other countries.

Have you looked into the impact of the trade agreement on S. 1663 and trading companies in the United States?

Mr. HODGES. The impact of the——

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Senator STEVENSON. The MTN legislation.

Mr. HODGES. Not specifically. I will.

Senator STEVENSON. I wrote Ambassador Strauss some months ago during the negotiations to express an interest in the subject and to ask if the codes being negotiated would adversely affect the creation of trading companies and I received from him a positive response. He indicated that it would not prevent us from creating the same vehicles as our competitors.

I'd like to enter that letter and some additional material in the record.

[The following excerpts from an earlier hearing by this subcommittee, titled "Multilateral Trade Negotiations," and held on April 4 and 5, 1979, were ordered inserted into the record:]

* * * * * * *

STATEMENT OF AMBASSADOR ALONZO L. MCDONALD, DEPUTY SPECIAL TRADE REPRESENTATIVE

* * * * * * *

Senator STEVENSON. I wrote Ambassador Strauss concerning a rumor that I heard, which was that certain export subsidies might get grandfathered in foreign countries, but be prohibited for our own, and raised with him illustratively the case of trading companies, not that those are subsidies. But they might be.

He has now written, saying that the codes will not prevent the United States from authorizing the creation of trading companies which hopefully could then compete with the trading companies of other countries including the Japanese.

As I think you know, our subcommittee report recommends that the United States approve the creation of such companies in order to represent competing product lines and small industries as well as large in all parts of the world.

To do that, we must grant trading companies some tax exemptions, for example, deferral of taxes on foreign earned income until it is repatriated. We would like to go beyond that to grant them some special considerations for their startup cost, just to help them get started.

Do you think tax incentives for new trading companies in the United States would be prohibited?

Mr. MCDONALD. I think that they will have to be carefully worked out, Mr. Chairman. But I believe most of the elements that you referred to can be accommodated within the range of the code.

As a matter of fact, in Geneva, we watched carefully the hearings conducted by this subcommittee as well as some of the other interested committees on the Hill, and I think you might be interested in ome of the guidelines we used at the negotiation table in terms of trying to preserve for ourselves as much latitude as we thought would be reasonable.

If I may, sir, I will summarize some of those, because I think they would be of interest.

Senator STEVENSON. Please.

Mr. MCDONALD. Here are some of the things that within the framework of our subsidies code, the way it is negotiated, we can

do. I am not suggesting these are necessarily controlling factors, nor should they necessarily be done.

But what our concern was as negotiators was make sure the choice was ours and we have not preempted by our international commitments from doing what we felt domestically would be in our best interests.

But, for example, in the area of export credits and guarantees, these can be provided and these can certainly be expanded within the framework of the gentlemen's agreement within the OECD. We have nothing that would prohibit that agreement from either changing or increasing.

As a matter of fact, I think we are at complete liberty to determine what would be the appropriate level of export credits to give to our entities and that is one of the elements I know your subcommittee had been concerned with.

Senator STEVENSON. Let me interrupt, if I may, as you go along.

Mr. McDONALD. Please.

Senator STEVENSON. Does that statement refer to CCC credits for agricultural exports as well as exemption for nonagricultural exports?

Mr. McDONALD. Yes, it does, Mr. Chairman. Although, as I indicated, I believe, earlier to the committee, our review of competitive situations indicates within our CCC we may be even closer to providing an appropriate solution than we are on the industrial side, but that is still a question deserving your review.

Senator STEVENSON. But CCC will not be adversely affected?

Mr. McDONALD. That is true.

Senator STEVENSON. Thank you.

Mr. McDONALD. The second I might mention concerns export promotion activities. I think we are free to provide whatever reasonable help we think appropriate, administrative assistance to exporters, information on foreign market, information on bids, translation activities and the other normal support activities that we might think would be appropriate for the launching of new activities or for the encouragement of a broader base of American business to take a first step in to the international area.

I might also say just in passing, this is a bit of a tangent from my direct response to your earlier question, one of the major elements we consider to be important in the whole series of codes deals with a higher level of certainty in terms of what the rules of the game are going to be.

In my earlier private enterprise experiences, one of the difficulties of embarking on an export program was the high risk and uncertainty related to that high risk. It is very hard to calculate. We are hopeful that some of the elements of those risks will be laced into a better framework of certainty that would be useful to us.

A third element in which we can take whatever actions we think are important, and one that is of great concern to you and members of the subcommittee, is in the relaxation of disincentives to exports. We know really of no limits that would be involved there. Those could involve such things as you mentioned in your committee report. We see no restrictions that would bother us domestical-

ly from proceeding in that direction in whichever way the Congress and the decisionmakers determine is appropriate.

Next is deferral of tax on earnings from sales operations based overseas to provide treatment equal to manufacturing operations abroad. Again, there is a differentiation between our and foreign practices. That would be another opportunity open to us if it appeared appropriate, without violating our international obligations.

Next we could refund many of the so-called indirect taxes that might be now existent in our economy or might later be considered.

Senator STEVENSON. Value added?

Mr. MCDONALD. Exactly. One of the statements that, following consultations with members of the Finance Committee and others from the House who were visiting in Geneva that I particularly made at their request was that the United States reserved all its options to look at those without any obligation for compensation later on. Although legally they are permissible in the GATT, we consider they do have a distorting effect on trade. If we chose at some point in time to equalize that situation, whether for trade reasons or for other reasons, we could consider that that would be our just due. So our latitude is wide open on that score.

Further, any generalized incentives, Mr. Chairman, that are not specifically aimed for exports themselves, but really contribute to the dynamism, competitive stature, the strength of our industrial base, would be entirely permitted.

Such things as accelerated depreciation, incentives for new capital investment, tax or other incentives for productivity increases, incentives for research and development, another item touched on in your committee report. Consequently, we think that, again, our latitude is quite wide.

Finally, one should mention liberalized tax treatment for representatives of the U.S. firms resident overseas. One should note just in passing that our treatment in our tax situation of individuals residing abroad is considerably different from that of other countries who tend to tax on the basis of residence rather than on the point of citizenship.

Just as an illustration, our United Kingdom friends, for example, seek opportunities for overseas assignments, even of short duration, because their earnings while on those commercial endeavors are exempt from their domestic high rate.

Consequently, one of the things that I think the Congress is already doing and we could certainly want to make sure, is that we have a reasonable representation of the American economic society in residence abroad. We have suffered some cutbacks in that area within the last few years as your subcommittee is well aware. We hope it has not moved below the danger point. But it is an issue of concern to those predominantly involved in exorting and international business.

The things we cannot do on the other side of the question, as I mentioned in my statement, Mr. Chairman, are to provide direct tax incentives for export efforts.

Senator STEVENSON. That will pick up——

Mr. McDONALD. Those are prohibited. We have made a special exemption, DISC. We felt we would have enough problems without undertaking that struggle.

The adminstration's position is quite clear on DISC. As a result of the negotiation, the United States is free to handle that ourselves. Its status has not been changed at all by the negotiation of the code.

Senator STEVENSON. You say there is a prohibition against these direct tax subsidies, if that is the right word, for the export sector, but not for DISC.

How do you do that? Is DISC just grandfathered in?

Mr. McDONALD. We in special notes to the code reserve the status of the DISC, as it is, by mutual agreement with our negotiating partners.

If we did not have the DISC at this point in time under the normal provisions of the code and had we not in effect grandfathered it, it would be ineligible to be considered under our international agreements.

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Senator STEVENSON. I will enter into the record the letter from Ambassador Strauss to which I referred earlier.

[The document follows:]

OFFICE OF THE SPECIAL REPRESENTATIVE FOR TRADE NEGOTIATIONS,
EXECUTIVE OFFICE OF THE PRESIDENT,
Washington, D.C., April 4, 1979.

Hon. ADLAI E. STEVENSON,
U.S. Senate,
456 Russell Office Building, Washington, D.C.

DEAR SENATOR STEVENSON: I hope I am able to allay your concerns with regard to the subsidy/countervailing duty code we have negotiated in Geneva. The code does not "grandfather" all existing export subsidies employed by our competitors. Quite the reverse—it tightens considerably the rules governing the use of such subsidies. The only grandfathering which has been done is a special rule for our DISC program.

A principal U.S. objective in the MTN—and one that was emphasized by the Congress in the Trade Act of 1974—was the negotiation of an improved international discipline on trade distorting subsidies. We believe we have succeeded in this.

With specific regard to export subsidies, the code concerns a general prohibition of their use in connection with the export of industrial products. However, there are exceptions. Export financing, provided it is consistent with the terms of the OECD Export Credit Arrangement, is *not* prohibited. In other words, our Ex-Im Bank activities are not restricted. Further, I do not see any bar to the formation of U.S. export trading companies, although clearly the specifics of any such proposal should be reviewed in light of the code provisions.

I do not pretend that the Code is perfect. However, it most certainly does *not* bless foreign subsidies while restricting our own. The Code will introduce a better international discipline on subsidized practices of all signaturies. I believe that such

general discipline serves the best interest of the United States and the international trading system.

Sincerely,

ROBERT S. STRAUSS.

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U.S. SENATE,
SUBCOMMITTEE ON INTERNATIONAL FINANCE,
March 8, 1979.

U.S. EXPORT POLICY

INTRODUCTION

Senator Adlai E. Stevenson, chairman of the Subcommittee on International Finance, announced on January 10, 1978, a study of U.S. export policy to be conducted by the subcommittee. The study was prompted by the rapidly mounting trade deficit and evidence that the competitiveness of U.S. industry in international trade and domestic markets was declining. The subcommittee held 11 days of hearings on export policy between February and May and received testimony from witnesses from the executive branch, industry, agriculture, labor and academic and research institutions. This report summarizes the subcommittee's findings and makes recommendations for insuring the competitiveness of U.S. agriculture and industry in world markets.

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CHAPTER 9.—RECOMMENDATIONS

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PROVIDING EFFICIENT INCENTIVES FOR R. & D. INNOVATION AND EXPORTS

Tax incentives should be used to stimulate higher levels of research and development than would otherwise occur in our "maturing" economy, and to encourage producers to make the extra effort required to enter foreign markets. Tax incentives may also be justifiable to enable U.S. producers to match European and Japanese competition in third country markets as long as competing countries continue to provide significant tax incentives to their exporters.

The United States has three tax policies which encourage exports: DISC, deferral on foreign corporate earnings, and section 911 tax relief for certain personal income earned abroad. DISC may not be a particularly efficient incentive but exporters believe DISC is essential to profitable exporting. Removal of DISC without providing a superior tax alternative could lead to a large reduction in U.S. exports. Accordingly, DISC should be retained until another, more efficient tax incentive can be put into effect.

The export benefits of DISC could be expanded in two ways. Smaller companies not directly involved in exporting but supplying parts and components used in exports can set up DISC's to sell to the exporting firms. In this way the benefits can trickle down to

smaller businesses. Use of DISC in this way is permissible at present, but has received little encouragement from the Government. Small firms may be unaware of this opportunity and may also be discouraged by the requirement that DISC's be formally incorporated. The incorporation requirement seems a needless expense for firms to incur.

Second, the money flowing into DISC's could be recycled to finance additional exports if it could be re-lent to other firms or foreign purchasers. The Export-Import Bank could use its resources in parallel with DISC funds to multiply the export punch of the DISC incentive.

DISC violates GATT rules and may come under further pressure as a result of the subsidies code being drafted in the Tokyo round. If DISC is barred, Congress should study alternatives, including a value-added tax with rebates for exports. The VAT system is widely used abroad, is consistent with GATT rules and could be used to fund a portion of social security benefits. VAT is often criticized as being inflationary as well as regressive in impact; however, these effects could be mitigated if VAT were adopted in conjunction with other tax changes. Many foreign countries have adopted VAT systems within the past two decades and their experience should help Congress determine what costs and benefits VAT would entail for the United States.

Another alternative to DISC would be to defer taxation of export sales abroad attributed to an export sales subsidiary. At present the United States attempts to restrict use of such "tax haven" arrangements by requiring such income to be reported as current earnings. The U.S. practice reduces the export incentive effect of the general deferral of taxation on income earned abroad, contrary to the practice of other governments. To be most effective, U.S. policy should encourage the formation and use of export sales subsidiaries by consortia of U.S. firms.

Section 911 of the Internal Revenue Act provides exemption for some forms of personal income and expenses by U.S citizens working abroad. Favorable tax treatment is an important export incentive in the engineering and construction industries, which in turn stimulate additional U.S. goods exports. The effect of section 911 on U.S. exports requires careful examination and the tax incentive should not be reduced prematurely.

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U.S. SENATE,
Washington, D.C., April 11, 1979.

Hon. ROBERT STRAUSS,
Special Representative for Trade Negotiations,
Washington, D.C.

DEAR BOB: Your letter of April 4 is reassuring with respect to the effect of the proposed export subsidies code on the competitive position of the United States. For the sake of further clarification, could you or your staff respond for the record to the following?

1. Would legislation to encourage formation of U.S. export trading companies which provided that trading company profits would be taxed only upon distribution to shareholders be permissible under GATT rules and the proposed subsidies code? An outline of provisions embodying this concept is attached for your review.

2. Would legislation which provided a tax credit to export trading company shareholders for any losses in the initial five years of operations, which would be

recaptured as profits are earned, be permissible under GATT rules and the proposed subsidies code?

3. Would legislation which authorized a Federal government agency to make loans to export trading companies to finance start-up losses during the initial five years of operations be permissible?

4. Would enactment of S. 864, the Export Trade Association Act of 1979, a bill introduced by Senator Danforth and others, and referred to the Banking Committee, raise any difficulties under GATT or the subsidies code?

5. You noted in your letter that export financing consistent with the terms of the OECD Export Credit Arrangement is not prohibited by the subsidies code. Is export financing which is consistent with the OECD Export Credit Arrangement or outside the scope of the Arrangement prohibited?

6. Enclosed please find a copy of a May 1973 report prepared by the Department of Commerce which lists nontariff barriers to trade used by foreign countries. Please annotate the list to indicate with respect to each trade barrier whether the practice will be halted, modified, or left unchanged by the proposed MTN codes.

7. Enclosed please find a copy of part 3 of hearings on Export Policy held last year by the Subcommittee on International Finance, which includes at pages 143 through 201 an analysis of export subsidies offered by six major trading countries. Please indicate with respect to each subsidy whether the proposed subsidies code or other provisions of the MTN package will secure removal or modification of the subsidy.

I want to thank you and Ambassador McDonald for your generous assistance to the Subcommittee in its review of the export implications for the United States of the proposed agreements.

With best wishes,

Sincerely,

ADLAI E. STEVENSON.

THE WHITE HOUSE,
Washington, D.C., June 29, 1979.

Hon. ADLAI E. STEVENSON,
U.S. Senate, Washington, D.C.

DEAR SENATOR STEVENSON: I am pleased to supplement my earlier statements to you and those of my colleagues on the possible impact of the MTN in the promotion of U.S. exports. I cannot presume to answer all the detailed aspects of your questions. To do this, I think it may be useful to arrange a meeting between your staff and Dick Rivers, our general counsel, who was responsible for negotiating the subsidy code.

With respect to the tax treatment of export trading companies envisioned in your letter, a number of subsidy code provisions are relevant. I have enclosed a copy of the code for your reference. First, the subsidy code deals with subsidies, especially export subsidies, granted on products. Any subsidy found to exist, therefore, must be related to the sales or distribution of a product. Second, the code does not undertake to define the concept of a subsidy or export subsidy. Instead it relies on illustrations, an approach that will require study, discussion and case law to supplement. As a start, the annex to the code contains an illustrative list of export subsidies. It is this section that provides guidance on the types of practices that are or could be subject to the code's discipline.

One of the illustrative examples of export subsidies in paragraph (e) of the annex is as follows: "The full or partial exemption, remission, or deferral specifically related to exports, of direct taxes . . . paid or payable by industrial or commercial enterprises." Thus, in your examples, altering the point of taxation (i.e. having company profits taxed upon distribution to shareholders) would not necessarily constitute an export subsidy.

Specific tax exemptions related to exports, however, could be regarded as prohibited subsidies. With respect to tax credit for losses, to the extent that such credits are considered a tax deferral to be recaptured as profits are earned, it may be considered an export subsidy. Nonetheless, a footnote "2" to section (e) states that tax deferrals ". . . need not amount to an export subsidy where, for example, appropriate interest charges are collected." The final answer to whether such a mechanism would be considered an export subsidy would depend on all its specific elements.

As a rule, questions of organizations for export, i.e. through export associations, would not be considered export subsidies under the subsidies code.

The availability of government funds is not necessarily regarded as a subsidy. While there is no specific section of the agreement that addresses your point, section (k) of the annex may be indicative. This section notes that export credits provided by governments at "rates below those which they actually have to pay for

the funds so employed or the payment by them of all or part of the costs incurred by exporters or financial institutions in obtaining credits. . . ." would be regarded as an export subsidy. The critical questions are the terms at which such funds are made available and the relationship of the funds to the exported product.

As section (k) of the annex indicates, if a signatory to the subsidy code is a party to the OECD Export Credit Arrangement, export credits provided ". . . in conformity with those provisions shall not be considered an export subsidy prohibited by this [subsidies] Agreement." If export credits are granted on merchandise that is not subject to the OECD Arrangement, then the general criteria of section (k) applies, in ascertaining whether a subsidy is involved, i.e., whether the credits are provided on terms more favorable than those available in the commercial market.

The various nontariff measures compiled by the Department of Commerce in 1973 provided an invaluable focus for the MTN. I wish I could say that all the NTMs contained in that list have been abolished or modified as a result of the MTN. That would be overstating the case.

In the early stages of the MTN, we considered approaching trading off NTM for NTM on a reciprocal basis, much like is done in the tariff field. Such an approach is filled with difficulties, not only of a political nature, but also from a practical point of view. How can you quantify the value of an NTM concession? What would the United States have given in return? We traditionally regard ourselves as not having many NTMs that affect trade. Thus, when it came to paying for foreign concessions our pockets would be empty.

In order to maximize our negotiating leverage, we approached various NTM fields through general negotiations. As you can see by the Commerce list, we've tackled all of the significant NTM categories. The success of the negotiations depends upon all signatories to the codes undertaking the necessary action to remove or mitigate the trade effects of the NTMs or being prepared to face international confrontation and compromise, including possible compensation or retaliation. The various codes contain new guidelines and principles by which such NTM activity and its trade impact can be gauged. This is admittedly not a perfect solution, but it is a significant step forward from the current state of international rules that permitted the growth of the massive amount of NTMs enumerated in the list. I cannot comment on each of the items in the Commerce list since some entries are general in nature while others refer to practices that may have to be modified.

Finally, country actions to remove or modify the various export subsidy practices contained in the Export Policy hearings will depend on a number of factors, not the least of which is domestic ratification of the agreement. Some measures may clearly correspond to those contained in the annex to the subsidies code, while others may fall in a grey area. Ultimately, as in any international agreement, the country can exercise its sovereign right to maintain a practice that may be in clear violation of the code. But it has to be willing to suffer the international consequences, including the withdrawal of the application of the code's provisions to its exports.

Sincerely yours,

ROBERT S. STRAUSS.

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[Present hearing continues:]

Senator STEVENSON. Since then I have heard some suggestions that the codes might prevent the United States from doing what its foreign competitors do. Existing export subsidies, so-called, are grandfathered; therefore other countries with existing trading companies would be permitted to continue but those without, like the United States, would be prevented.

We are going to have to look into that problem. Could your Department take a look at that question and give us something further for the record?

Mr. HODGES. This is a note that the Treasury Department will probably give some views on that question, but I will definitely look into it.

Senator STEVENSON. Well, if I know the Treasury Department, we're going to have to know more views that its. I have not only talked with Ambassador Strauss, but I very recently had another conversation with someone within that office which negotiated the

codes and I got very recently orally an answer which I suspect would be a little different from the comments we get from the Treasury Department. So I think it would be helpful if you could take a look at that too and maybe there are others we should consult also. So we look forward to a response to that.

Mr. HODGES. We would be happy to look into it.

Senator STEVENSON. Well, I was particularly pleased by the realism of your comments. At least I think it's realistic. It's not as optimistic as some, but there are those who live by economic orthodoxy and sometime preach the old religion—all we have to do is nothing except rely on relative growth rates and the magic of the floating exchange rate system to rectify the trade deficit. I expect at these hearings we will hear again that all we have to do is have higher growth rates abroad and an depreciating dollar to rectify our deficit. I don't mean to suggest that the floating exchange rate system and the devalued dollar won't have some effect, and the depreciation of the dollar is having some effect.

Mr. HODGES. I don't think our products are on the shelf abroad and I think we have to put them there. We have had it so good in this country that we have never faced up to working hard on exporting. We have to, and as I point out, we are a heavily service economy and if we don't export service we have a really serious problem.

Senator STEVENSON. The MTN hailed as it is, would create opportunities for others as well as ourselves.

Mr. HODGES. Starting January 1. That's why we want to get started.

Senator STEVENSON. Well, like I say, I think it's a realistic attitude. In any event, nothing is lost by giving the United States the same tools that its competitors have in a highly competitive marketplace. Senator Heinz.

Senator HEINZ. Thank you, Mr. Chairman, and I'd ask unanimous consent that my opening statement be placed in the record at this point.

Senator STEVENSON. Without objection.

[Statement follows as though read:]

OPENING STATEMENT OF SENATOR HEINZ

Senator HEINZ. Pogo's famous remark, "We have met the enemy and he is us," seems particularly relevant to the situation in which we find ourselves today in the international trading arena. All too frequently we have been our own worst enemy. Where our trading partners have incentives and governmental export promotion programs, we have created impediments and barriers for our most competitive exporters to surmount before they can even begin to compete in the international arena.

Worldwide, we still have the greatest absolute volume of exports, with $143 billion in 1978, but increasingly our trading takes on the pattern of a less developed country, with agricultural raw materials accounting for an ever greater percentage of the volume. Over the past 3 years, while Germany and Japan were running a combined manufactured goods trade surplus of more than $120 billion, the United States slipped into the deficit column in this category. Meanwhile, our bill for imported oil went from $7 billion just 6

years ago to an estimated $60 billion this year. The result has been a trade deficit which totaled $31 billion in 1977, $34 billion last year, and which could reach the same abysmal level in 1979 despite the significant devaluation of the dollar which has taken place in the meantime.

The bills which we have before us today represent serious attempts to address that problem. I must say that I am disappointed that the administration does not have similar proposals to present, or that it has not at the very least taken a position in favor of one or another of these approaches. Export promotion is a problem which calls for ideas and programs now. Without export expansion we doom ourselves to further economic decline. Trade deficits of the sort we have experienced recently severely weaken the dollar, thus beginning the vicious cycle with which we are all too familiar. The price of imports including energy rise, thereby inducing inflation, which in turn leads to economic slowdown and budgetary deficits. The result is the sort of recession we find ourselves in today.

Obviously, we are not going to solve this problem overnight. But every successful program of trade expansion is a step in the right direction. As cosponsor of S. 864, the Trade Association Act of 1979, which revises and updates the so-called Webb-Pomerene Act, I believe it is time for a serious reconsideration of our antitrust attitudes toward export trade associations. Clearly, the Justice Department's thinly veiled hostility toward activities carried out under the Webb-Pomerene Act and export trade associations formed under the act's protective umbrella has inhibited their formation. That hostility has deterred Webb-Pomerene Associations to the point where today they account for an insignificant percentage of total export trade while in the 1930's they accounted for fully 19 percent of that trade. If one compares them to their counterpart Japanese trading companies, which are nurtured and subsidized by the Japanese Government, one begins to appreciate the handicaps which American businesses, particularly small- and medium-sized ones, operate under in the United States.

S. 864, S. 1499, and a bill to be introduced by Senator Inouye, significantly alter the legislative charter for Webb-Pomerene associations. There is no need to go into the details of those bills because I am sure they will be amply discussed during these 2 days of hearings. Suffice it to say that it is clear to me—and it ought to be clear to the administration—that a major revision of the Webb-Pomerene Act is badly needed. The National Construction Association estimates that merely adding services to the list of permissible exports of Webb associations, as these bills do, would increase worldwide U.S. construction receipts by $2 billion. Moreover, there are 30,000 small- and medium-sized businesses not now involved in exporting, many of which might be induced into this area with the right incentives and the promise of a minimum of governmental interference.

I look forward to hearing the witnesses this morning, and it is my particular hope that the distinguished representatives of the administration will be able to explain what amendments, if any, would be necessary to enable the administration to support any, or all, of these bills.

I can't help observing, however, that a hearing like this reminds you of Pogo's famous expression: "We have met the enemy and he is us," because all the problems that we appear to have in trade—which you have tried to set forth—quite candidly would appear to stem from the fact that we simply haven't done anything to remove unnecessary barriers and to assist in creating structures, so that we may as effectively compete as our trading partners do in the international marketplace.

I have one question of a general nature. Is there a particular reason that we have not received—correct me if I'm wrong—a Presidential message or a similar statement of how our policies need to be changed from the administration before this time? Is there a reason that the administration has not addressed Webb-Pomerene, or some of the issues that Senator Stevenson raises in his bill, S. 1663?

INTERNATIONAL EXPORT POLICY

Mr. HODGES. I think the administration is at this point speaking to those questions. The administration has directed its attention to a national export policy, which is not the most dramatic thing in the world, but it's the first time this country ever had one, and we are working in this area through the President's Export Council and, most importantly, trade reorganization, which will be before you soon and about which the President spoke on July 17.

I think the organization of the executive branch to encourage exports in international trade is a necessary first step. So I think the administration is addressing it.

Senator HEINZ. Correct me if I'm wrong, though I read as carefully as I could the administration's statement on export policy I don't recall—but it may be forgetfulness on my part—that calling for amendments to Webb-Pomerene and I don't remember it calling for the establishment of the equivalent of a trading company. Is that right?

Mr. HODGES. I don't think they were part of that at all. I'm just saying these are—I think having a broad policy recognizing the need and reorganizing the Government were first steps. These amendments were very necessary subsequent steps.

Senator HEINZ. Now my question is, Were they omitted because nobody had thought them up at that point or were they omitted because somebody objected to them?

Mr. HODGES. At the present time there is no objection on the part of the administration.

Senator HEINZ. I beg your pardon?

Mr. HODGES. At the present time, there is no objection to that.

Senator HEINZ. And you're not in a position to say whether they were omitted because they were considered insignificant or because nobody thought of them or because the Justice Department said they need time to further study it?

Mr. HODGES. No, sir.

Senator HEINZ. You don't know the answer to that?

Mr. HODGES. No, sir.

Senator HEINZ. One question that has to occur to people is the question of how great the danger is that increased use of Webb-

Pomerene associations will lead to attempts at domestic price fixing rather than their stated purpose of enhancing the U.S. share of international markets. Do you have any fear along those lines?

Mr. HODGES. Not really. I touched on it in my statement and I don't feel that that's a problem.

Senator HEINZ. And you believe there are sufficient safeguards in the S. 864?

Mr. HODGES. Yes.

Senator HEINZ. How important do you believe the preclearance provided for in S. 864 is?

Mr. HODGES. I don't know that I'm exactly familiar with preclearance.

Senator HEINZ. This is the antitrust clearance, where you look at the charter association and decide whether or not it is inherently anticompetitive or might lead to something bad, such as price fixing.

Mr. HODGES. I addressed the antitrust exemption. I'm not certain about——

Senator HEINZ. Would it be helpful if the staff explained the preclearance procedure to Mr. Hodges?

Mr. STEVENSON. Yes.

Mr. RUSSELL. Mr. Secretary, the procedure contained in two of the bills—S. 864 and S. 1499—would involve the submission by the proposed trade association of all the activities they intend to engage in and specifying where they would operate abroad as well as the membership. If the association were certified, any change would have to be submitted to the administering agency which would be either the FTC or the Commerce Department. The result would be to immunize the association from antitrust actions as long as its activities were consistent with its charter.

Senator HEINZ. Thank you.

Mr. HODGES. I understand the term, and I just think as I testified that it is necessary to give businessmen the certainty that is needed.

Senator HEINZ. I suppose I'm driving at the question of whether you foresee any potential problems in getting the Justice Department to accept your judgment on matters relating to antitrust.

Mr. HODGES. Well, I won't——

Senator HEINZ. This is nothing personal on my part you understand.

Mr. HODGES. I know, and I can't say that I don't foresee problems, but I think that we can handle it and it's necessary to be done. Nothing is going to be necessarily easy.

Senator HEINZ. I think all of us here understand the great potential that exists for small- and medium-sized firms to play a much greater role in our export potential. Would you say that S. 864 or S. 1663 would make a major difference in assisting small- and medium-sized firms or will those, on the one hand the Webb-Pomerene amendments and on the other the trading company approach, benefit principally larger firms?

BENEFIT TO SMALL FIRMS

Mr. HODGES. Again, I think it goes to smaller companies, those that can't afford some of the bidding procedures and can't do everything on their own. The construction industry, for example, as I pointed out, where most of the small firms have sales and revenues of $500,000 to $1 million.

Senator HEINZ. That's good news.

Mr. HODGES. I think it helps small business. I think in the service area it's particularly important that we have the amendments. I think that the next big step is the psychological one of getting people to think in terms of exporting and trading companies are a necessary step for small business.

Senator HEINZ. I'd like to turn for my last question to S. 1663, which is Senator Stevenson's bill, which I support very thoroughly in concept, although when I was offered the opportunity to be a cosponsor of it recently I declined; not because I didn't like the general idea, but because the provisions for Federal loans and Federal guarantees gave me pause for thought on two grounds: First, that we seem to be throwing Federal loans and loan guarantees at just about every place we can think to throw them and that bothers me; and second, I was just not convinced that they were absolutely necessary or particularly useful here as allowing these export trading companies to meet their startup costs to begin exporting.

Do you have any strong feeling on that? Do you endorse the need for Federal loans and loan guarantees as provided in S. 1663 or not?

Mr. HODGES. I endorse having the facility available. I don't know that it's necessary. I don't know exactly what will be needed. I understand your concern about the use of guarantees in Government, but——

Senator HEINZ. I didn't understand what you endorsed.

Mr. HODGES. Including the provision of authority to do that. I don't know that it's absolutely critical to foster trading companies around the world to have Federal guarantees.

Senator HEINZ. But you do endorse having the authority?

Mr. HODGES. Having the authority if that is a procedure that is necessary to get them off the ground. I think there's going to be some support that's required to get them off the ground and some incentive to create the provision down the road for them to be free standing in the private sector.

Senator HEINZ. When you say you would like to have them, has the Commerce Department done any study as to the extent which they are actually necessary?

Mr. HODGES. Trading companies or loan guarantees?

Senator HEINZ. Loan guarantees.

Mr. HODGES. I don't think they are absolutely necessary.

Senator STEVENSON. If the Senator would yield——

Senator HEINZ. I would be happy to yield.

Senator STEVENSON. The proposal for financial assistance, the financial concessions to these trading companies was motivated by comments from industry, but also by a study conducted for the Commerce Department in March 1977. That, of course, is before

you came to the Department, Secretary Hodges, but it does conclude, as you indicated might be the case, that these companies are going to need some help with their startup costs and, of course, they do have Government assistance in various forms available in other countries. I would hope it wouldn't be necessary, and as you indicated, if it isn't necessary, it wouldn't be used.

[The study referred to above is reprinted in this hearing at p. 413.]

Mr. HODGES. Right.

Senator HEINZ. Mr. Chairman, that concludes my questioning. Thank you very much.

Senator STEVENSON. Secretary Hodges, you expressed one reservation at least about S. 1663, and that is the restriction on participation by foreign-owned entities. We will take that into consideration. It's a helpful comment.

Leaving that issue aside, let me just make sure I understood something else you said. You said the administration has no objection to S. 1663 or were you referring to the Webb-Pomerene amendments?

Mr. HODGES. I believe I was referring to all the bills, subject, however, to reservations as to the tax and financial provisions of S. 1663 which Secretary Bergsten will deal with in his testimony.

Senator STEVENSON. I'm glad to hear that. It's the most positive statement I've heard from this administration.

Senator HEINZ. Mr. Chairman, I would note with respect to this, if Secretary Bergsten would agree, that we might consider adjourning now and moving on to the floor.

Senator STEVENSON. I would suggest Secretary——

Senator HEINZ. Maybe we should meet with Secretary Bergsten privately and see if he's going to recant any of the previous testimony.

Senator STEVENSON. He is here. We could go into executive session like we do in the Ethics Committee.

I have no further questions. We might have some for the record. Thank you again, Secretary Hodges, and we welcome you again to this subcommittee. We may have further questions.

Senator HEINZ. Thank you, Secretary Hodges.

Mr. HODGES. Thank you.

Senator STEVENSON. Well, we're going to skip over the next witness.

Senator HEINZ. I'm sure he wouldn't totally mind.

Senator STEVENSON. This will not be the first time our next witness has appeared before this subcommittee, nor I suspect will it be the first time he has told this committee what he's about to tell this committee. I don't agree with him frequently, but he is a good man and we welcome the Assistant Secretary of the Treasury for International Affairs, Dr. C. Fred Bergsten. As you know, we would be happy to enter your full statement in the record if you want to summarize it.

STATEMENT OF C. FRED BERGSTEN, ASSISTANT SECRETARY OF THE TREASURY FOR INTERNATIONAL AFFAIRS

Mr. BERGSTEN. Thank you, Mr. Chairman.

Despite the asides, it's always a pleasure to appear before the committee. I think we have the same objectives, although we sometimes may differ in the methods for getting there.

Senator STEVENSON. Frequently.

Mr. BERGSTEN. And I'm glad to continue that discussion and hope we can find some common ground this morning. I will start out by sharing fully the view that you expressed and others expressed this morning of the critical importance of export expansion for the U.S. economy. From the Treasury perspective, I would simply add that, of course, it's critical for strengthening the dollar and is obviously the most constructive way over the long term to pay for oil and other imports and the whole range of the U.S. international activities.

Exports are essential to the overall strength of the U.S. economy. They account for one out of every eight U.S. manufacturing jobs, the production of 1 out of every 3 acres of American farmland and, along with the international activities of American firms, almost $1 out of every $3 of U.S. corporate profits.

Exports have already become one of the fastest growing sectors of the U.S. economy. U.S. manufactured exports expanded at nearly twice the rate of total U.S. production of manufactured goods between 1972 and 1978. Agricultural exports grew even faster—at three times the rate of growth in total U.S. farm production. Without exports, domestic growth would have been seriously constrained.

A healthy and expanding export sector is essential for the long-run stability of our external accounts and thus of the dollar. Exports are the most constructive way to pay for imported oil and other products which the U.S. economy demands and U.S. consumers want.

They provide essential stimulus to improved productivity and they can help reduce prices in the U.S. economy through greater economies of scale in U.S. production.

The recently concluded Multilateral Trade Negotiations offer important new opportunities to expand U.S. exports in the decade ahead. They also offer improved assurances that international trade will be conducted on a fair and equitable basis. We must now insure that American business will take full advantage of these opportunities. Above all, the U.S. community as a whole must be more export oriented.

As is true for most countries, large corporations in the United States account for the major portion of U.S. exports. DISC data demonstrate that 132 firms with assets of $1 billion or more accounted for 70 percent of the net DISC earnings in 1977—or more than 50 percent of total U.S. exports. Exporting is big business and frequently offers larger profits than can be earned at home.

At the same time, considerably more small- and medium-sized firms could be involved in exporting, given the proper encouragement and understanding of foreign opportunities. Initial startup costs, the expense and expertise required to research foreign markets, and the need to service export markets once they are won have unfortunately discouraged many small firms from the export business. Increasing the number of firms which export is an important part of the U.S. export promotion effort.

I therefore welcome this opportunity to comment on the concept of export trading companies, the current export trading associations under the Webb-Pomerene Act, and alternative means for improving U.S. export performance.

At the outset, it should be noted that U.S. exports have done remarkably well over the past 1½ years.

Exports have risen strongly and steadily since the first quarter of 1978. The volume of nonagricultural exports grew at an annual rate of 23 percent during this period, a sharp change from a pattern of no growth at all over the previous 4 years.

Compared with the exports of 18 other developed countries, the U.S. share of world trade volume in 1978 rose to the highest level in 3 years and was higher than in 1971-72. It is clear, given export growth so far in 1979, that we have continued to record further gains in market shares this year.

U.S. earnings on services last year were $15 billion—nearly 24 percent—larger than the year before, increasing our net surplus on services payments and receipts to more than $25 billion.

As a result, our total current account—covering trade in goods and services, and transfers—will experience a much reduced deficit this year—around $5 billion, compared with $14 billion last year. We expect to run a current account surplus in 1980.

The U.S. export situation is thus encouraging. It is by no means desperate. We are doing something right. Our competitive position is improving. However, the need to expand U.S. exports steadily throughout the foreseeable future makes it clear that we cannot relax the effort to do even better.

Steps which the President has already taken will help to encourage further expansion of U.S. exports in the months and years ahead. These include a substantial increase in the Export-Import Bank's direct loan authority, loan guarantees by the Small Business Administration to help small exporters, increased Commerce and State Departments export development programs, work on a computerized information system on international marketing opportunities, a comprehensive study of Federal export disincentives, steps to clarify and reduce the uncertainty of the Foreign Corrupt Practices Act, and new procedures which assure that export consequences are taken fully into account in the administration of export control regulations and that weight is given to foreign availability in considering export controls for foreign policy purposes.

The proposed bills now before this committee—S. 864, S. 1799, and S. 1663—as well as Senator Inouye's bill which has not yet been introduced, offer two general options for further encouraging U.S. exports in the future: (1) The expansion and modification of the Webb-Pomerene Act facilitating the formation of export associations; and (2) New legislation to license and encourage the formation of export trading companies involved in both import and export trade, presumably along the Japanese model.

Both require an analysis of whether the current Webb-Pomerene provisions have been a successful means of export facilitation. Should we build upon the existing Webb-Pomerene base or consider a fresh approach, as in S. 1663, which proposes a whole new concept in U.S. trade law? Are other measures also necessary, or more feasible.

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The idea of adapting the Japanese trading company concept for the U.S. market is a very intriguing one. Adaptation of successful foreign practices to suit Japanese traditions has been one of the key factors behind Japan's dramatic economic growth during the past two decades. Could the United States do the same, as Ezra Vogel in his recent book, "Japan as Number One," suggests we must? Is the Japanese trading company adaptable to U.S. business practices? Or does the United States already have trading companies of its own? Would the stimulation of trading companies as envisaged in S. 1663 offer real gains for the U.S. economy, without imposing too great a cost?

My comments will focus on: (1) The Japanese trading companies and their adaptability to the United States; (2) Current U.S. trading companies; (3) U.S. experience to date with Webb-Pomerene associations; and (4) Specific elements of the legislative proposals before this committee. Finally, I will discuss alternative measures in one of the key areas of U.S. export promotion: Export-Import Bank assistance to U.S. exporters.

THE JAPANESE EXPERIENCE

The Japanese Sogo Shosha are by far the largest and most successful trading companies engaged in international commerce. They are uniquely Japanese, initially designed to provide specialists in dealing with foreigners and the intricacies of foreign commerce with Japan was little more than a closed feudal state.

As part of conglomerates—Zaibatsu—which included banking, manufacturing, transportation, and insurance, they dominated Japan's pre-World War II economy. Although the conglomerates were officially disbaned after World War II, they have formally reassembled as groups. All the Sogo Shosha are now part of such groups of banking, shipping, and manufacturing operations.

The trading companies have performed important services for Japan, in both import and export trade. On the import side, they have ably supplied the vast quantities of imported raw materials demanded by Japan's economy. They have used their bargaining power to get low prices, and have been able to finance long-term supply contracts. Service charges have been modest. They have transported the materials smoothly and efficiently. When necessary, they have been able to put together large projects to open up new sources of supplies.

They have also had success in marketing certain types of Japanese exports. They have been strong in commodities, such as steel and other metal products, textiles and machinery. They are especially good at large projects, such as turnkey plants and major investments. More recently, the Japanese trading companies have been expanding their activities into trade among foreign countries as well as into distribution and retail trade in Japan itself.

They have, however, been weak in other areas, especially in marketing differentiated manufactured goods such as electronics, autos, and cameras. In general they are good at selling in markets with few buyers and poor at selling in mass consumer markets. The big Japanese export successes in such major products as autos

and electronics have been achieved without much help from the trading companies.

The Japanese trading companies have made major contributions to the Japanese economic miracle. It is therefore appealing to try to borrow the idea and apply it to our situation. Unfortunately, I do not believe that can be done.

First, the successes of the trading companies have not been attained without substantial costs. The market power of the top nine firms is staggering. According to the latest data—Japan fiscal year 1975—these nine control 56.4 percent of all Japanese exports and 55.6 percent of total imports; their total sales equal 31 percent of Japan's nominal GNP. Occasionally they have a role in speculative booms and busts. The concurrent buying and selling activities of these conglomerates can cause normally small fluctuations in commodity prices to become magnified overnight. Close relationships with the banking establishment often result in credit discrimination. Extensive vertical integration and horizontal cooperation have produced oligopolistic concentration in many sectors of the Japanese economy.

In the second place, the Japanese trading companies are integrally meshed with related banking, shipping, and production companies. Half of their sales are domestic transactions in Japan—not import-export business. It is not possible to pull out one part of this system, the trading function, and expect it to operate the same way.

Third, the success of the companies is largely due to their exploitation of economies of scale. They can support a huge and expensive commercial intelligence network because they have so much trade in so many products—they are not simply trade associations in one product line. Because of their size, and resultant borrowing power, they can finance trade. Their huge volumes permit small service charges. We should carefully consider whether we want to have firms of equivalent size with the consequent power they would have over our economy or, conversely, whether the whole approach would work in more limited form.

Fourth, these companies have had a century of experience to learn how to do what they do. We cannot hope to achieve the same effectiveness overnight.

Finally, a vital element in their success is a close, symbiotic relationship with government. The companies were originally fostered by the government. Through the Japanese consensus system, the companies can simultanously influence and carry out Japanese Government policy. This structural relationship may be the key element in the success of the Japanese trading firms—and we cannot duplicate that relationship, nor does our business community want to do so.

U.S. TRADING COMPANIES

In contrast to what most people believe, the United States does have its own unique trading companies already. They are not the same as the Japanese model, but they offer many of the same services and operate on a vast international scale in a similar manner. They are the major grain companies, operating out of home offices both in the United States and overseas. Owned by

seven American and European families, these companies now control a major portion of world trade in basic food commodities valued at some $50 billion a year.

Their success mirrors the rapid growth of U.S. grain exports and the dominant U.S. position in world grain trade. They offer global services in market intelligence, sales, shipping, insurance, and finance, similar to the Japanese trading companies. They deal primarily with small farmers or cooperatives in the U.S. market, and governments or major wholesale purchasers overseas.

They are not in the retail consumer business. They sell a basic agricultural commodity, homogeneous in nature, which can be stored and moved rapidly in response to market conditions. They operate in an environment of—and can clearly influence—rapid changes in global grain prices. They are largely privately owned and operated, with no institutional responsibility to public stockholders. They do not operate as trading associations under Webb-Pomerene. Although these firms specialize in the export of grain, they are also diversifying into such areas as chrome processing, scrap metal, chemical products, research installations, intercoastal trade, chickens, bread, frozen dinners, animal food, cattle, nails, salt, meat packing, highway deicing, coal, copra, sugar, tapioca. They are, in a true sense, multinationals with hundreds of overseas subsidiaries and vast trade operations.

Would they work for other U.S. exports? Could they sell and service differentiated, consumer-oriented products, small manufacturers, and similar items? Could services develop similar operations? Would they need a Webb-Pomerene antitrust exemption in order to do so? Would we want the grain companies to spread to other sectors?

I'm not sure. The grain companies may well be unique in their own way, even as the Japanese trading companies are unique to Japan. Similar to the Japanese trading companies, considerable size appears to be a prerequisite for active participation in the global grain market.

We might find that trading companies with a clear license to import or export would concentrate on U.S. raw material exports and imports of manufactured items from other nations. Would this be beneficial to the United States?

Possibly the most we can say is that U.S. business has developed its own models for trade operations based on extensive experience and a minimum of Government involvement. The grain companies have not needed special legislation encouraging the formation of trading companies in order to be successful. They have not needed the benefits of the Webb-Pomerene Act.

U.S. business can be inventive on its own initiative. The U.S. Government's role might best be aimed at removing unnecessary barriers to U.S. export, while meeting foreign competition in the area of export credits, rather than attempting to graft a model of operations in one area onto U.S. trade as a whole.

Neither the Japanese model nor the United States grain company model is likely to be transferrable to United States trade as a whole. The immediate issue is whether something short of that approach, based perhaps on the present Webb-Pomerene Act, would be desirable.

WEBB-POMERENE EXPERIENCE

After an indepth analysis of Webb-Pomerene associations in 1967 "Webb-Pomerene associations: A 50-Year Review," Federal Trade Commission, 1967, the Federal Trade Commission concluded in 1967 that:

> A half century of experience with the Webb-Pomerene Act reveals that associations have not proven to be effective instruments either for the expansion of overall U.S. exports or for the expansion of exports by small firms.

That conclusion is still valid. Exports by Webb-Pomerene associations account for less than 2 percent of U.S. exports. Associations have generally been successful only in two areas: motion picture and television film exports, and exports of standardized raw materials. The film association has worked because, facing screen-time quotas in most countries, it has been able to act as a negotiating agent with foreign governments on such matters as quotas and taxation.

Associations for the export of raw materials have worked when the economics have permitted what economists call successful monopoly activity. For such products, which are produced by only a few U.S. companies, demand is relatively insensitive to price. In these circumstances, common action—especially common pricing—can be beneficial to the firms. Thus, successful Webb-Pomerene associations have been exporters of such products as sulfur, phosphates, and carbon black, products that had the required characteristics.

Webb-Pomerene associations have not worked to promote exports by small producers of differentiated products. Because those producers' marketing success depends so heavily on distinguishing their products in small ways from the products of their competitors, cooperative behavior is generally not attractive to them. Their exemption from antitrust laws does not remove the underlying sense of competition that exists between them and thus is of limited significance in promoting joint export efforts.

In short, the Webb-Pomerene exemption from our antitrust laws has not been an effective export assist because the exemption has been useful only in very limited circumstances.

My conclusion from a review of Webb-Pomerene experience, Japanese trading companies, and the present grain traders is that changing U.S. law to promote trading companies is likely to provide only modest benefits. The antitrust exemption of Webb-Pomerene has been of limited utility to our exporters. Changes in U.S. law are unlikely to result in the development of U.S. trading companies to equal the Sogo Shosha. These are uniquely Japanese. And there already are U.S. trading companies where they make economic sense—trading standardized products in large shipments.

COMMENTS ON THE LEGISLATION

Mr. Hodges of Commerce has already testified on the Webb-Pomerene Act, and indicated support for liberalization of it. I will therefore limit my comments to the provisions of S. 1663 relating to the proposed role of Eximbank financing, tax exemptions, the

prohibition against foreign ownership, and bank purchase of corporate stock.

(1) Eximbank financing

Eximbank loans or financial guarantees to an export trading company, as contemplated in section 105 of S. 1663, is an interesting idea. However, we believe that it would be more efficient to use funding from other Government sources, primarily the Small Business Administration or the Economic Development Administration, for these purposes. They are much better equipped than Eximbank to evaluate the capital needs of small firms.

Eximbank has for many years resisted efforts to have it finance working capital needs. Such financing is generally available from private sources. Authorizing or requiring the Bank to provide working capital for trading companies would open the door to demands for it to finance the domestic needs of other groups. The fundamental purpose of the Bank—to assist in the financing of exports for which private funds are unavailable or inadequate—could be jeopardized.

We support the use of Small Business Administration and Economic Development Administration funds as proposed in S. 1663. Indeed, the Small Business Administration has already been directed by the President to channel up to $100 million of its current authorization for loan guarantees to small exporters as seed money for their entry into foreign markets.

(2) Tax exemptions

Treasury opposes provisions for special tax treatment of export trading companies, including the exemption of export trading companies from Federal income taxes. Under S. 1663, income earned in the United States or from providing services which facilitate such exports would be exempt from taxation. Thus, export income would be treated much more favorably than under the existing DISC provisions, which provide for a deferral, but not exemption, of income tax liability.

As Treasury's annual reports on the DISC have demonstrated, DISC is an inefficient export subsidy. Similarly, exempting export income from taxation may be more effective in rewarding export sales that would have been made without the subsidy than in stimulating increased exports.

It is also likely that this exemption would be inconsistent with commitments the United States has made as a signatory to the MTN Code on Subsidies and Countervailing Measures. Among the export subsidies prohibited in the annex to the agreement is the exemption of direct taxes specifically related to exports. The agreement, however, does not affect the status of DISC. Since the agreement, generally speaking, does not apply to services, the exemption for ancillary export services income may not be a violation, but the exemption for income from the export of goods probably is. In view of the U.S. energetic support for multilateral action to limit the use of export subsidies, any legislation which seems contrary to the subsidies agreement may be unwise.

Since an export trading company would have no U.S. income tax liability, S. 1663 also provides that the company's investment and

foreign tax credit may be claimed by its shareholders. We view these flow-through provisions as undesirable tax policy since they would extend the benefit of corporate tax exemption to the shareholder level.

Section 201 also would exempt an export trading company from the arm's-length pricing requirements of section 482 of the Internal Revenue Code in its dealings with a foreign subsidiary. This would permit an export trading company to artificially shift profits to a subsidiary. Although the export trading company would be exempt from U.S. income taxes, this might be done to generate additional foreign source income to absorb any excess foreign tax credits on highly taxed foreign income.

As a general principle, we believe it is undesirable to adopt tax provisions which encourage artificial transfer pricing. In addition, like the exemption from income tax, this also probably would be a violation of the Subsidies and Counterveiling Measures Agreement.

(3) Foreign ownership

S. 1663 provides that an export trading company may not be foreign owned. Such a prohibition runs counter to traditional U.S. policy of neither discouraging nor encouraging foreign investment in the United States, with certain stated exceptions—broadcast networks, telecommunications, shipping, et cetera. This denial of domestic tax benefits to foreign persons would also violate the nondiscrimination provisions in our double taxation conventions with other countries. Finally, foreign-owned export trading companies licensed through the mechanism proposed in the bill would be subject to U.S. law in any case, and ownership restrictions would therefore not be necessary.

(4) Bank participation

There is another provision in S. 1663 which we question. It is section 105(c) which would permit banks, bank holding companies and Edge Act corporations to purchase shares in export trading companies. It is a long established principle in this country that banks should not be owners of commercial organizations. Giving banks an equity interest in the success of a commercial venture could bias their lending, trust, and other activities, and could require substantial policing to insure that such financial relationships are based solely on sound and equitable business considerations.

This basic tenet of American law, that banking and banking related activities should be separate from other business practices, demonstrates the difficulty of transferring to the United States the Japanese model, where bank-firm relationships are an integral part of the entire business and commercial structure. Moreover, the Japanese experience with some banks exposed to difficulties from equity investments in troubled commercial groups may illustrate the wisdom of the American principle of separating banking and commerce.

OTHER EXPORT PROMOTION MEASURES

Mr. Chairman, you also asked us to address alternative measures to increase U.S. exports. One possibility is more extensive use of Eximbank funds for these purposes. I would like to comment on this essential area of our overall export policy.

As the chairman and members of this committee are well aware, the administration has sought an expanded direct loan and financial guarantee program for the Export-Import Bank of the United States. The direct loan and financial guarantee program is where Eximbank packs its punch, and makes up three-quarters of the Bank's portfolio. We are convinced that a more vigorous and aggressive Eximbank is necessary to meet foreign official credit competition. We also believe that it can effectively serve as a catalyst for new U.S. exporters.

1. Competitiveness

What countries were willing to do in reducing export subsidies in the context of the GATT, they have been unwilling to do in the context of official trade finance. As the President reported to the Congress on March 16: "Our strong efforts to convince the 22 participants in the International Arrangement on Export Credits to reduce the wasteful subsidy elements in trade finance were not successful." Therefore, he reluctantly concluded that further negotiations would not be productive at this time and said, "We should modify some of our own programs and policies until such time as there is more willingness among our trading partners to impose the needed self-discipline in export credit practices." Accordingly, the Export-Import Bank, operating within the framework of the International Arrangement on Export Credits, has been much more aggressive in providing export financing in support of U.S. exports.

The Bank has increased the percentage of cover from around 40 percent of export value to over 60 percent in fiscal year 1979. It has held its interest rates—which are considerably higher than the arrangement minimums—while dollar interest rates in the private market and the cost of money to the Bank have continued to rise. Because of its ample reserves—$3 billion—the Bank is able to do this and remain financially self-sufficient.

In support of U.S. aircraft manufacturers, the Bank has met the generous financing offers made by the Governments of Germany and France in support of the airbus. During the past year, these Governments have typically offered 10-year loans covering 85 percent of the value of the aircraft and charged only 7½- to 8-percent interest—in dollars or dollar equivalent—the most liberal allowable under the arrangement. It has been costly to match this: Nearly half of the Bank's fiscal year 1979 budget has been for aircraft. We should continue to stand behind U.S. aircraft manufacturers when faced with Government supported financial competition. However, airlines of the world do not generally need such concessionary financing. We would be delighted if these countries would establish a common line more consistent with private market rates.

On a selective basis, Eximbank has also met mixed credits offered by France and the United Kingdom. This practice is not only nettlesome, but has the effect of closing out U.S. exports. In Cyprus we matched a British mixed credit and won the contract. In Tunisia—a market long closed to many United States firms because they cannot match the terms of the French Government's mixed credit line—Eximbank recently approved a $100 million mixed credit at terms matching the French. As with aircraft financing, we are putting our money where our mouth has been.

During past periods of U.S. trade surpluses, the Government largely ignored these nettlesome and wasteful practices. We will do so no more. If the Europeans and Japanese are unwilling to listen to reason, we have no choice but to match them when and where we see fit.

2. Catalyst

By providing programs of ready financial assistance, Eximbank can serve as an important catalyst in making a broader range of the U.S. business community more interested in exploring the export market. The Bank cannot and should not become an export subsidy program, but it can provide the stimulus to increase American business interest in exporting.

It is precisely in this area of developing markets for U.S. exporters where Eximbank can be most helpful. Eximbank has been effective in providing support for exporters who are competitive in pricing and quality with foreign manufacturers with the result that a large percentage of its loans result in exports which would not have otherwise taken place.

CONCLUSION

Exports have clearly become an essential component of the U.S. economy and a vital means of paying for the foreign goods we both need and want. A strong and growing export sector can be achieved, given the right economic environment. No single policy can promise results overnight, but a determined, cooperative effort on the part of both the Federal Government and the U.S. business community can make a real difference in our competitive position both at home and abroad. We have already taken a number of steps in the right direction. Our recent export growth has demonstrated that the United States is, indeed, actively in the ballgame.

We at Treasury are prepared to work closely with other agencies, Members of Congress and U.S. business to assure that we stay in there—and win an increasing share in the years ahead.

Senator STEVENSON. Thank you, sir. You suggested that I was trying to emulate the Japanese experience. There are others I'd like to enter into the record a partial list of non-Japanese trading companies.

[The following table is reprinted from "The 'Sogo Shasha': Japan's Multinational Trading Companies," by Alexander K. Young, Westview Press, Boulder, Colo., 1979:]

TABLE 1.5—LARGE NON-JAPANESE TRADING COMPANIES (WHOLESALE AND TRADE), 1976

Company and country	Sales [in millions]	Earnings per share (dollars)
Kesco, Finland	$1,718	0.32
Beijerinvest, Sweden	1,555	2.18
KF (Kooperativa, Förbundet), Sweden	2,950	(2)
C. F. Bally, Switzerland	287	95.85
Acklands, Canada	270	1.17
Provigo, Canada	502	1.18
H. Russel, Canada	287	0.90
Wajax, Canada	96	2.50
Westburn International, Canada	864	2.27
Jardine, Matheson, Hong Kong	[1]584	0.31
Bousteadco, Singapore	32	0.80
Inchcape, Singapore	250	0.04

[1] 1975 figure.
[2] Not available.

Source: Business Week, July 25, 1977, pp. 81–98

Senator STEVENSON. The largest on this list is a Swedish firm with sales in 1976 of about $3 billion. What I am really trying to do is to learn from the experience of many countries, to give the United States the same tools with which to compete as others have given their own industries. I recognize that the Japanese experience rooted in an alien culture is not, in many respects, appropriate for our own.

Now, to try to piece together. Some of the comments you made about tax exemption, I haven't had a chance to reread this bill since its been printed, but it was intended to provide tax deferrals as opposed to exemptions. And since being printed, I've been told that it can be changed in certain particulars so as to overcome the prohibitions in the codes and permit us to give our own export companies substantially the same so-called subsidies as their competitors have abroad.

These changes will involve not only the use of deferral but also apparently a very different treatment of taxes on services, as opposed to sales. Now, I noted the changes along those lines. I'm sorry I can't explain them very well, but would you still object—and incidentally, I think before this hearing is over, we'll be able to get a far more precise explanation of what is needed to overcome the problems in the code—assuming those problems can be overcome, would the Treasury still object to the tax exemptions?

Mr. BERGSTEN. Mr. Chairman, we would look at them again and we would take a fresh look. When the President announced our overall export promotion effort a year ago, he did indicate clearly that we did want to try to work with the Congress to find, if we could, effective tax devices to support U.S. exports. We did take the position that the DISC system was inefficient, but at the same time we were quite prepared to work with the Congress to look for alternatives.

The intent of the Congress, as we've heard it so far through legislation and other efforts, is to retain the DISC and not be too active in looking for alternatives. But if you wish to do so in this context, we will take a look at any alternatives or revisions of what

has been presented here, to see if it would meet the tests that we have in mind, the cost effectiveness test and the test of conformity with the new subsidy codes.

So we're certainly open to looking at alternative suggestions or provisions that you might have in mind.

DISC IS INEFFICIENT

Senator STEVENSON. That's an interesting idea. I haven't thought of this as an alternative, but I do agree that DISC is inefficient. One of the ironies of the MTN trade agreements is that they prohibit subsidies but the grandfather clauses tend to perpetuate the DISC for the United States and much more effective subsidies, including trading companies, for other countries.

I don't know about the Congress. I sense a large amount of interest in trading companies. There has never been a whole lot of enthusiasm for DISC's. Whether it is realistic to consider one an alternative over the other, I don't know, but I certainly would explore that possibility with you and with other witnesses, if that's the only way to get trading companies. I think it's worth exploring.

Now, you mentioned SBA and EDA. I didn't quite understand what you were saying. Are you suggesting that these would be more appropriate than the loans and loan guarantee as means of providing financing for trading companies? Or for the support of small to intermediate companies?

Mr. BERGSTEN. Well, I think we could go along with either way, Mr. Chairman. The main point I was trying to make was that we feel EDA and SBA would be the more effective agencies to help the small- and medium-sized firms develop a production base for export purposes. The bill called for Eximbank loans or guarantees to these firms for that purpose. We see the division of labor more efficiently as SBA and EDA working with the firms in their domestic production, and then Exim coming into the act, as it now can, and perhaps should do so more on financing and guaranteeing the exports themselves. It's simply a kind of comparative advantage situation as between agencies.

Senator STEVENSON. Well, that's what I was afraid of. The only problem with your approach is that it doesn't work. We've been working on it over at Exim ever since I've been in this position. It goes back about 8 years. Something more has to be done that involves marketing abroad and financing at home, beyond Exim's resources, to get the smaller companies actively involved.

But, if I hear you, you'd be willing to consider working out something to bring in SBA and EDA, and in either case bring them into the financing of trading companies—assuming other problems can be solved.

Mr. BERGSTEN. Right.

Senator STEVENSON. As a possible alternative to the loan guarantees and loans that we provide, that, too, is worth looking into.

Now, you made a couple of references to our export policy and I did, too. But I defined your export policy; you didn't. I defined it as do nothing except rely on relative growth rates and floating exchange rates to rectify the trade deficits. Was my description of your export policy accurate? If not, how is it inaccurate?

Mr. BERGSTEN. Right. I would respectfully disagree with your characterization, Mr. Chairman, on two counts. The first is to say that I think it is legitimate to count as part of our export policy those macroeconomic things that you seem to dismiss. Whatever we could do through the kind of changes proposed in this legislation, or many other proposals that have been made in terms of direct Government support for U.S. exporters, we know that the most crucial determinants of U.S. exports really are the growth rates in our markets abroad, whether our pricing is competitive—which means both our anti-inflation policy at home and the equilibrium exchange rate of the dollar.

I think it's legitimate to count those as part of an export program. And what I was suggesting, and what I think the data for the last 18 months show, is that there's been some noteworthy success, in part as a result of those components of export effort.

The second place where I would respectfully disagree is to say that even in the area that I think you're defining as export policy, direct Government help for exporters, I believe we have not been sitting idle and doing nothing. I focused primarily on the Export-Import Bank. We have brought about a fivefold expansion of its activities within 2 years, and major qualitative changes in its program. I enumerate those in my statement, including meeting mixed credits by other countries increasing the percentage of cover, and meeting airbus competition head-to-head. So in both qualitative and quantitative senses, we have used the Export-Import Bank as a direct tool of U.S. Government support for exporters to help exploit the opportunity that we, in turn, helped put in place by promoting faster growth rates in our major markets, by permitting an equilibrium exchange rate for the dollar, and by concluding the MTN, which reduces foreign barriers to our exports and puts some limits on the export subsidy activities of other governments. In short, I would submit that whereas we haven't done everything we could, we have got a fairly extensive, fairly comprehensive, fairly wide ranging export policy.

EXPORT POLICY

Senator STEVENSON. I would agree with one thing that you said, which is that that phrase, "export policy," should include a large macroeconomic position. I guess I would have to agree to one other suggestion, and that is that strong efforts abroad and price competitiveness are essential. But I think that that strong reliance on relative growth rates—that is to say, higher and stronger growth rates abroad—and floating exchange rates implies slow growth at home and a weak dollar. And that, I suggest, for the long term, is a prescription for inflation, for recession, for endless cycles of inflation and unemployment—owing a large part to our noncompetitiveness because of our failure to face up to all of the complex factors that are at work in the 20th century.

So, I would go beyond macroeconomics and focus on a lot of structural changes that I believe are needed in the world and its institutions and in our own domestic economy. Today we consider just two such changes. The administration may have wide-ranging

policies, I feel that their structural response is very weak. I sense more of that weakness here today.

Would you agree with what Secretary Hodges said, in his relatively positive statement, that the administration has no objection to S. 1663?

Mr. BERGSTEN. No, I would not agree with that, Mr. Chairman, and I gave some reasons why we would not support certain phases of the bill. And I will rest with that.

Senator HEINZ. Mr. Chairman, may I ask a question?

Senator STEVENSON. Senator Heinz.

Senator HEINZ. I thank the chairman. I have to leave to attend a 12 o'clock meeting.

You mentioned the Export-Import Bank, and I believe you said that in addition to the 4.1 billion requested in fiscal 1980, more might well be needed. Senator Stevenson, Senators Garn, Danforth, and myself and others on the Senate Appropriations Committee, are recommending a 50-percent increase for Exim, specifically to $6 billion. I understand from this letter from Mr. Moore, he's saying he could really use $8 billion for fiscal 1980.

Do you think that we could move a little more quickly in getting the administration to endorse an increase in funding for the Eximbank?

Mr. BERGSTEN. This is a topic that we have under active consideration right now, and I would expect we will come to some early judgments on it.

Senator HEINZ. How early?

Mr. BERGSTEN. It's literally under active discussion. We'll be having more discussions with John Moore as soon as he gets back from his current African trip, which is a week away, and we hope we can come up with recommendations on that shortly.

Senator HEINZ. I would only note, Mr. Chairman, that Secretary Bergsten did hold discussions with our trading partners over the issue of predatory financing, which failed to achieve agreement, and that means that they're going to keep being predators. We'd best move as quickly as possible if we intend to even send them any message to allow our companies to compete.

One last question. On page 16 of your testimony, I note with some glee the following quote: "It is a long-established principle in this country that banks should not be owners of commercial organizations."

FOREIGN ACQUISITIONS OF U.S. BANKS

As you may know, I have introduced Senate Joint Resolution 92, which calls for a 6-month study of and moratorium on foreign acquisitions of U.S. banks. One of the things that troubled me was the fact that foreign banks can retain nonbank enterprises in their own countries and abroad. I take it, then, that it bothers you as well, that foreign banks are able to come in here and do these things. Would that be accurate? You recognize, of course, that I am stopping short of construing it as an outright endorsement of Senate Joint Resolution 92.

Mr. BERGSTEN. That's accurate for you to do that.

The reading is in the eye of the reader. The factor you mention is certainly one of the factors that we're looking at very carefully

in trying to come to a judgment about the whole issue of foreign investment in U.S. banks.

Deputy Secretary Bob Carswell did testify on this, as you well know, about a month ago, and indicated that we have a number of factors under consideration. Looking at it on the basis of the evidence we have seen so far, we do not view the increased foreign investment in U.S. banks as a problem which would lead us to change existing laws or regulatory requirements. But we do have it under close continuing review.

Senator HEINZ. I am obviously aware of that. But I guess my question is relevant to this legislation. Does it not trouble you, in a sense, you're establishing a double standard, a standard that says we don't want American banks to be owners of commercial organizations or to participate in them, or to hold an equity interest. But on the other hand, we don't have any strong feelings about foreign banks coming here and buying either American banks and/or commercial companies. That seems to be a double standard and one that's scarcely fair to U.S.-owned interests.

Mr. BERGSTEN. As you well know, there are many, many areas in this whole range of international economic and financial relationships where asymmetries of that type do exist. They do bother me. I think the more we can work toward international harmonization in all these areas, the better off we're going to be.

But, as you know, too, there are some offsetting factors in the bank area that argue the other way. So, as in most cases where the laws, practices, regulations of different countries are different, as they are in many areas, one has to make some net judgments as to where to come out.

Senator HEINZ. Thank you, Mr. Chairman.

Thank you, Mr. Bergsten.

Senator STEVENSON. A point of information. I am told that the appropriations subcommittee in the Senate will meet Thursday of this week to mark up the Exim authority. They may not wait for John Moore to get back. What's more, I have had some conversations with the White House which indicate that they're sympathetic to a large increase, apparently owing to the strong possibility of eligibility for the PRC. So, it might be helpful if some of this be done by the administration sooner than you indicate.

Thank you, sir. We appreciate your help—some of it, the helpful part, at any rate.

Mr. BERGSTEN. Thank you, Mr. Chairman.

Senator STEVENSON. Our next witnesses will comprise a panel. They are: Neil J. Boyer, international attorney and consultant, and Raymond J. Waldmann, attorney, representing the Chamber of Commerce of the United States; Dr. Frederick W. Huszagh, of the Dean Rusk Center at the University of Georgia; John F. McDermid, general counsel of the National Association of Manufacturers.

Gentlemen, I will invite you to proceed in that order and to summarize your statements, in which case the full statements will be entered into the record.

Mr. Boyer.

STATEMENTS OF NEIL J. BOYER, INTERNATIONAL ATTORNEY CONSULTANT; RAYMOND J. WALDMANN, ATTORNEY, REPRESENTING THE CHAMBER OF COMMERCE OF THE UNITED STATES; FREDERICK W. HUSZAGH, DEAN RUSK CENTER, UNIVERSITY OF GEORGIA; AND JOHN F. McDERMID, ASSISTANT GENERAL COUNSEL, NATIONAL ASSOCIATION OF MANUFACTURERS

Mr. BOYER. Thank you, Mr. Chairman. I am Neil J. Boyer, an attorney and consultant on international trade law and finance, and a member of the export policy task force of the Chamber of Commerce of the United States. I am also chairman of that task force's subgroup on antitrust, that was established recently to develop the chamber's position on the impact of U.S. antitrust laws on our international trade performance.

Also appearing with me is Raymond J. Waldmann, an attorney with the firm of Schiff, Hardin & Waite, in Washington, D.C. Mr. Waldmann is a member of the chamber's international service industry committee and chairman of its subcommittee on antitrust matters. He will discuss the legislation before this subcommittee as it relates specifically to the service effort.

With us also is Howard Weisberg, director of international trade policy for the U.S. Chamber.

I am here to express the chamber's support for recent legislative initiatives to encourage small- and medium-sized businesses to enter the international trade arena. Both of the Webb-Pomerene amendments introduced in the Senate, S. 864 and S. 1499, go a long way toward making this act a more useful export promotion vehicle.

AMENDMENT NECESSARY

It is necessary to amend the Webb-Pomerene Act to encourage all businessmen, and small businessmen in particular, to increase their exports through cooperative ventures. Senate bills S. 864 and S. 1499 and Senator Inouye's new bill appear to be designed to do this by removing ambiguous or confusing language and substituting the tests of reasonable restraint on trade and substantial impact on competition in conformity with current antitrust standards.

As it now stands, Webb-Pomerene raises more issues than it solves. The unclear language creates risks that businessmen would prefer not to assume. Small businessmen, particularly, cannot afford the cost of experts to interpret the unclear law, nor can they afford the time to organize such seemingly speculative ventures. Where the business risk of dealing abroad is already high, they will not risk more in a venture where they may be subject to prosecution for unpredictable violations of the law.

Past strong antitrust enforcement has conditioned businessmen to avoid antitrust situations at all costs. This negative atmosphere may be desirable in the United States, but it is a substantial deterrent to increasing foreign trade through cooperative ventures.

The proposed amendments would improve the act's language and thus lessen the uncertainty of businessmen toward cooperative export ventures and provide a more positive psychology toward exporting among smaller businesses.

S. 864 appears to go a step further to create a positive atmosphere. It shifts the administration of the act—favorably, in our view—to the Commerce Department, which is responsible for increasing exports. It would also permit entry by important service industries. These amendments also appear to incorporate adequate antitrust safeguards. They provide for coordination among agencies before taking action against export associations. This gives a prior chance for agreement by the agencies on policy objectives—that is, whether it is more important to export or to enforce antitrust laws in a particular case. Also, the amendments restrict nonpolicy parties from interfering in the process by limiting actions to Government agencies.

Prior arguments against Webb-Pomerene exemptions are based on inconclusive evidence or cannot be substantiated as to their potential harmful effects on U.S. commerce. It can be conceded that Webb-Pomerene associations have not increased exports substantially in the past, but there is no showing of significant harmful effects either.

Certain minimal antitrust risks were fully assumed by Congress in 1918 in order to meet a severe foreign competitive threat to U.S. industry. They hoped to stimulate exports by removing a potential antitrust barrier. This, however, was a passive means of encouraging exports. A substantially greater threat today by foreign government sponsored industry requires more active means to promote U.S. exports.

In general, foreign competition has no antitrust restrictions to inhibit exporting activities. To the contrary, they receive great government support for exports. They have an enormous advantage in access to government funding, as well as high-leverage bank financing and strong insurance against political and commercial risks. Based on past conduct of other nations, we may be sure that the new multilateral trade agreements recently approved by Congress will not stop foreign government objections to programs like our DISC program, so new measures must be taken by Congress to encourage exports, and the programs must be similar to foreign programs.

The success of large foreign trading firms is linked to their access to high-leverage financing, untaxed operating revenues, and better risk insurance. With such financial support, they can establish large, expert overseas sales and support operations. To be competitive, U.S. firms must have positive export stimulation programs to match the risks and difficulties of doing business overseas.

The chamber welcomes the introduction of legislation such as S. 1663, which is intended to encourage exports by providing for the licensing of export trading companies. An improved environment for Webb-Pomerene associations is one important component of our developing national export policy. Legislation for the development of trading companies is another. Whereas improving the Webb-Pomerene Act is primarily a passive means of encouraging exports, in that the focus is on the removal of antitrust barriers, legislation to encourage the formation of trading companies is a more active mechanism.

WAYS TO FOREIGN MARKETS

At the present time, unless small businesses participate in Webb-Pomerene associations, suppliers have four ways to go to foreign markets: First, they can sell directly to foreign end users; second, they can sell through foreign agents or brokers; third, they can sell through U.S. export management companies; or fourth, they can find a large U.S. multinational firm that needs certain products for specific overseas activities.

The drawbacks of each approach are obvious. Selling directly overseas, because of slower payment time than in the domestic market, ties up current cash flow. Generally, it is cheaper and less risky for the small company to develop its U.S. market to the fullest. Foreign export agents or brokers demand total product control and extremely flexible pricing, leaving the supplier at the agent's mercy. Whether selling directly or through an agent abroad, the small businessman also has to worry about export packing, long-distance multishipper transportation, export and import licenses, lack of trustworthy credit information, paper processing, payment insurance costs, and similar followup and detail work.

Because of these difficulties, many small suppliers turn to export management firms to handle their foreign sales. The majority of these professional middleman operations are too small to handle more than one or two accounts competently. They also lack the management and capital necessary to expand geographically and to establish sales offices overseas. So, even if the export management firm is the best channel for a small supplier interested in exporting, he may still be frustrated in his export efforts.

Selling to large U.S. multinational firms does not get smaller businesses directly involved in foreign trade. A generally accepted objective of a U.S. national export policy is to increase the number of U.S. firms engaging in exporting, particularly small- and medium-size firms.

Therefore, the trading company concept should prove to be an attractive alternative for small business involvement in foreign trade, and the introduction by Senator Stevenson of S. 1663 hopefully heralds serious consideration being given to that concept by the Congress.

Because of its recent introduction and complexity, the chamber has not completed its analysis of S. 1663. The bill has been submitted to the chamber's various departments to give careful consideration to the tax provisions, the antitrust implications, the international financing aspects, and the trade impact.

An obvious strength of the proposal is that it gives formal recognition to organizations devoted to exporting. Once legislation is in place to create a favorable environment for trading companies, the concept should quickly take root and significantly contribute to increasing the flow of U.S. exports.

Before closing, I would like to stress that all of this applies to small businessmen particularly. They need the incentive to export. They are confused by the laws' complexity. Being small, they have limited access to capital for exporting, and they face the highest risks in dealing abroad.

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They have few good paths into exporting, as mentioned before. There are problems of honesty, cost and risk in dealing directly or through foreign agents with foreign buyers. In dealing with current undercapitalized export management companies, they risk poor service from overworked specialists. And these small suppliers have little interest in common with the large multinational U.S. firms.

All of this points to a strong need for cooperative associations and some kind of favored industry status, in order for small business to raise capital, improve the quality of services, establish strong overseas sales offices, and to finance increased exports.

Thank you for this opportunity to present our views on this important matter. I defer to Mr. Waldmann for comments on the impact of your proposed legislation on service industries.

Mr. WALDMANN. Mr. Chairman, if I may continue the statement for the U.S. Chamber. My name is Raymond Waldmann. I believe you have in the record the statement from me. I'd like to make just a few points, if I may, based to some degree on my own experience as Deputy Assistant Secretary in the Department of State for Economic and Business Affairs, but most recently as a member of the chamber's international service industry committee.

This committee was formed in 1978 as a recognition of the importance of services in our international trade. The committee includes industries such as advertising, accounting, banking, insurance, air transportation, leasing companies, franchising, health services, construction, computer services, and a host of others.

About 65 percent of the U.S. gross national product is accounted for by services. Last year, in 1978, services accounted for a $23 billion surplus in our trade account. This is an important factor when you consider that our merchandise trade suffered in the same year a deficit of $34 billion.

While the United States is still the largest service economy and the largest importer and exporter of services in the world, our international position is not without challenge. Between 1969 and 1976, our share of the world's trade fell by one-fifth, from 25 to 20 percent. Our service industries face strong competition from other industrialized countries, such as Japan, Germany, and France, and from the more advanced developing countries, such as Brazil and Korea.

SERVICE INDUSTRIES OVERLOOKED

It's our view that service industries have been overlooked in U.S. trade policy for many years. The testimony cites two examples of recent Government reports, the Murphy Commission report in 1975 and the Williams Commission report in 1971. In both these cases, the attention which was paid to the service industries was scant indeed.

To give you a few more examples, trade adjustment assistance is not available to the service industries. DISC legislation applies only to two service industries—architectural services and construction. The export promotion programs of the Commerce Department have, until very recently, ignored most service industries. And the data collection services within the Government are not organized

to report on service industries to the extent that they report on other trade groups.

The chamber's Service Industry Committee analyzed whether improvements in the Webb-Pomerene Act would benefit service industries. Our conclusion was that they could. Given the explicit exclusion of service industries in the past, however, we have no experience with the act. But we strongly believe that there is a potential value to U.S. service exporters, particularly in those industries which involve heavy start-up, presale investment, or proposal-writing expenditures.

Finally, any assistance that can be provided through amendment of the act itself or through similar legislation, such as S. 1663, which could allow for greater competitiveness on the part of the U.S. service industry, would be helpful. Based on the administration's testimony today, I believe that it's fair to say that inclusion of service industries in any of these bills would not be controversial.

The Commerce Department this morning mentioned that the inclusion of services was absolutely vital, and all of the bills before the committee have this effect. Assistant Secretary Bergsten also suggested that he had no objection to including services in any actions taken by the committee, and we would certainly support any action along that line.

Thank you.

Senator STEVENSON. Thank you, sir.

[The complete statements follow:]

STATEMENT
on
LEGISLATION TO AMEND THE EXPORT TRADE ACT
and
TO PROVIDE FOR LICENSING TRADING COMPANIES
before the
INTERNATIONAL FINANCE SUBCOMMITTEE
of the
SENATE BANKING COMMITTEE
for the
CHAMBER OF COMMERCE OF THE UNITED STATES
by
Neil J. Boyer
and
Raymond J. Waldmann
September 17, 1979

I am Neil J. Boyer, an attorney and consultant on international trade, law, and finance, and a member of the Export Policy Task Force of the Chamber of Commerce of the United States. I am also chairman of that Task Force's Subgroup on Antitrust, which was established recently to further develop the Chamber's position on the impact of U.S. antitrust laws on our international trade performance.

Also appearing with me is Raymond J. Waldmann, an attorney with the firm of Schiff, Hardin and Waite in Washington, D.C. Mr. Waldmann is a member of the Chamber's International Service Industry Committee and chairman of its Subcommittee on Antitrust Matters. He will discuss the legislation before this subcommittee as it relates specifically to the service sector. With us is Howard Weisberg, director of international trade policy for the U.S. Chamber.

The U.S. Chamber represents a membership of over 84,000 small, medium, and large businesses, 1,270 trade associations, over 2,600 state and local chambers of commerce, and 42 American chambers of commerce overseas.

I am here to express the Chamber's support for recent legislative initiatives to encourage small and medium-size businesses to enter the international trade arena. Both of the Webb-Pomerene amendments introduced in Senate, S. 864 and S. 1499, go a long way toward making this Act a more useful export promotion vehicle.

Webb-Pomerene Act

The reasons why small businessmen favor change in the Webb-Pomerene Act are simple. They cannot afford either the time or expense of dealing

with antitrust enforcement agencies like the Federal Trade Commission (FTC) or the Justice Department. They see that formation of Webb-Pomerene associations entails a significant amount of time and money for lawyers and accountants, not to mention the inconvenience of arranging and attending numerous organizational meetings for uncertain exemption from the antitrust laws. In short, the present costs outweigh the uncertain future rewards.

To induce small businessmen to participate in Webb-Pomerene associations, they must see a reasonable return on their investment. This means that, first, they must have a clear explanation of the type of associations that can be formed under the Webb-Pomerene Act and what the rules of conduct and benefits are under the Act. As currently written, it is difficult to explain the rules and project the benefits of the Webb-Pomerene Act. Its language is confusing and vague. As a consequence of hearing about the arguments over its true meaning and the opposition of the Justice Department and the FTC during the past 60 years, all businessmen, small and large, rightfully distrust the Act and, accordingly, discount the benefits.

Now, more than any time in the past, we need amendments like S. 864 and S. 1499 which positively and unequivocally restate Congress' intent to encourage smaller businessmen to use this cooperative mechanism without fear of the sanctions of U.S. antitrust laws. The Danforth bill (S. 864) is preferable to the extent that it would place primary authority and administrative responsibility with the Commerce Department, whose basic objectives are, we feel, in keeping with the critical need to stimulate U.S. exports. It is most desirable to move the administration and monitoring of these associations away from the negative influence of the antitrust agencies, whose primary concern, after all, is enforcement and prosecution. In the positive environment offered by the Commerce Department, we will for the first time be able to test whether or not aggressive, commercially oriented programs can encourage the formation of successful associations of smaller companies.

In general, both bills seem more than adequate to protect against unreasonable or unnecessary restraints of trade. While the Danforth bill leaves the enforcement authority with the Department of Justice, the Roth proposal (S. 1499) transfers jurisdiction to the Federal Trade Commission. Either agency can be expected to see that export associations adhere to these proposed laws.

Both bills would also correct an important omission in the original Act by extending the protective umbrella over service industries. This is especially important to the many small firms that specialize in management consulting, engineering, architecture, finance, insurance, transportation, and communications, where so much of our best exportable talent is found today.

One area which is not considered in either bill is the desirability of permitting export associations to participate in government-funded overseas projects. This type of activity was restricted under the decision of U.S. v. Concentrated Phosphate Export Association, 393 US 199(1968). Since there seems to be no philosophical reason why such associations should not be permitted to participate in such projects, language could be inserted into this bill to allow export associations to participate in large foreign industrial projects under government controls when funded by U.S. agencies like AID. Otherwise, small companies may find themselves still without the means to participate in U.S.-sponsored projects on a significant level.

Criticism of the Webb-Pomerene Act and of attempts to enhance it seem to boil down to the following debatable observations:

1) that Webb-Pomerene associations do not serve many small or medium-size exporters, but instead represent only certain oligopolistic industries marketing products that cannot be differentiated from competitors' products;

2) that they promote domestic price stabilization through a foreign "venting" of surplus production;

3) that they serve the interests of foreign cartels by stabilizing foreign market prices and sometimes even collaborate with them;

4) that they do not act as selling agents for members and are not designed to do so, but rather they are only designed to act as price setting mechanisms; and

5) that they have actually caused formation of foreign cartels where they never existed before.

We do not accept these observations. For the sake of argument, however, assume they are valid. Congress originally foresaw that minimal trade restraints might occur and assumed that risk. Beyond a minimal restraint, the antitrust laws come into play under the watchful eye of the Justice Department, so that the five concerns delineated above are controlled.

The vagueness and overly restrictive judicial and administrative interpretations of the Webb-Pomerene Act have discouraged its use. So it does not seem relevant to criticize the Act or call for its repeal on the grounds that not many Webb-Pomerene associations have been formed or exist today.

The intent of Congress today ought to be stronger in favor of exports than it was even in 1918. At that time this nation faced a trade crisis with foreign cartels threatening important segments of our economy. That same threat exists today, only on a much larger and more serious scale, because many of the foreign cartels are government-owned, supported, or managed. The magnitude and seriousness of the problem is vividly illustrated in a recent Harvard Business Review article by Kenneth Walters and R. Joseph Monsen of the University of Washington's Business School. They show that more than one third of the 50 largest industrial companies in Europe are wholly or partially owned or controlled by their national governments. The primary goals of such organizations include expansion and diversification of their international operations in direct competition with U.S. industries.

Government-controlled companies enjoy great competitive advantages over U.S. companies. They expand freely, by integration or diversification, without fear of antitrust sanctions. They engage in high-risk research and business development activities without fear of losses or bankruptcy. They do not need to earn profits or pay dividends in order to attract capital when they are guaranteed capital from their nation's treasury. They are not restricted by concerns with unfair competition. They enjoy monopoly control over national markets. Their subsidies are disguised as tariffs or import quotas against competitive products or as technical standards. There are no public financial disclosure mechanisms to force them to reveal the real costs of their operations.

Foreign companies which are not nationalized can also be effective tools for carrying out national competitive economic policies. The

Japanese general trading companies are superb models of how a nation can enjoy many of the benefits normally derived from nationalization. Other developing countries, such as Korea, are emulating the Japanese because of their overwhelming success in foreign trade. Such trading companies often operate so closely with their governments as to be indistinguishable from national companies. Typically, they are large institutions which enjoy easy access to high-leverage financing. Thus, without large profits they establish worldwide marketing operations, have large support staffs at home, and integrate vertically and horizontally with other companies, domestically and overseas, for greater control over the flow of international trade. They attract the best managers and technical people, who then go after the sales accounts of the lowest-cost producers or the technological leaders of an industry.

We cannot begin to compete with these national combines until Congress takes such simple first steps as clarifying the Webb-Pomerene Act. Once that is done, Congress and the Administration must quickly follow through with positive export-stimulating programs.

Although I have referred to the needs of small and medium-size businesses, I do not mean to suggest that large business will not benefit from the passage of such legislation. The Chamber believes that effective legislation for export associations and trading companies will encourage new export undertakings regardless of company size.

Trading Company Legislation

The Chamber welcomes the introduction of legislation such as S. 1663, which is intended to encourage exports by providing for the licensing of export trading companies. An improved environment for Webb-Pomerene associations is one important component of our developing national export policy. Legislation for the development of trading companies is another. Whereas improving the Webb-Pomerene Act is primarily a passive means of encouraging exports, in that the focus is on the removal of antitrust barriers, legislation to encourage the formation of trading companies is a more active mechanism.

At the present time, unless small businesses participate in Webb-Pomerene associations, suppliers have four ways to go to foreign markets: 1) they can sell directly to foreign end-users; 2) they can

sell through foreign agents or brokers; 3) they can sell through U.S. export management companies; or 4) they can find a large U.S. multinational firm that needs certain products for specific overseas activities. The drawbacks of each approach are obvious.

Selling directly overseas, because of slower payment time than in the domestic market, ties up current cash flow. Generally, it is cheaper and less risky for the small company to develop its U.S. market to the fullest.

Foreign export agents or brokers demand total product control and extremely flexible pricing, leaving the supplier at the agent's mercy.

Whether selling directly or through an agent abroad, the small businessman also has to worry about export packing, long-distance multi-shipper transportation, export and import licenses, lack of trustworthy credit information, paper processing, payment insurance costs, and similar follow-up and detail work.

Because of these difficulties, many small suppliers turn to export management firms to handle their foreign sales. The majority of these professional middleman operations are too small to handle more than one or two accounts competently. They also lack the management and capital necessary to expand geographically and to establish sales offices overseas. So, even if the export management firm is the best channel for a small supplier interested in exporting, he may still be frustrated in his export efforts.

Selling to large U.S. multinational firms does not get smaller businesses directly involved in foreign trade. A generally accepted objective of a U.S. national export policy is to increase the number of U.S. firms engaging in exporting, particularly small and medium-size firms.

Therefore, the trading company concept should prove to be an attractive alternative for small business involvement in foreign trade, and the introduction by Senator Stevenson of S. 1663 hopefully heralds serious consideration being given to that concept by the Congress.

Because of its recent introduction and complexity the Chamber has not completed its analysis of S. 1663. The bill has been submitted to the Chamber's various departments to give careful consideration to the tax provisions, the antitrust implications, the international financing aspects, and the trade impact.

An obvious strength of the proposal is that it gives formal recognition to organizations devoted to exporting. Once legislation is in place creating a favorable environment for trading companies, the concept should quickly take root and significantly contribute to increasing the flow of U.S. exports.

I defer now to Mr. Waldmann for comments on the impact of the proposed legislation on service industries.

IMPACT ON SERVICE INDUSTRIES

The Chamber supports amendments specifically making services eligible for the Webb-Pomerene or other equivalent exemptions and would like to encourage improvements in the Act which would make it more attractive for service industry firms to take advantage of its provisions.

Services are an important and growing part of our trade. For this reason the International Service Industry Committee was formed by the Chamber in 1978. It brings together representatives of industries which are often not adequately served by government policies and programs relating to international commerce. The Committee includes industries such as advertising, accounting, banking, insurance, air transport, lodging, licensing, law, leasing, franchising, finance, health services, construction, computer services, engineering, consulting, communications, data transmission, shipping, tourism, motion pictures, and others.

The American economy is becoming more service oriented with almost seven out of every ten working Americans employed in the service sector. About 65 percent of our GNP is service derived. Last year U.S. exports, plus imports of service industry products, as well as direct investment flows, fees, and royalties, totaled about $129 billion, or 30 percent of all U.S. trade. The services account produced a $23 billion surplus, an important offset to the $34 billion deficit suffered in merchandise trade.

U.S. service industries also have a presence abroad. The latest available U.S. government estimate puts the value of overseas sales by foreign branches and subsidiaries of U.S. service industries at about $50 billion in 1974. Since then, the figure has probably doubled.

While the United States is still the largest service economy and the largest importer and exporter of services, our international position is not without challenge. Between 1969 and 1976, our percentage share of the world invisibles trade receipts fell by one fifth, from 25 percent to 20 percent of the world's total. Our service industries face strong competition from industrialized countries, such as Japan, Germany, and France. The more advanced developing countries, such as Brazil and Korea, are daily making inroads into international service markets. Domestic service sectors in foreign countries are strengthening almost everywhere.

U.S. service industries also face foreign competitors whose governments do a better job of promoting and defending their international service industries than we do. These governments recognize the major and growing role of services in their international economic activities. In the United Kingdom and France, service industries enjoy encouragement and support equal to that given to manufacturing. Given the phenomenal growth of the Japanese service economy, it is only a matter of time before Japanese service industries begin penetrating international markets.

U.S. service industries have been overlooked in U.S. trade policy for years. Traditionally, our policymakers have shown little disposition to think in terms of service industry interests or whether these differ from those of manufacturers or the agricultural community. This is evidenced in theoretic studies of governmental international organizations. For example, both the Murphy Commission Report[1] and the Williams Commission Report[2] overlooked the entry of the U.S. service sector into our foreign commerce and, thus, never considered the fact that it was commonly ignored by policy processes. Most responses to unfair trade practices are not available to services. Though U.S. services may suffer from import competition, the trade adjustment assistance provisions of trade legislation are not available to service producers. DISC legislation is applicable to only two service industries. The export promotion programs of the Commerce Department ignore most services. The data collection mechanism of the U.S. government is not organized to analyze service flows.

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[1] Report of the Commission on the Organization of the Government for the Conduct of Foreign Policy (June 1975).

[2] United States International Economic Policy in an Interdependent World (July 1971).

Formal recognition of services in Washington finally came in the Trade Act of 1974, when a congressional initiative created the authority to negotiate reductions in barriers to services trade. Little was accomplished with these authorities in the MTN -- another example of services failing to capture executive branch attention.

In attempting to define the Trade Act mandate and determine negotiating parameters, it was necessary to refer the matter to a White House interagency task force chaired by the Secretary of Commerce. This group proceeded to review in detail the position of U.S. service industries in foreign commerce and the inadequacy of the present governmental structure for dealing with them.

In a massive 1976 report (U.S. Service Industries in World Markets -- Current Problems and Future Policy Development, U.S. Commerce Department, Washington, D.C. December, 1976), the task force concluded that services are now of major importance in U.S. foreign commerce and their increased future importance to U.S. economic health and growth is an "inescapable fact." Moreover, governmental abilities to adapt and respond to this fact have lagged as international economic policy formation and related programs "have been almost exclusively focused on goods, not services."

This background is necessary to fully understand the challenges facing U.S. service industries when they attempt to export or operate abroad. In order to face these challenges more effectively, the Chamber's Service Industry Committee analyzed whether improvements in the Webb-Pomerene Act could benefit services. It concluded that action to extend Webb-Pomerene type exemptions to service industries was highly desirable.

It is important to recognize that U.S. service industries have no experience with the Webb-Pomerene Act because the explicit language of the Act restricts provisions to trade or commerce in "goods, wares, or merchandise." At the time of the Act's passage in 1918, excluding services may have made sense because services were considered "handmaidens" to trade in goods. Today, this situation has changed. The potential value of the Webb-Pomerene Act to U.S. service exporters is considerable, particularly those in industries involving heavy start-up and presale investment expenditures.

Of particular importance to potential service industry users of the export association (or trading company) is how service industry is defined within such legislation. Legislation which includes services should make explicit that services are services per se and not just those services traditionally related to trade in goods. Ambiguity in this respect in the 1974 Trade Act tended to circumscribe the extension of its benefits to all service industries.

Because U.S. industries often face competition from foreign industries supported by their governments (and in some cases by discriminatory practices), any assistance that can be provided through amendment of the Webb-Pomerene Act or similar legislation would allow greater competitiveness on the part of U.S. service industries.

Senator STEVENSON. Mr. Huszagh?

Dr. HUSZAGH. I'd like to summarize and emphasize a few of my written testimony points, and then outline some personal thoughts on strengths and problems of the bills you are now considering.

JAPANESE TRADING COMPANIES

The Japanese trade companies have many facets that contribute to their success. They make available to manufacturers-clients extensive credit facilities, supplies, and raw materials. They have elaborate linkages with the Japanese Government, which while often exaggerated in current literature give them considerable leverage in world markets.

Another facet of the trading corporations often overlooked is that they reduce risk for creditors. Essentially they're intermediaries and make credit decisions in the field. The large banks give them enormous lines of credit with the understanding that the trading corporations will parcel it out in ways that minimize risk.

Another facet of Japanese trading companies apparently not contemplated in the various Senate bills is that they handle a broad range of products, both exports and imports. For example, by buying raw materials for their manufacturing clients in large volume at the lowest costs, they help materially reduce manufacturer costs. Then, they manage the export of the manufactured products over long time frames to strategically develop markets that mesh with increases in manufacturing capacity. By developing markets to absorb the growth, their manufacturing clients are able to go down the volume/cost curve faster than competitors.

Another major function of trading companies is the collection of information on all sorts of technologies, and its distribution to their client companies who adapt such technologies to their own preproduction processes.

Some people have observed that these trading companies are now reaching the point of diminishing returns on cost cutting through strategic planning of supply purchases, market growth, volume increases, etc. Thus, they must rely on such things as product servicing to enhance competitiveness. By and large, however, manufacturers are better able to service products they build than intermediaries. This is where Americans may gain a significant competitive advantage. Japan is also reaching the stage

where it can no longer adapt R. & D., but must undertake its own basic R. & D. Here again, the people best able to make the R. & D. investments and wisely allocate research resources are the manufacturers themselves, because they understand the total process of product design, production, sale and servicing.

ANTITRUST CLARIFICATION

I view the current bills as ambivalent on trading company relationships with manufacturers. They seek to clarify antitrust issues but don't go far enough. The perennial controversy regarding the Webb-Pomerene Act makes clear the Justice Department's reticence to defer to FTC determinations, and creates anxiety about criminal and civil penalties. Although the probability of Justice Department suits is low, escalating criminal and civil penalties minimize the risk reduction benefits of Webb-Pomerene associations.

I see no reason why a Senate bill does not authorize the Government to obtain the data it needs to detect antitrust violations and to monitor; and seek license withdrawal under the Trading Company Act if violations seem likely. Provisions for consultation under current bills inadequately aid trading companies that must necessarily be closely associated with the manufacturing process.

My testimony includes several models of extractors, merchandisers and manufacturers. They demonstrate how basic manufacturing functions cannot be divided from other functions. If these various functions, however, are done by different entities on a coordinated basis, they may be construed as violating antitrust laws.

This committee is encouraging experimentation with activities other countries have found quite beneficial. We need more experimentation. The reticense of the Federal Government to engage in such experimentation has caused State governments to be much more active in assisting their resident companies. Their economic welfare depends upon those companies and they must be responsive to them for political reasons. Exports are a very large component, up to 30 to 40 percent, of a State's economy and are often essential to its stability. I believe the Governors of this country view the bills now being considered as an important move to expand exports and enhance State interests. They are making similar moves on their own. Thus, I feel the bills should more concretely improve the linkages between existing federal promotional programs and these trading corporations.

Your bill makes significant strides in that direction regarding tax policy. It authorizes tax deferral that may significantly simulate export activities. I believe, however, it ought to contain more definitive language on the benefits these companies can derive from the Commerce Department programs now being formulated. Conversely, there ought to be more clarity on the kinds of information the Secretary of Commerce can collect to avoid fishing expeditions. Finally, the bills should more concretely deal with confidentiality problems. Senator Danforth's and Senator Stevenson's bills could be easily merged in that regard.

DATA COLLECTION AND COMMUNICATION

Apart from the above comments, let me stress that trading companies have unique value because they collect enormous amounts of data and distribute it efficiently. Books and articles on the communication facilities of trading corporations in Japan and here (like Phillips) suggest they almost equal Defense Department facilities.

Further, these companies are very sophisticated in how they analyze this data and redistribute it for action. Unfortunately, this type of elaborate communication raises significant antitrust and confidentiality issues.

Apart from the problems noted, this subcommittee should be concerned about the bills' impact on State initiatives. State governments increasingly have facilitated business activities abroad. Written testimony from Governor Romero of Puerto Rico emphasizes this point. It would be unfortunate if, by implication, this bill was construed as a Federal preemption of such State activities.

Since this is a very complex constitutional area, it would seem advisable that final legislative language contain findings that the bill authorizes an adjunct to State activities and not a substitute for them. States are not active in promoting export trade, and serve a very vital purpose in our economy. Thus, their activities should not be impaired.

Thank you.

[Complete statement follows:]

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I. Overview of Export Trading Companies

Trading Companies traditionally have helped producers in their countries expand export trade to and maintain market shares in foreign regions. In past centuries, English and Dutch trading companies also assisted their respective country's global influence while providing authors with rich material for fictional and non-fictional literature. They sold their country's products, supplied it with needed raw materials, and "synchronized" foreign government action with major policy interests of their country and company.

In this century the Japanese trading companies, Sogo Shoshas,[1] have maintained the mystique created by their European counterparts and developed an operating span and style which is awesome. They trade tens of thousands of different commodities, operate all over the globe and sell hundreds of billions of dollars of goods and services each year. Their capacity to get things done and Japan's premier position in export trade, create envy in other countries like ours and invite emulation. The senate bills now before the subcommittee have been stimulated in part by these Sogo Shoshas.

Legendary trading companies have also developed in America, but their penchant for secrecy and focus on commodities has limited their value as models for export expansion initiatives.[2] Consequently, our inspirations must be derived from poorly understood foreign examples and implemented through awkward strictures like the Webb-Pomerene Act, fashioned when we cared little about exports and understood little about the real dynamics of export trade.

II. Basic Functions of Trading Companies

Trading Companies undertake many functions depending on their country of origin and business focus; important ones being the provision of financial services to small and medium manufacturing firms, collection of information about potential export markets, reduction of risk undertaken by various creditors to the exporters, execution of paperwork associated with the export transactions, and provision of insurance, warehousing and other transportation services. In recent years many trading companies have also coordinated large-scale development projects involving many different manufacturing and service organizations. While each of these services is important, perhaps the most significant relates to the information services. For firms expanding into the export business, the more successful Japanese trading companies:[3]

> "supply information on the size of potential markets; competitive manufacturers in the export country; current prices and profit potential; foreign exchange rates and likely financial fluctuations; distribution channels; the credit standing of potential wholesale and resale distrbutors; current attitudes of industrial users, customers, competitiors, labor unions, or government officials toward the proposed export products; foreign import regulations and other tariff and non-tariff barriers; and the various export permits required by the Japanese government. To domestic manufacturers that depend on advanced technology, the big ten provide information on current scientific and technological advances in the U.S. and Western Europe, on the latest equipment available,

on market potential, and on technology licensing or joint venture requirements."

The information services, however:

"are not limited to economic and business information of immediate practical value; they extend to global, political-legal data (e.g., anti-trust law decisions), demographic data, and the social-cultural environment (e.g., anti-business attitudes, consumer movements, anti-pollution sentiments, youth culture, and the like), and trends that are likely to have impact on the Japanese economy."

These services, provided in an efficient manner by companies of enormous scale who have close working and management relationships with their client constituencies, permit large-scale importation of raw materials needed for low cost manufacturing. They also ensure broad scale development of foreign markets for manufactured products which have allowed producers to rapidly increase their scale of production, and thus further reduce costs. Also because of their size and close relationships with manufacturing clients, banks, insurance companies, etc., the trading companies can provide low cost financing, insurance, warehousing and transportation, contract negotiation, and fabrication, processing and distribution centers in world markets. Apart from materially facilitating manufacturers' price competitiveness, they provide information and advice on advanced foreign technology, market conditions, foreign tariffs, local laws, overseas business customs, human relations, natural resource development, project feasibility, product quality, and sales promotion.

The phenomenal success of Japanese exports rests significantly upon the close working relationships among the Trading Companies, the banks that provide capital through the Trading Companies to manufacturers at leverage unheard of by American standards, and small, medium and large manufacturing organizations. Equally important, these three private sectors coordinate closely with the Japanese government through the Ministry of Industry and Trade (MITI) and the Japanese External Trade Organizations (JETRO).[4] These latter units not only manage and condone the close relationships of the private sector entities, but deploy significant analytical and financial resources of their own to undertake tasks at both the macro and micro levels which cannot conveniently be undertaken by private sector entities.[5]

As the opportunities diminish for the types of cost reductions just mentioned, due to a number of factors both within and outside Japan, the vitality of Japanese exports and of the Trading Companies must rest increasingly on manufacturers' capacity to provide improved service on their products in foreign locations and develop new technology as opposed to adapting European and U.S. technologies to Japanese production techniques. Some feel that Trading Companies are not well suited for success in these areas as opposed to extension of the manufacturers' capabilities, and thus will play a declining role in export expansion. The only exception would be in the commodities area where research and development and servicing are relatively unimportant attributes of sales success.

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III. American Export Expansion: Keys to Success

In contrast to the evolution of Japanese production and export methods, U.S. enterprises depend largely on servicing and research and development innovations to maintain market competitiveness. Close relationships between public and private sectors and among private sector units have been of only marginal importance because they frequently are forbidden by law or have been retarded by the inherent adversarial relationship between U.S. business and government. Consequently, our most successful exporters adroitly link market demand with product design by combining marketing and production functions within a single management structure. For example, early in this decade when capacity to supply automobiles began to outstrip apparent demand for a basic utility vehicle, our automotive companies were able to generate an almost infinite variety of colors and models in order to keep up with the evolving tastes of the American consumers and attract new consumers by appealing to taste rather than needs.

The extent to which our manufacturing enterprises have integrated production and marketing functions is apparent from a comparative analysis of the three attached charts modeling the basic features of the extractive, manufacturing and merchandising industries. At the one extreme is the extractive industry, which is basically a commodity industry. Here the major emphasis is on production and distribution, with little attention being paid to the marketing function. At the other extreme is the merchandiser who increasingly seeks success through innovations in distribution, credit and inventory control. The American manufacturer, especially the medium and large ones, have of necessity tightly integrated these merchandising and production functions in a way which would be hard to duplicate through an externalized marketing organization loosely attached to manufacturing facilities. Of course, these producers are more and more emphasizing service and research and development, which are not functions most efficiently undertaken by Trading Companies.

I believe this subcommittee should pay careful attention to American industrial structure in designing initiatives for export expansion; detailed reasons for this belief are contained in my April 5, 1978 testimony submitted in connection with this subcommittee's landmark review of U.S. Export Policy. If trading companies are to be an important stimulant to American exports, they must be allowed to have close relationships with both manufacturers and credit sources that facilitate the flow of communications and permit efficient allocation of management responsibilities. We will not be competitive in foreign markets solely by encouraging the proliferation of "wholesalers." They must be allowed to integrate with producers in a way which insures efficient responses to shifting market trends and production costs.

IV. Senate Proposals on Export Trading Companies: Potential Impact and Relationships to Alternatives for Export Expansion

While much export expansion potential has been attributed to the Webb-Pomerene Act since its inception, the act has been of little value for a number of reasons. First, the act does not preclude the Department of Justice from attacking export associations as restraints on commerce despite Federal Trade Commission approval pursuant to the Act. The Justice Department insists upon

this right of independent action, but downplays its probability of being exercised. Increasing criminal penalties and civil penalties associated with Justice Department action, however, have transformed a small enforcement risk into a major deterrent. Since the final business decision is based on a multiplication of the enforcement probability times the costs involved if enforcement action is taken, business has not found much value in existing Webb-Pomerene exemptions. Furthermore, the parting remarks of Attorney General Griffin Bell suggest that the criteria used by the Justice Department in evaluating enforcement actions is substantially detached from the national policy making process regarding export expansion. The lackluster results of the Webb-Pomerene Act are also traceable to its inapplicability to service industries which are of growing importance in world trade due to inherent comparative advantages.

Apart from these obvious inadequacies, other more serious issues limit the Act's utility. It discourages the essential unity between marketing and production which has long been a hallmark of American enterprise. Thus, while the law encourages economies of scale in the sale of products overseas, it maintains a division between this marketing function overseas and the domestic production and marketing functions. As noted earlier, this bifurcation strikes at the very heart of American comparative advantage.

Various bills now before this committee as well as proposals presented since the early 1970s, expand the types of enterprises eligible for exemption and, to varying degrees give greater definition to the concurrent jursidiction of federal agencies over the anti-trust aspects of export trade associations. Depsite the imposition of elaborate reporting requirements and extensive government monitoring, however, none of these bills assures Trading Companies and their owners that they will not be subjected to onerous criminal and civil liability at the instigation of the federal government.

There are legitimate, philosophical reasons for maintaining separation between law enforcers and government agencies interested in promotion of changing policies. It does not seem wise, however, to perpetuate ambiguity that substantially undermines the utility of the experiment at the outset. Furthermore, these bills, regardless of the government supervision involved, give the government considerable license to reverse its position without assuming the burden of proof for reversal. In light of the extensive capital and human investments that must underlie an effective trading corporation, it is unlikely investors will undertake these costs if government can easily change its mind on the continued licensing of a trading corporation. For example, public utilities would not make major investments in dams if the licensing agency was not bound by constitutional due process requirements when taking property as a result of license revocation. While the Stevenson Bill appears to deal with these issues, there is the eventual caveat which maintains Justice Department autonomy and limits judicial review far short of that associated with regulation in the public utility field. S. 864, while no better on the antitrust issue, does explicitly require government observance of APA standards.

While the Justice Department may correctly assert the probability of independent prosecution is low if trading companies operate as now anticipated under existing legislation, the odds would surely increase as trading corporations developed close relationships with manufacturers in the same sector, credit institutions, insurance companies, etc., to achieve the real

efficiencies inherent in the trading company concept. If they are precluded from moving in these directions large scale investments essential for substantial export expansion are unlikely.

Apart from anti-trust considerations, current legislation establishes little linkage between the trading companies and public sector credit and export intelligence services, which is a hallmark of the Japanese success story. The Stevenson Bill provides a basis for such linkage and provides tax incentives for trading companies, but one must be skeptical whether private and public sector activities really have the compatibility necessary to make them function as one unit, such as is the case in Japan. Already the federal government is strengthening its sectoral analysis capability and planning helpful services for the private sector (e.g., TEMP program of the Commerce Department). A careful analysis of these efforts, however, suggests the price of acquiring these services may be extensive submission to federal direction rather than a collaboration with federal policy makers and technicians. Inherent fear of what federal policy makers will extract for providing benefits may stimulate industry to seek closer working relationships with state government activities. From a political standpoint, states are constrained from being heavy handed and pursuing unchecked, public sector planning of private sector activities.

If the past is a prologue of the future, the private sector reporting needed to derive the benefits established by these bills will materially compromise existing freedoms, produce another layer of paperwork and reporting requirements, and result in dubious material benefits. Furthermore, private sector applicants may be exposed to unforseen problems. For example, only one bill indicates the extent to which monitoring reports will be available to the public generally and thus compromise the competitive positions of the various trading corporations. Secrecy is the hallmark of trading companies and the potential of spreading internal operations upon the public record will surely extinguish interest in becoming a "licensed" trading company.

While the trading company/association bills now being evaluated by this subcommittee do not create an optimal trade development environment, they reflect a significant commitment to systematic expansion of our exports. If properly linked with other private and public sector institutions, these initiatives will challenge businesses to substitute aggressive export salesmanship for complaints of government interference and will give the world community reason to have confidence in the dollar. Thus, the Congressional history and findings of this legislation ought to make clear how previously authorized federal activities and observed deferences to non-federal activities should reinforce export expansion objectives of trading entities. The Stevenson bill does make explicit advantageous linkages with tax benefits, but more is needed.

The Justice Department should be encouraged to expand and streamline its business review procedures and abandon the threat of retroactive prosecution. The Small Business Administration, Ex-Im and the Department of Commerce should support creation of export management corporations in each city servicing a major portion of a state or region. Federal programs like TEMP and WITS should be optimized to help particular sectors actually in need of such services, while minimizing the paperwork and reciprocal commitments which are the bane of many federal programs. Finally, current state initiatives to increase local commitment to and interest in export sales should not be limited by withdrawal

of federal encouragement or the threat of federal preemption justified in terms of elusive and counterproductive goals of uniformity. Conversely, federal programs ought to be further synchronized with these regional experiments to give them greater impact and provide state and local personnel with insights necessary to further commit their local constituencies to export expansion.

V. Recommendations

A. Application of antitrust laws to authorized export trading companies/associations should be further clarified by increasing the government's burden of proof concerning prosecution of activities inherent in initial authorization and limiting sanctions to license revocation or cease and desist orders whenever possible. Also it should be made clear that government actions are subject to constitutional due process requirements.

B. Clearly limit information and action concessions that the Secretary of Commerce can extract from the private sector as a requisite for initial and continued license approval. Also limit the extent to which evolving federal sectoral planning efforts can be used as criteria for regulating activities of export trading companies and preclude disclosure of application information which is not essential for administration of the export trading company program.

C. Further elaborate fiscal, information, and regulatory benefits that Congress wishes to be made available to licensed associations with a minimum of paperwork, uncertainty and time delay.

D. Mandate annual reports to the Congress concerning administration of the program and additional benefits needed to make export trading companies best serve U.S. citizens' interests. Special attention should be given to their potential for translating research and development investments into export competitiveness.

E. Make clear that legislation does not reflect Congressional intent to curtail current individual and collective state efforts that facilitate export sales to discharge state health, safety and welfare responsibiities. Further, state programs supporting export expansion through trading company activities should be given priority support by federal facilities established to promote export expansion.

Footnotes

1. A.K. Young, The Sogo Shosha: Japan's Multinational Trading Companies (Boulder, Colorado: Westview Press, 1979).

2. See generally D. Morgan, The Grain Merchants (New York: Doubleday, 1979) and Business Week cover story on Philipp Brothers, September 3, 1979.

3. Supra, n.1 at pp. 61-62.

4. For general analysis of linkages between the private and public sectors see E.F. Vogel, Japan Is Number One: Lessons for America (Cambridge: Harvard University Press, 1979).

5. See J.E. Sanford, Export Stimulation Programs in the Major Industrial Countries: The United States and Eight Major Competitors (Library of Congress, 1978).

OUTLINE OF EXTRACTIVE INDUSTRY TASKS

I. Marketing and Sales

A. Conduct marketing research; forecast and review sales.

B. Assess competition.

C. Determine general economic conditions.

D. Contact prospective buyers.

II. Exploration

A. Determine resources available for profitable extraction.

B. Evaluate resource.

1. Determine recoverable content.
2. Estimate future market price.
3. Estimate production costs.
4. Assess resource life.

C. Conduct feasibility studies; compute costs and profits; and set price.

D. Formulate engineering plans for resource development.

1. Estimate development costs.
2. Design quality control standards.
3. Design pollution control.

III. Finance

A. Finance exploration.

B. Finance resource development.

IV. Resource development

A. Plan short, medium and long term development.

B. Acquire land.

C. Comply with environmental and legal constraints throughout development.

D. Transport equipment for development and support services.

E. Prepare land for extraction; provide transportation and infrastructure facilities.

F. Recruit and train labor.

G. Implement method for development, support systems and services.

H. Implement quality control standards.

I. Implement pollution control standards.

J. Maintain facilities, support systems and services.

K. Conduct research and testing related to development.

L. Process or refine resource.

1. Utilize raw materials, processes, additives to upgrade or concentrate.

2. Adjust processing to meet quality control standards.

3. Process further when necessary (repeat 1 and 2).

M. Dispose of wastes consonant with government regulations.

N. Prepare processed resources for transport.

O. Maintain processing plant and equipment.

V. Marketing and Distribution

A. Transport extracted resource from field to processing plant or distributor.

B. Sell resource consonant with contract specifications.

C. Transport processed resource to distributor, manufacturer, or consumer.

D. Provide and maintain transportation systems.

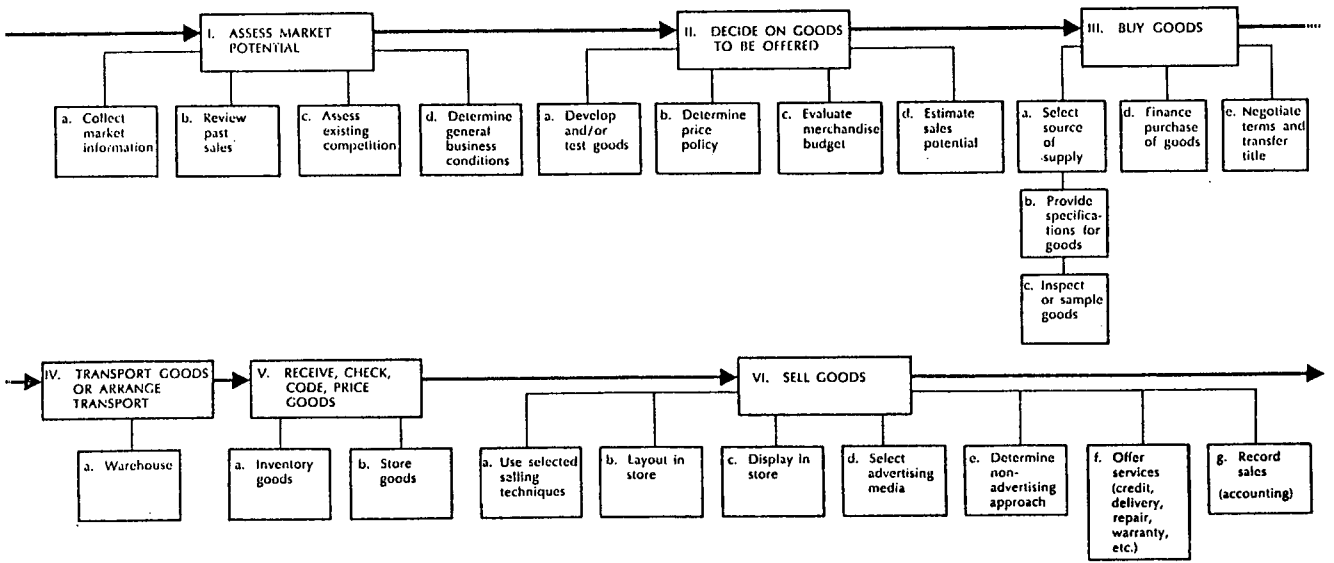
E. Warehouse and inventory extracted or processed resource when necessary.

VI. Post-Extraction

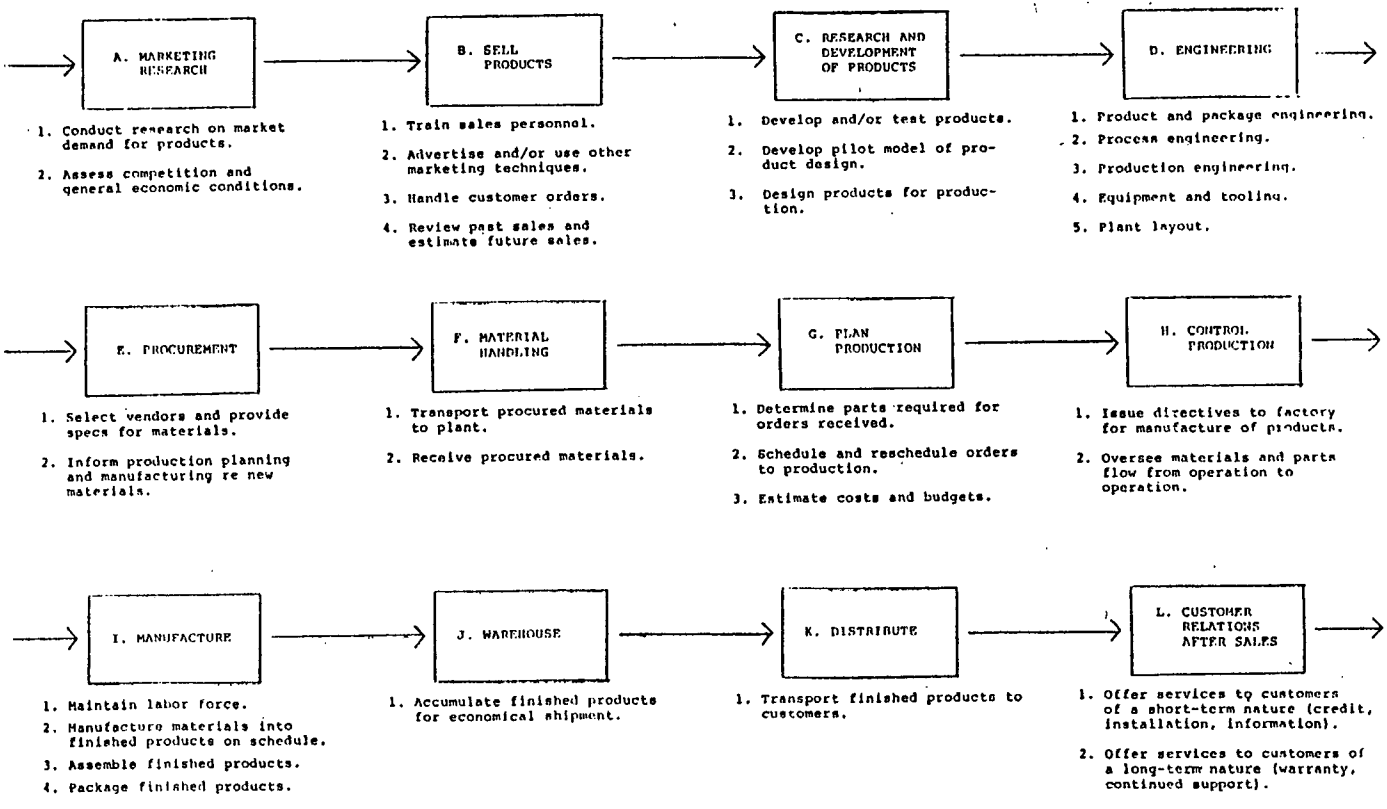
A. Restore land in harmony with reclamation, dumping, government regulations.

B. Recover resources from or

TASK MODEL OF MERCHANDISER



TASK MODEL OF MANUFACTURER



Senator STEVENSON. Thank you, sir, and for your continuing help.

Mr. McDermid?

Mr. MCDERMID. Yes, Mr. Chairman.

As flattering as it is to me—I was given a promotion this morning—I am, for the record, assistant general counsel rather than general counsel of the National Association of Manufacturers.

At the outset, I want to tell you that we are in favor of the principles behind S. 864, S. 1499, and at least title I of your bill, S. 1663. I'll need to elaborate on that qualification in a minute.

I'd also like to clarify a couple of matters that were raised this morning. Mr. Bergsten noted that Japanese trading companies in his opinion do not account for a big trade surplus. In my statement, I have attached as an appendix a description of conditions in Japan. I picked Japan for several obvious reasons, but one more obvious one is that in 1976 NAM conducted a survey of our multinational members, and that survey revealed that their most significant competitors were the Japanese.

In the appendix I have referred to a very good study recently published by Mr. Alexander Young, which in my view, at least, is a definitive study on Japanese trading companies. He concluded that the role in export expansion by the 10 top Japanese trading companies has been, without any doubt, the greatest contribution to the postwar Japanese economy.

I believe that this conclusion is somewhat at odds with Mr. Bergsten's.

I also note what is to me a rather surprising figure; that is, the top Japanese trading companies accounted in 1976, I believe, for slightly over 5 percent of the world export trade, as compared to approximately 17 percent for the United States. This perhaps highlights the success of the top trading companies.

I would like to highlight some of the points in my statement, which is much too long to try to read before this subcommittee. I think that probably one of the greatest problems in any discussion of the Webb Act and amendments thereto is that people rely very heavily on our disastrous trade account, and they leave it at that. As per the need for the exemption, I think its essential that two additional points with respect to the need must be made. They are elaborated at length in my statement.

OPPOSITE VIEWS OF OFFICIALS

One is with respect to the views of various officials at the Justice Department. I say various officials because this is one of the problems. U.S. exporters, as well as Webb-Pomerene members, listen to the head of the Antitrust Division, who says cooperation in export is fine, it doesn't affect U.S. consumers, it doesn't affect interstate commerce. At the same time, other representatives from the Justice Department are saying cooperative action, particularly Webb-Pomerene cooperative actions, are inherently anticompetitive because they spill over in terms of effects on domestic commerce.

I see these as confusing, to say the least, and perhaps even conflicting. At the same time, you have another Justice Department official—a former head of the Foreign Commerce Section,

Antitrust Division—who says export associations, more particularly, Webb-Pomerene associations, are really not so bad. They only seek to achieve minor economies of scale. This comforting type of advice is fine and dandy in itself; however, again it's very confusing for exporters.

In my statement, I further elaborate as to why our antitrust laws are unpredictible in the foreign commerce area. Again, this relates to the need for the exemption. They are not clear and concise.

Donald Baker, the former head of the Antitrust Division, has told us that guidance with respect to "collateral restraints" are too vague and confusing. Further, the "Antitrust Guide for International Operations" tells us that certain cooperative arrangements, particularly short-term cooperative arrangements, are fine, but prior to that passage—and this is often neglected—it says that export cooperation involves a substantial risk, because again, it may result in a spillover effect.

The second point with respect to need relates to what I said earlier with respect to Japan, and I certainly endorse what you said earlier with respect to other countries and how they have stimulated exports through governmental encouragement, et cetera. I think this point is essential: The Federal Trade Commission in its recently published study of the Webb-Pomerene Act, which I might add is very seldom referred to by the Justice Department officials, and in fact wasn't referred to Mr. Bergsten this morning—he referred to the old study—states that there's been a change, a tremendous change in foreign commerce today and that the change has adversely affected U.S. exporters due to the presence of what antitrust lawyers refer to as monopsonies—singular foreign buyers—I believe this condition underscores why the need is so critical in today's international trade environment.

ADMINISTRATION OF DRAFT

With respect to the bills themselves, rather than go through each bill—which I'd be glad to do upon request—as a general matter we would certainly encourage and endorse the expansion of the Webb Act to include services. We are going on record to say this once again; we've said it four or five times. We also believe very strongly that the administration of the exemption should be housed in the Department of Commerce. This would better reflect the balancing of national priorities.

As it is right now housed in the Federal Trade Commission, it is clearly viewed as an antitrust provision. Mr. Hodges addressed this point this morning.

And third, in the event an association's activities go beyond that which is permitted in its license, it should be the Department of Commerce which would be the principal body for remedying that transgression.

Then, as a last resort, the Federal Trade Commission, upon the advice of the Department of Commerce, should be brought in if judicial action is necessary. Thus, we would eliminate the Department of Justice as a governmental entity involved in the administration of the Webb Act. I elaborate this point further in my

statement as well. Primarily, this recommendation is based upon a confusion of who is actually in charge.

Also, as a general recommendation, we believe that the guidelines for determining whether an association meets the requirements of the act should only be issued by the Department of Commerce following some specifically provided consultation with the Federal Trade Commission. I also have in my statement set forth other, more specific recommendations; for example, making sure that the substantive antitrust violation language elaborated in each of these bills does not in any way put into jeopardy the *Minnesota Mining* decision.

I believe this concludes my recommendations. I should backtrack a bit, Mr. Chairman. We are not able at this time to comment on title II of your bill for the sole reason that we have not had an opportunity to go through our relevant committee to seek an opinion.

[The complete statement follows:]

STATEMENT

OF THE

NATIONAL ASSOCIATION OF MANUFACTURERS

BEFORE THE SUBCOMMITTEE ON

INTERNATIONAL FINANCE

OF THE

SENATE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

ON

S. 864, THE "EXPORT TRADE ASSOCIATION ACT OF 1979"
S. 1499 THE "EXPORT TRADE ACTIVITIES ACT"
S. 1663 THE "EXPORT TRADING COMPANY ACT OF 1979"

SEPTEMBER 17, 1979

My name is John F. McDermid. I am Assistant General Counsel of the National Association of Manufacturers (NAM), a voluntary association which represents 12,400 member firms which employ a majority of the country's industrial labor force and which produce over 75% of the nation's manufactured goods. The Association also represents 158,000 firms affiliated with the NAM through the National Industrial Council.

By way of background, I served for two and a half years as an investigative attorney and later advisor to the U.S. International Trade Commission. For two years, prior to my arrival at NAM last year, I served as a staff attorney, primarily responsible for international trade matters, with the Bureau of Competition, Federal Trade Commission.

NAM is grateful to the Subcommittee for this opportunity to express our views on S. 864, the "Export Trade Association Act of 1979,"

S. 1499, the "Export Trade Activities Act," S. 1663, the "Export Trading Company Act of 1979" and such additional general observations relevant to improving this country's export performance.

The NAM has been extremely active in urging Congress to seek ways of strengthening this country's ability to compete in world markets. These efforts have included appeals that the Export Administration Act be amended to reflect a clear national priority for export expansion as well as appeals that Congress establish a government trade reorganization plan similar to that proposed by Senators Ribicoff and Roth (S. 377). NAM has also gone on record several times in recent years[1] in support of retaining, clarifying, and expanding the Webb-Pomerene Export Trade Act of 1918 (hereinafter the Webb Act).[2] While we do not submit that any one of our recommendations in and of themselves are the panacea for curing this country's deteriorating international trade position, we strongly believe that each should be viewed as an integral part of any successful effort to promote U.S. exports.

The Webb Act--Background and Enforcement

S. 864 and S. 1499 are designed to amend the Webb Act by improving its effectiveness. Although the Act is a relatively unknown law which provides export associations a limited exemption from the Sherman Act, it has--almost since its inception--generated

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[1] See, NAM, "The International Implication of U.S. Antitrust Laws: An Issue Analysis of Global Economic Reality," (1976); Testimony of William L. Wearly, on behalf of NAM, Before the Senate Commerce Committee, September 28, 1978; Prepared Statement of the NAM Before the National Commission for the Review of Antitrust Laws and Procedures, November 17, 1978.

[2] 15 U.S.C. §§61-65.

considerable controversy within Congress,[3] by the government's antitrust enforcers,[4] and within the academic community.[5]

In order to understand why NAM believes that the Webb Act should be substantially revised to make it a more effective vehicle for promoting U.S. exports, it is first instructive to place the Act's origins and administration in perspective.

In 1914, Congress directed the newly formed Federal Trade Commission (FTC) to study the conditions affecting U.S. export trade.[6] A year later the FTC published an extensive two-volume report which explained that the low level of American export trade was due primarily to the difficulties U.S. firms were experiencing in their effort to compete against foreign businesses.[7] The FTC Report deplored the presence of large cartelized foreign buyers and sellers and the existence of "more effective [foreign] organizations"[8] which placed American exporting firms at a significant competitive

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[3]See, e.g., H.R. 4493, 78th Cong., 1st Sess. (1944) (urging repeal of the Webb Act); S. 1483, 93rd Cong., 1st Sess. (1973) and S. 1774, 93rd Cong., 1st Sess. (1973) (define "export trade" to include services and other major changes to strenghten the Act).

[4]See, e.g., Shenefield, John, Antitrust and Trade Regulation Report (BNA) No. 875, AA-3 (August 3, 1979) (supporting repeal of the Act); Letter of September 19, 1972 from Miles W. Kirkpatrick, Chairman, Federal Trade Commission, to O.V. Stovall, Director Int'l Div., General Accounting Office (supporting retention of the Act).

[5]There have been numerous, mostly critical, law review articles on the Webb Act. One list of such articles is set forth in the Nat'l Commission for the Review of Antitrust Laws and Procedures "Briefing Book" prepared by the staff for use by the Commission (June 13, 1978).

[6]15 U.S.C. §46(h)(1976)

[7]Report on Cooperation in American Export Trade (FTC) (1916).

[8]Id. Pt. 1 at 4.

disadvantage. The FTC's study further noted that the threat of Sherman Act prosecutions deterred exporters from carrying out collective efforts to challenge such cartels and large commercial entities. As a result, the FTC suggested that legislation be passed to remove this impediment.

Contrary to the contentions by many of the Webb Act's critics, Congress did not envision that U.S. cartels or huge combines of the type that U.S. exporters were facing in 1916 or are presently facing, would mushroom across the export business landscape.[9] It did not permit, for example, Webb Associations to combine with their foreign competitors.[10] Nor did Congress provide that all producers should combine to gain greater advantages in export trade. No new market power than that which was already present was created; that is, the kind of market power that would be undoubtedly necessary to establish effective export cartels. This Congressional intent has apparently been realized for most, if not all, Webb Associations have not been in a position to establish export cartels such that they command whatever price they dictate to foreign buyers. As stated by the former head of the Foreign Commerce Section, Antitrust Division, Justice Department:

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[9]See, 56 Cong. Rec. 7517 (1917); H.R. Rep. No. 1056, 64th Cong. 3d Sess. (1917); H.R. Rep. No. 50, 65th Cong., 1st Sess. 2-3 (1917).

[10]See, 56 Cong. Rec. 172 (remarks of Senator Pomerene) (1917) See also, United States v. Alkali Export Association where the court held that cartel arrangements are not sanctioned under the Act. 86 F. Supp. 59, 66-67 (S.D.N.Y. 1949).

> . . . since there are very few products which the U.S. alone accounts for a dominate share of the world export, most of the [Webb] associations do not have the power to achieve prices higher than the international market level.[11]

He also concluded that:

> An all-inclusive condemnation of [Webb Associations] ignores the fact that many export associations lack market power and exist merely to achieve minor economics of scale in selling abroad.[12]

In a similar vein, it is noted that contrary to the beliefs of many of the Webb Act's critics and contrary to the unsupported conclusion reached by the Antitrust Commission for the Review of Antitrust Laws and Procedures,[13] Webb Associations' functions are not limited to fixing prices and allocating markets, and, therefore, do not carry out classical cartel-type activities. As found in the recently published FTC analysis of the Act:

> It has been contended that setting prices and dividing business are the exclusive reasons that export trade associations exist. That does not appear to be the fact. While many associations do engage in one or other of these functions, they are often incidental to attainment of other commercial objectives.[14]

Only one association, the FTC found, is primarily involved in pricing, and for that sole association, their prices are recommended rather than binding to the members, and they "generally report price

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[11]Davidow, Joel, Legal Times of Washington, June 26, 1978 at 21.

[12]Davidson, Joel, remarks before the Center for Interdisciplinary Research Bielefeld, West Germany, July 16, 1979 at 28.

[13]Report to the President and the Attorney General of the Nat'l Commission for the Review of Antitrust Laws and Procedures. January 18, 1979, reprinted in Antitrust and Trade Regulation Report (BNA) No. 897, Special Supplement at 86.

[14]Federal Trade Commission, Summary and Analysis of Survey of Webb-Pomerene Associations (Nov. 9, 1978) at 8.

variances."[15] Rather Webb Associations perform a variety of other functions (all of which were intended by Congress) which permit them to lower their costs for export, including: (1) the establishment of sales agencies from offices in the United States, (2) the establishment of sales agencies from foreign sales offices or through foreign sales agents, (3) market research and analysis of export markets, (4) freight consolidation, rate negotiation and ship chartering, (5) credit information and collective facilities, and (6) a variety of other services that can best achieve efficiencies through joint action.[16]

Moreover, it is instructive to note the Antitrust Division, Justice Department's views with respect to the Webb Act as compared to their views with respect to non-Webb Act joint export activities. The Department has constantly urged Congress to repeal the Act because, *inter alia*, it is not needed on the basis that the antitrust laws as presently enforced might not prevent many joint export arrangements. In this regard, the Department tells U.S. exporters:

> We stress, whenever possible, that many joint export activities and other forms of international business cooperation are not prevented by our antitrust laws, since they produce no adverse effect on competitors and consumers in the U.S. (emphasis added)[17]

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[15] *Id.* at 9.

[16] *Id.* at 12.

[17] Shenefield, John "Antitrust Enforcement and the Antitrust Debate: Guarantors of the Free Enterprise System," remarks before Time Inc. Conference on Antitrust, May 7, 1979 at 12.

However, the Antitrust Guide itself notes that "Any joint venture may spill over into other areas," and therefore be prohibited.[18] Further, in addressing the Webb Act, a former chief of the Antitrust Division stated: ". . . the existence of an antitrust exemption for export associations inevitably affects competition at home and thereby affects the American consumer" (emphasis added).[19] More recently, the present Chief of the Foreign Commerce Section, Justice Department stated that they were "itching to sue" a Webb Association and that in certain cases domestic restraints are "virtually inevitable" as a result of Webb Association's joint export activities.[20]

To put this antagonistic Departmental position in perspective, it is instructive to look by analogy at other antitrust exemptions. For example, there is an exemption which permits the world's oil companies to sit down on a continuous basis to discuss the reallocation of world oil supplies in the event of another oil disruption of the type in 1973.[21] If the Department were to announce that this type of

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[18]U.S. Department of Justice, Antitrust Guide for International Operations (1977), reprinted in CCH Trade Regulation Reports, No. 266, Part II (February 1, 1977).

[19]Turner, Donald F., Int'l Aspects of Antitrust 1967: Hearings Before the Subcommittee on Antitrust and Monopoly of the Senate Committee on the Judiciary, 90th Cong., 1st Sess. 124 (1967)

[20]Rosenthal, Douglas, remarks before the President's Business Advisory Panel on Export Issues, Antitrust and Trade Regulation Report (BNA) No. 892, December 7, 1978 at A-16, 17.

[21]Energy Policy and Conservation Act of 1975, 42 U.S.C. §6272 (Supp. V 1975).

cooperative activity would inevitably have adverse effects on U.S. commerce, it is likely that the participating U.S. oil firms would be unwilling to take such antitrust risks and the exemption would be rendered impotent. Yet, in the case of this exemption, the Department has given its approval after essentially weighing the risks and balancing them against the public interest gains. Such a reasonable analysis is totally absent with respect to the export exemption.

Additionally, it is extremely misleading for the Department to state that many joint ventures and other joint export arrangements are lawful and that U.S. exporters are living under unfounded "perceptions" with respect to the notion that our antitrust laws impede various U.S. international transactions.[22] In this regard, several important points must be emphasized.

First, depending upon its audience, the Department would like us to believe that on the whole joint-export arrangements are free of antitrust scrutiny. A closer examination of representatives' views and the law reveals this simply is not the case. For example, as stated by a former Antitrust Division chief, antitrust lawyers themselves find that the standards for analyzing "collateral restraints" in joint ventures are "both too tough and too vague."[23]

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[22]See, e.g., Sierck, Alexander, Director of Trade Policy, Antitrust Division, remarks before the World Trade Institute, New York, September 6, 1979, at 2.

[23]Baker, Donald I., "The Antitrust Guide for International Operations: Two Years Later" (1979) at 11-12.

This important area of international trade activity is, he noted, "quite rightly subject to confusion and criticism and the [Antitrust] Guide" did nothing to resolve the issue.[24]

Second, although certain narrowly defined short-term joint ventures may be permitted by the Justice Department,[25] there is a failure to recognize that many long-term ventures are necessary to reap the benefits of developing and retaining profitable foreign markets. If properly administered and encouraged, the Webb Act could make a significant contribution towards realizing the gains from longer term projects where a high degree of dependence and continuity can be achieved.

Lastly, as indicated in the Guide itself, this country's antitrust laws--particularly as they apply to foreign commerce--are rarely susceptible to clear and concise rules for determining what is permissible conduct. As stated in the Guide:

> The United States antitrust statutes do not provide a checklist of specific, detailed statutory requirements, but instead set forth principles of almost constitutional breadth. This broad mandate frequently requires private parties, prosecutors and the courts to consider the overall purpose and effect of business arrangements in order to evaluate them under the antitrust laws.[26]

In a similar vein, with regard to the necessity for the exemption for antitrust enforcement reasons, in the important Minnesota Mining decision, the court set forth several activities which may be lawfully

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[24] Ibid.

[25] See, the Guide, supra note 18 at 21.

[26] Id.

carried out by Webb Associations.[27] Without the exemption, they would be curtailed or impossible, thereby inviting potentially crippling antitrust challenges. Further, it is important to note that, unlike most, if not all, other antitrust systems of the world,[28] any cooperative arrangements by American firms restraining U.S. export trade, even if such a restraint has no effect on interstate trade, would be prohibited. Also unlike other antitrust systems, under our antitrust laws if a nongovernmentally approved agreement restraining trade is harmless or even if it is found to be in the national interest, it is irrelevant to antitrust enforcement.[29] Thus, in one landmark case, for example, the Court found that "the art has rapidly advanced, production has increased enormously, and prices have sharply declined . . ." Yet, because "the suppression of competition . . . is in and of itself a public injury . . ." a violation was found.[30]

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[27] United States v. Minnesota Mining and Manufacturing Co., 92 F. Supp. 947 at 964-65 (D. Mass. 1950). For example, a Webb Association can refuse to deal with nonmembers, fix prices for goods bought for export, agree to export only through the association and charge higher prices to American exporters than to foreign distributors.

[28] See, letter and attachment of November 20, 1978 from Frank A. Weil, Ass't Sec'y for Industry and Trade, Dep't of Commerce, to the Antitrust Commission at 24.

[29] As observed by Mr. Davidow, "Other [countries] would have very little bias against private trade restraints per se, evaluating them after the fact in terms of their effects." supra note 12 at 28.

[30] United States v. National Lead Co., 63 F. Supp. 513 (D.C.N.Y.), aff'd., 332 U.S. 319; See also, Carnation Co. v. Pacific Westbound Conference, 383 U.S. 213 (1966).

The inconsistency and confusion in the Department's public views[31] and the inherent complexity of determining--under our system--the legality of export arrangements, have the predictable effect of inhibiting and even preventing firms from exporting and, more particularly, of clearly discouraging exporters from joining Webb Associations. Perhaps one of the more disturbing features of the Department's antagonism towards Webb Associations is its institutional refusal to balance the need to protect the public interest as it relates to competition against the equally important public interest of promoting U.S. export trade. It is nothing short of ludicrous to believe that this government has followed the Minnesota Mining direction that "ungrudging support to the policy of the Webb-Pomerene Act" should be given.[32]

The Need for S. 864 and S. 1499

That there is an urgent need for multiple legislative responses for relief from the deteriorating state of this country's export performance will not be belabored. It should be well known by this

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[31]We further note that even the Justice Department (reluctantly) recognizes that U.S. exporters are meeting unfair competitive practices in foreign commerce. To this, Assistant Attorney General Shenefield stated:

> Increasingly foreign governments are encouraging quasi-private and often secret international cartel activity...this activity can cause significant injury to important United States enterprises.

Letter from John Shenfield to the Honorable Jacob K. Javits, September 27, 1978. Yet, only one month or so earlier, the Antitrust chief stated that the Webb Act "is not at all necessary and should in fact be repealed." Antitrust and Trade Regulation Report (BNA), No. 875 at AA-3, August 3, 1978.

[32]Supra note 27 at 964.

time that our trade in manufactured goods, which represents two-thirds of the dollar value of U.S. exports, generally has been declining rapidly in both absolute and relative terms to major U.S. trading competitors. The statistics need no elaboration. From 1975 to 1978, the U.S. trade account in manufactured goods dropped from roughly a $20 billion surplus to a deficit of over $5.8 billion, while the surplus of Germany and Japan reached $51 billion and $72 billion respectively.

The President is acutely aware of this critical trade problem. In his September 26, 1978 export policy message,[33] he listed several proposals for improving U.S. export trade. One method of improving American competitiveness abroad would be to permit cooperative arragements. To this point the President said:

> There are instances in which joint ventures and other kinds of cooperative arragements between American firms are necessary or desirable to improve our export performance. The Justice Department has advised that most such joint ventures would not violate our antitrust laws, and in many instances would actually strengthen competition. (emphasis added)[34]

However, NAM was disappointed that the President failed to address the necessity of retaining and expanding the Webb Act. We have earlier explained why the exemption may be of considerable value in minimizing the risk of antitrust attacks. The procedural change recommended by the President, such as expediting the Business Review Procedure--as desirable as it may be--does not adequately recognize or respond to

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[33] Statement by President Carter at White House Briefing, Daily Report for Executives (BNA), September 26 1978.

[34] Id. at 3.

exporters' concerns. For example, the clearance offers no insurance against private suits, including those brought by state attorneys-general, and similarly does not protect exporting firms from a Federal Trade Commission proceeding.

Thus, although there may be a general awareness that our trade account is in need of repair, little concrete action is being taken. This being the case, the proposals being addressed by this Committee represent an extremely valuable step in the right direction. But, discussions relating to the Webb Act, as one of many proposals for change, too often miss what is considered to be an essential fact; namely, that U.S. exporters need the Act even more today than they did when it was passed.

As early as 1954, the American Bar Association's Antitrust Section concluded that the Webb Act should be retained not only because of the existence of foreign cartels but because of the new international commercial climate whereby:

> The existence of state controlled buying agencies, state monopolies and other foreign industrial combinations [make] it desirable that American exporters be permitted to combine among themselves in export associations.[35]

More recently, the FTC Webb Act report also concluded that the foreign commerce environment "suggests the likelihood of a new situation" from that which existed when the Act was passed.[36] After citing the same

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[35]Report of Committee on Antitrust Problems in International Trade, Proceedings A.B.A., Section of Antitrust Law, Annual Meeting 188 (1954).

[36]Supra note 14 at 13.

conditions as those found in the above ABA report, the FTC staff concluded that "public and private marketing power now appear to be of numerically equal competitive importance."[37]

As stated in a recent Harvard Business Review article, "today no industry is immune to competition from state enterprises" in which profit motives are irrelevant, bankruptcy nearly unheard of, dividends not paid and monopoly power achieved.[38] A strengthened Webb Act would considerably improve U.S. exporters' ability to deal with such monopsonistic foreign buyers.

It does not take a sophisticated international trade expert to identify which industrial nation is today exerting the greatest competitive pressures on U.S. exporters in foreign commerce. Indeed, in a 1976 survey of NAM's multinational members, an overwhelming majority stated that Japanese enterprises were their primary competitive rivals. To understand at least the basics as to how Japan has implemented its socio-economic strategies--particularly as they relate to its continuous export expansion drive--is to better understand the conditions American exporters are facing as they struggle to be competitive not only in Japan's home market but in third-market countries where Japan's presence is felt.

Accordingly, we have attached to this statement an Appendix which briefly explains the various factors which have greatly contributed to Japan's international trade strength. In particular, we focused on the

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[37] Ibid.

[38] Walters and Monsen, "State-owned Business Abroad: New Competitive Threat," March-April 1979 at 164.

Japanese mentality towards antitrust enforcement and how they view enforcement of their antitrust laws only within the context of broader national priorities, such as export expansion. The inter-governmental coordination that exist so as to carry out economic goals is particularly significant as a contrast to the lack of an effective U.S. policy-plan to achieve the same ends.

In reviewing the attached Appendix, one should also keep in mind that other industrialized nations have taken steps to improve their ability to compete against the historic presence of U.S. multinationals and the newer presence of Japanese multinationals. For example, within the European Economic Community it has been noted:

> Even within the [EEC] Commission there are those who feel the Community's best bet for trade and economic parity with the U.S. and Japan is to build up giant corporations capable of matching the foreign multinationals head on.[39]

Simply stated, then, while this country takes either no steps or counterproductive ones vis a vis U.S. export trade, the remainder of the developed world is taking measures that assume U.S. enterprises are retaining their competitive superiority, thereby placing our ability to gain entry into foreign markets in even greater jeopardy. In this regard, it must be made clear that NAM does not believe this country should emulates the Japanese "guided free enterprise" experience. Rather, we believe that this country can take positive steps towards improving U.S. firms' ability to compete in foreign commerce without sacrificing our fundamental socio-economic and democratic principles. By giving the Webb Act a transfusion of the types being considered by

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[39] European Community May-June 1978 at 38.

this Committee, these principles will not be jeopardized for each proposal provides sufficient remedies to assure that competition within this country's borders is adequately maintained.

Terms of S. 864 and S. 1499

Both Senator Danforth's (S. 864) and Senator Roth's (S. 1499) bills have as their primary purpose the rejuvenation of the Webb Act so that it can make a more meaningful contribution towards improving U.S. firms' ability to compete internationally, thereby increasing U.S. exports.

Although the bills differ in various details, the common thread to both is the expansion of the Webb Act to include services. Consistent with our earlier statements relevant to the Webb Act, we strongly endorse this amendment. By including within the Act's coverage the service industries, more U.S. firms, particularly small and medium sized ones--would be able to furnish the combination of products and services which are so frequently required by large foreign buyers.

More particularly, this amendment would likely have considerable significance to many small and medium sized architectural, engineering and construction firms that would not--working individually--be able to participate in bids on foreign projects because of the extremely high costs involved in bid preparations and feasibility studies.

Furthermore, any such expansion of the Act will beneficially impact the export of manufactured goods as well, since the disadvantages often suffered by U.S. exporters due to the design of specifications by foreign engineering or construction firms would thus be largely neutralized. Moreover, as is discussed more thoroughly in the Appendix

to this statement, the "services" provision is particularly needed today in view of the dramatic increases in "industrial cooperatives" and trading companies which cross national frontiers and are able to provide foreign buyers "full service" packages within a relatively short period of time.

Lastly, we note that the Antitrust Commission recommended that if the Act is retained it should be expanded to include services and that Congress, in passing the Trade Act of 1974 (19 U.S.C. 2101) declared that service industries are part of the definition of "export trade."

With respect to more specific changes proposed in S. 864 and S. 1499, NAM strongly endorses the underlying principles behind both bills, namely to make the Act more effective. We submit that the following endorsements and suggestions would more effectively carry out this purpose.

1. We endorse Section 2 of S. 864 whereby the administration of the Webb Act would be transferred to the Department of Commerce

The Webb Act should not be administered by antitrust enforcers. As enforced today, the Act is treated not as a bill to stimulate export trade but as a bill to assure that antitrust concerns are carried out. By providing Commerce the primary responsibility for the Act's administration, the originally enacted Congressional intent to permit companies to work cooperatively in gaining access to foreign markets is reinforced. Although Commerce will not be in a position to provide any blanket antitrust immunities to export firms since an Association's activities could always be diverted from their original purpose, it is clear that the prime determiner for passing on their conduct will be a

Department whose mission is to promote export trade rather than a Department solely concerned with carrying out another, frequently conflicting national policy. This proposal would further relieve many of the fears associations have over Justice Department intervention and would alleviate the confusion as to which government entity actually has responsibility for monitoring the Act. We reject, therefore S. 1499's proposal to give the Federal Trade Commission exclusive jurisdiction over the Webb Act even though the principle of providing one government agency oversight responsibility has merit. In this regard, however, we recommend:

2. The Federal Trade Commission should be given exclusive jurisdiction to bring a district court action if an association's activities are believed to violate the Act. Actions by third parties should only be processed through the Secretary of Commerce by means of the adjudicative procedures set forth in Section 2(b)(2) of S. 864.

By giving the FTC sole governmental responsibility to prevent abuses of the Act, Webb Association members would feel more assured that the policies of only one antitrust enforcement agency are controlling. Further, the FTC has the requisite know-how, experience, and personnel familiar with the Act so that it could effectively deter violations. Moreover, the S. 864 procedures available to injured third parties would effectively protect such parties from further violations while at the same time protect Webb Associations and their members from potentially crippling treble damage actions.

3. That Webb Associations must serve or promote export trade should be clarified so that whatever rules and regulations that are promulgated do not undermine the purpose of the Act.

Both the Danforth bill (Section 2(a)(1)) and the Roth bill (Section 4 and 5(c)(1)(A)) essentially condition certification upon an association's export promotion accomplishments. We do not envision that this provision, read literally, and as we believe intended, will cause problems since individual exporters join Webb Associations for the purpose of improving their export performance. However, we strongly oppose the suggestion by critics of the Act to condition the exemption upon a showing of need, and it is feared that this provision might be susceptible to a "need" interpretation. Thus, either the bill itself or the legislative history should make clear that the export promotion provision is intended only to assure what undoubtedly will take place anyway; that is, that Webb Associations have as their primary function the stimulation of export trade.

4. We urge the Committee to reexamine the substantive conditions that associations must meet before qualifying for an exemption under both S. 864 and S. 1499 and compare them to the three conditions presently set forth in the Webb Act.

We query why the two proposals change in different respects the criteria presently set forth in Section 2 of the Act. We have not carried out an in-depth analysis as to the effect the language might have on future enforcement. Thus, we can only raise the question whether the proposals would in any way jeopardize the various activities considered lawful by the Court in Minnesota Mining. This judicial guidance is unique to the history of the Webb Act, is relied heavily upon by antitrust counsel advising Webb Associations, and should not, perhaps inadvertently, be threatened by what could initially be thought of as a minor change in the statute.

5. Guidelines that must be issued for purposes of determining whether an association meets the requirements of the Act should only be issued by the Department of Commerce following a mandatory request for the views of the Federal Trade Commission and any other interested persons.

As presently drafted, S. 864 would require the FTC, Justice and Commerce Departments to issue guidelines, and S. 1499 would require only the latter two agencies to issue guidelines. We believe, however, that both mandates: (1) would likely result in duplications of efforts, (2) invite conflicting priorities, and (3) would considerably confuse and probably deter many firms from taking advantage of the exemption. In order to avoid these undesirable consequences, we suggest that the Act be amended such that the Commerce Department would be solely responsible for issuing guidelines. In order for it to carry out this responsibility, the Act should require the Department to consult with and seek advice from the FTC as well as interested persons so that antitrust concerns can adequately be reflected in the guidelines.

6. Section 4 of the present Webb Act broadens the jurisdiction of the FTC Act to include acts outside of the United States. Any modification of the Act should clarify the relationship between enforcement of Section 5 of the FTC Act and potential violations of the Webb Act.

There has never, to the best of our knowledge, been a clarification of the relationship between Section 5 of the FTC Act and activities by Webb Associations. Can, for example, the FTC conduct an investigation of a Webb Association's activities under the vague "unfair methods of competition" language found in Section 5? There appears to

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be some ambiguity on this point. In the process of amending the Act the issue may gain considerably more significance than it has under the present law. We urge, therefore, that the Committee consider the potential problems associations' would have if Section 5 enforcement were to supplement whatever violation language may be adopted.

Terms of S. 1663

S. 1663, entitled the "Export Trading Company Act of 1979"--like the earlier discussed proposals to reform the Webb Act--is intended to permit U.S. exporting firms to carry out certain cooperative activities in export trade. Title II of S. 1663 is designed to provide export companies various incentives to carry out the purposes of the Act. It is our understanding that S. 1663 is intended as an additional proposal to promote U.S. export trade rather than as a replacement for the proposals to amend the Webb Act.

We are prepared today to comment in detail and favorably with respect to Title I, the provision relating to the establishment of export trading companies. With respect to Title II, which deals with tax and finance aspects of the proposed new trading companies, we are not prepared at this time to make specific comments, although we wish to commend this imaginative and innovative approach designed to promote greater use to trading companies.

Title I

Many of the comments provided earlier in this statement relevant to S. 864 and S. 1499 are also applicable to our views on S. 1663. Thus, we strongly endorse the exclusive role the Department of Commerce would play in being the primary governmental body responsible for export promotion proposals such as those under consideration before this Comittee. Similarly, we further support the S. 1663 definition of

export trade, which includes trade or commerce in goods as well as services. We also support the flexibility provided the Secretary of Commerce to remedy certain export trading company activities that may go beyond those set forth in its license. Thus, for example, that a trading company may file an amended application or modify its organization before resort is made to termination of its license. These provisions, therefore, permit the trading company to continue operating, but only within the confines of its license.

Lastly, we endorse the exclusive right of the United States to bring a judicial action in the event the licensed export company's activities violate one or more of the three antitrust criteria set forth in proposed Section 106 of the bill. This avoids, then, the crippling effect of a private treble damage action while still assuring that U.S. competition is maintained. Judicial action by the United States should, however, be available only after the Secretary's efforts to remedy transgressions under Section 103(c) are exhausted.

The only additional suggestion we have at this time relates to Section 106, the antitrust provision. More particularly, Section 106 (a)(2) provides that a licensed trading company may not engage in activities that constitute or result in "an unfair method of competition against a domestic competitor." As noted earlier, we are concerned that the extraordinary breadth of this phrase may result in considerable enforcement uncertainty to firms wishing to join as a certified trading company. We believe that subsection (a)(1) adequately protects U.S. competitors by prohibiting a "substanital restraint of trade within the United States" and that subsection (a)(2) is, therefore, unnecessary to achieve the purposes intended. Moreover, we note that the proposal's definition of antitrust laws does not include the Federal Trade Commission Act, yet the "unfair method of competition" provision is extracted from that trade regulation law. We suggest, then, that deletion of subsection (a)(2) would better reflect the bill's intention to confine itself to antitrust violations as that term is consistently used.

APPENDIX

JAPAN: A DILEMMA FOR U.S. EXPORTERS

The Relationship Between Government and Business in Japan

It is generally recognized that much of Japan's economic growth is attributed to their success in incorporating into their own system the most efficient characteristics of the free enterprise and non-market economy systems. The literature on Japan's phenomenal socio-economic development uniformly seeks to explain the unique relationship between government and business--a relationship which is enormously complex and which frequently defies any rigid comparative analysis to other States' economic systems. However, in searching for a phrase that might best define Japan's economic policies, Ezra Vogel's "guided free enterprise"[1] appears to be the most accurate.

The key government entity responsible for effectuating streamlined industrial policies is the powerful Ministry of International Trade and Investment (MITI). The Ministry plays a persuasive role in assuring that Japanese industries satisfy the need of the State. By way of comparison to our own system, MITI's influence ". . . is closer to that of the Department of Defense in the United States than the Department of Commerce."[2]

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[1]Vogel, Ezra F., "Guided Free Enterprise in Japan," Harvard Business Review, May-June 1978.

[2]Johnson, Chalmers, Japan's Public Policy Companies, (1978) at 23.

Among its many responsibilities, MITI plays an active role in assuring that domestic enterprises continue to be keen international rivals. Overproduction, underproduction, inefficiencies, etc., are governmentally scorned as being against the best interest of industry at large and, therefore, the people it serves.

Although Japanese scholars differ as to the extent of the government's role in the Japanese businessman's affairs, there appear to be seven areas where assistance is furnished:

1. through fiscal measures, including long-term interest funds to particular industries,

2. through tax relief or suspensions intended to stimulate exports, rationalize industry, and foster technological development,

3. through government subsidies,

4. through "direct allocation or rationing systems" which permit the government "to fix the amounts of a product that a factory may produce,"[3]

5. through licensing and approval authority to foster industries,

6. through direct government investment in industry through specially tailored legal entities and,

7. through "administrative guidance" by which the government intervenes to carry out public needs, such as the need to stimulate export trade.

There are numerous examples as to how MITI has executed its self-perceived belief that it is the protector, developer, and promoter of Japanese manufacturing industries. For example, the

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[3] Id. at 22. See also, The Foreign Policy of Modern Japan (1977), at 227-279.

Japanese computer industry, which as one MITI official commented is "as important to Japan as the defense industry to the United States,"[4] is a "national policy industry" and has received considerable governmental assistance and guidance; so as "to increase its strength relative to foreign computer manufacturers."[5] Recently, a Forbes magazine article on Japan's remarkable computer industry growth concluded that:

> The Japanese Government forced computer makers to cooperate. Such cooperation would, of course, be impossible in the U.S. But to the Japanese, economic survival takes precedence over antitrust laws.[6]

As a result, according to the United States Japan Trade Council, "Japan's computer industry has reached technological parity with its American counterparts in the development of hardware."[7] However, because it is believed that Japan's software is behind American industries, with "guidance" and subsidizations MITI is encouraging the major Japanese manufacturers to jointly work together on a five-year software development plan.[8]

In contrast, what has the United States done to assist its computer industry? We do not believe the U.S. government should be encouraging through subsidization for example, this country's

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[4]Chalmers, supra note 28 at 58, reference to remarks of Amaya Naohiro, "Immediate Economic Problems between Japan and the United States and Their Long-Range Prospects," March 6, 1973.

[5]Caves, Richard, and Uekusa, Masu, Industrial Organization in Japan, (1976), at 51.

[6]"That Old Nobushi Spirit," Forbes, July 23, 1979 at 47.

[7]United States Japan Trade Council "Trade Round Up" No. 23, July 27, 1979.

[8]Ibid.

computer industry. Experience reveals that rather than incentives, one points to the Justice Department's recent 10th anniversary "celebration" of its case against IBM for monopoly and attempting to monopolize. Since the case began in 1969, IBM has examined approximately 26 million pages of government documents and Justice has had access to approximately 60 million pages of IBM documents. Estimates are that IBM has spent nearly $60 million defending the suit.

The steel industry in Japan underwent a similar experience as that which is being carried out with the computer industry. Several years ago MITI undertook a successful campaign to promote large scale mergers in Japan's steel industry so as to put an end to "cutthroat internal competition."[9] According to one Brookings Institute study, before the creation of the mammoth New Japan Steel Company, MITI "actively promoted cartel arrangements to divide new capacity among five leading firms."[10]

Competition Policies in Japan

The discussion thus far necessarily leads to the question of how Japan carries out its competition policies. Japan's antitrust laws are embodied in the "Law Relating to Prohibition of Private Monopoly and Methods of Preserving Fair Trade." There are numerous similarities between the prohibitions under Japanese antitrust laws and U.S. antitrust laws. Although a considerable amount of antitrust enforcement information is unavailable, it

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[9]Johnson, supra note 2 at 59-60.

[10]Caves, supra note 2 at 59.

appears that there exist a potentially powerful Antimonopoly Law established in Japan but that "there is very little empirical evidence of it being utilized thus far."[11] There are also substantial differences in enforcement and multiple ways for the government to circumvent the broad prohibitions set forth in the antitrust provisions. The enforcing agency--the Fair Trade Commission--does not have a history of adjudicating cases, imposing fines, or imprisoning violators. If the government antitrust authorities believe certain anticompetitive conduct should be condemned, even though it has some authority to act, the party subject to the prohibition has considerable room to maneuver for, "unlike MITI and the Ministry of Finance, the FTC does not have the arsenal of carrots and sticks that the ministries have."[12] This could not be more unlike the relationship in this country between, for example, the Department of Commerce and the Department of Justice.

There appears to be little disagreement that enforcement of the antitrust laws is often subsumed by other national policies such as the promotion of exports or stabilization of domestic trade. Perhaps representative of Japan's mentality in this regard, a former Vice-Minister of MITI stated:

> It is dangerous to determine a priori that free competition is a good thing and cooperation is a bad thing. There is desirable competition and useless competition within the general category of free competition.[13]

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[11]Rabinowitz, Richard, Current Legal Aspects of Doing Business in Japan and East Asia, (ABA Pub., 1978) at 136.

[12]Id. Haley, John Owen, "Antitrust in Japan: Problems of Enforcement," in Current Legal Aspects of Doing Business in Japane and East Asia at 124.

[13]Johnson, Chalmers, supra 2 at 250 (quoting Vice-Minter Sahashi).

To U.S. policymakers this perspective is well known. In 1978, a Deputy Assistant Secretary for Economic Business Affairs, State Department, observed before this Subcommittee that:

> The Japanese Government does not view competition as essential but rather as one of a number of industrial policy tools. Enforcement of the law allows a degree of selectivity, and there are special exemptions in the national interest. Export cartels are common. The Japanese have taken the view that as trade is liberalized, domestic companies must be large enough to be competitive with U.S. and European firms. (emphasis added)[14]

(a) Exemptions from the Antitrust Laws

Even if the Fair Trade Commission were to actively enforce the antitrust laws, it would be hamstrung by the multiple laws unrelated to antitrust that permit or even encourage anticompetitive conduct. The laws are considered essential ingredients for implementing broad socio-economic objectives and are particularly designed to assist particular industrial sectors when the need arises.[15] These "special" laws provide one of the basic methods for establishing cartels in Japan. According to one Japanese authority they permit ". . . large enterprises . . . to combine, fix prices and allocate markets"[16] and are applicabe to entire industries. By 1961, the 634 private section "societies" that blossomed as a result of one broadly structured exemption were particularly effective in helping industries better compete in export markets.[17] According to a 1964 report in the Oriental Economist:

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[14]Hormats, Robert D., Prepared Statement of March 9, 1978 Before the Subcommittee on Int'l Finance, Senate Committee on Banking, Housing and Urban Affairs, Part 3 at 68.

[15]The Foreign Policy of Modern Japan, supra note 3 at 254.

[16]Hadley, Eleanor, Antitrust in Japan (1970), quoting Professor Kanazawa at 376.

[17]Ibid.

> Of the 1,002 cartels in existence at March 31, 1963, 90% were in connection with medium and small operations, and with foreign trade. Of the medium and small enterprise cartels, 591 have been formed under the Medium and Small Enterprise Organization Law, and 95 are those formed under the Environment Sanitation Proper Management Law. Of the Foreign trade cartels, 194 have been formed under the Export and Import Trade Law, and 11 were established under the Export Marine Product Industry Promotion Law. Fifty-five agreements are shipping conferences in the ocean freight area under the Marine Transportation Law.[18]

As a result, it has been estimated that in 1962, a staggering 42.4% of Japan's export trade was cartelized.[19] This percentage does not include administration guidance cartels in which the government utilizes extra legal devices whereby it suggests what an industry should produce or what its pricing practices should be. There are still other types of cartels that are permitted as exemptions from the Antimonopoly Law. They are generally referred to as "depression" or "naturalization" cartels. Both cartels require FTC approval. At times, the FTC has been quite liberal in permitting depression cartels, and they have covered rather large segments of industries. For example, in May 1978, the Japanese Diet approved a special bill for assisting industries suffering from a recession such as the minor steel (dependent on electric and open heat furnaces), aluminum smelting, synthetic textile, and others such as the corrugated paperboard liner industry.[20] Occasionally, the FTC will permit a depression cartel to avoid the alternative approach whereby MITI establishes a cartel through its

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[18] Id. at 377. See also, Caves, supra note 2 at 147.

[19] Hadley, Eleanor, supra note 16 at 380.

[20] See, "International Weekly Edition of Nihon Keizai Shimbun," (May 16, 1978) at 1-23.

administrative guidance plans.[21] This reluctance to directly confront MITI may be explained by the power MITI has, for "the FTC has not been able to attack the cartels of large enterprises promoted by MITI . . ."[22] The total number of cartels exempted from the Antimonopoly Law numbered approximately 1,000 from 1964 to 1976.

There is also a broad policy of controlling industry through so-called "administrative guidance." Sometimes such guidance is carried out by the relevant government agency responsible for enforcing the law which has been tailored as an exemption from the antimonopoly law. Other times administrative guidance is based upon "request" or upon "advice" by MITI to export manufacturers to limit production for a period of time so as to offset depressed conditions due to "excessive competiion. "[23] Thus, such guidance will often not be based upon any explicit statutory authority and is generally directed towards "the creation of efficient scale plants as well as fearful of excess capacity and ensuing price competition."[24] The success of this and other types of guidance[25] has affected a wide range of industries from

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[21]Caves, supra note 2 at 146.

[22]Id. at 151.

[23]Johnson, Chalmers, "MITI and Japanese International Economic Policy," The Foreign Policy of Modern Japan, (1977) at 254.

[24]Caves, supra note 2 at 54.

[25]There is also guidance through "mediation" whereby MITI is placed in a brokerage role in which a high government official acts as a guide and coordinator with industry. Examples of such guidance include the merger of the Prince Automobile Company with Nissan Motors. See, Johnson, Chalmers, supra note 23 at 255.

rayon thread to vinyl rope to computers. "Only the strongest of business leaders dare to take issue with the government" when it issues its guidance "suggestions."[26]

Lastly, in the private sector there are approximately 20,000 registered trade associations, many of which focus on commodities designed for export. These associations differ substantially from our own in that they publish price lists, maintain statistics on inventories and production, and try to get a "consensus as to production, prices, and future prospect."[27] According to a Brookings Institute study, "The behavior of industrial prices alone, reflected in paralleled announcement of price changes by rival sellers, indicated a great deal of collusive price-fixing in Japanese industry."[28] The FTC has seldom investigated the activities of trade associations and has never undertaken any broad-based review of their conduct. Only recently have FTC officials announced that they will be examining the competitive consequences of trade associations' joint activities.[29]

(b) Export Cartels

At the outset, in view of the significance of Japan's export trade and that such trade involved small, medium, and large enterprises, it is clear that what appears to be domestic

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[26]Hadley, Eleanor, supra note 16 at 386.

[27]Address by Fair Trade Commission Chairman Hashiguchi Before the ABA International Trade Committee, Washington, D.C., June 22, 1979 at 7.

[28]Caves, supra note 2 at 151.

[29]Supra note 27 at 7.

cartels--whether they be defined as naturalization, depression, administrative guidance, etc.--have an effect on the ability of U.S. exporters to compete in Japan's home market and in third-country markets where Japan competes.

In Japan, export cartels have served not only to promote efficiencies and to exert greater market power in export trade but, according to an OECD study, are an "integral part of [Japan's] trade policy."[30] It has been the government's plan "to permit export cartels when combined efforts are needed to improve the quality of commodities produced by small firms." The OECD Report concluded: "As these criteria are very broadly defined, there is an imminent danger of abuse by the cartelized firms."[31] Once many of these export cartels have achieved their objective; that is, "a sound development of export trade,"[32] they may be advised by MITI and the FTC to discontinue. Thus, the "extensive use of export groups or, as they are more realistically termed, export cartels,"[33] may in fact be terminated at some point by the government but only after they have succeeded in their mission. According to the OECD study, in 1974 there were 141 export cartels covering everything from binoculars to bicycles.[34]

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[30]OECD, Report of the Committee of Experts on Restrictive Business Practices on Export Cartels, (1974) at 49.

[31]Ibid.

[32]Ibid.

[33]Fugate, Wilbur. Foreign Commerce and the Antitrust Laws, (1973) at 252.

[34]Supra note 30 at 60-70.

Japan's Trading Companies

Recently an army of U.S. antitrust enforcers and their Congressional allies have been urging the legislators to return this country to a simpler "horse and buggy" entrepreneurial way of life. In the face of these efforts, one finds that the Japanese have a history of implementing opposite policies, including the development of large trading companies, initially established to assist their home-market exporters to better compete against large U.S. and European multinationals. The Japanese trading companies are unique to world trade and have met with extraordinary success. According to Alexander Young in his recently published definitive treatise on Japan's trading companies, their "role in export expansion has been without any doubt, their greatest contribution to the postwar Japanese economy."[35] Therefore, any discussion as to American firms' ability or inability to compete worldwide must take into account the presence and success of Japan's trading companies.

Japan's trading companies were founded upon the simple notion that what can be done in combination is better than that which can be done independently.[36] That commercial coordination has succeeded is evidenced by the staggering size and apparent efficiencies of the ten largest Japanese trading companies. In

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[35]Young, Alexander K., The Sogo Shosha: Japan's Multinational Trading Companies (Westview Press, 1979) at 129.

[36]Hadley, Eleanor supra note 16 at 148.

1976, they grossed nearly $133 billion in sales, carried out 56.4 percent of Japan's total exports and 55.6 percent of its imports. "Their export and overseas (i.e., third-country trade) transactions accounted for slightly over 5 percent of world [export].[37] The two largest trading companies (Mitsui and Mitsubishi) each had sales in excess of $30 billion in 1977. As of March, 1974, the six largest companies had more than 600 subsidiaries: two-thirds in Japan and one-third in foreign markets.[38] These subsidiaries rely heavily upon their parents for supplies of raw material and for sales of manufacturers. In September, 1976, there were approximately 61,000 full-time Japanese employed by the top ten trading companies. They have accumulated unbelievable amounts of capital[39] and have a network of global offices in both developed and developing countries in which the parents exercise remarkable managerial control. The largest trading companies have communications networks that can only be characterized as phenomenal and which are so highly sophisticated and effective that a major, complex international joint venture transaction can be handled within a few days.

Although generally believed to be solely service oriented "brokers," the modern day Japanese trading company is engaged in a much greater variety of businesses. For example, Mitsubishi

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[37]Young, Alexander, supra note 35 at 4.

[38]Id. at 46.

[39]Id. at 71.

Corporation is involved not only in the purchase, sale, export, and import of products ranging from iron and coal to pulp and paper, but it is also engaged in the worldwide development, production, and manufacturing of such goods. As a result, the major trading companies have greatly contributed to Japan's economic growth by strengthening the competitiveness of the nation's exports.

The trading firms also provide an impressive array of "bonuses" to their clients which have aided significantly in the non-price competitiveness of Japanese exports. A staggering amount and number of credit, loans, and loan guarantees are furnished. This is accomplished through significant low-interest loans taken out by the trading companies from commercial banks. This procedure is particularly helpful to the many small and medium sized exporting firms who are clients of the mammoth trading companies and who could not otherwise afford the higher interest rates that would be demanded through direct loans. Moreover, the trading companies furnish a significant amount of marketing, technological, and even legal and political information, "usually free of charge to their customers."[40] Such benefits lead to "substantial cost reductions for the manufacturer customers of the trading companies."[41]

With the guiding hand of goverment, the trading companies have been permitted and in fact encouraged to merge amongst themselves. In the 1960's, the firms first entered consumer industries and than in the 1970's began carrying out extensive marketing of high

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[40] Id. at 67.

[41] Id. at 67.

technological products. Recently, because more and more Japanese companies have begun to resort to direct marketing and therefore rely less upon trading companies as intermediaries, they began not only significant diversification efforts but total integration strategies. Thus, new areas of supply and demand were sought with upstream (processing, wholesale distribution, and retail sales) integration. As a result, the ability of Japan's enterprises to compete internationally in both competitive and noncompetitive terms has been substantially improved due to the presence of trading companies.[42]

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[42] Id. at 132-136.

Senator STEVENSON. Thank you, sir. We welcome your comments on title II when you have had a chance to consult the relevant committee.

Mr. McDERMID. We will submit that for the record.

[Information not submitted in time for publication.]

VIOLATES GATT CODES

Senator STEVENSON. Good. Secretary Bergsten indicated that the provisions of S. 1663 would violate the GATT codes on subsidies. Any comments on that testimony and how this might be corrected? Has the Chamber looked into it?

Mr. BOYER. The Chamber has not looked into that yet, sir.

Mr. McDERMID. The NAM is focusing on that issue.

Senator STEVENSON. All of you, of course, if you do have comments now or later, we would like to have them on that problem.

Dr. HUSZAGH. I believe, Mr. Chairman, that Governor Busbee of Georgia, who is Chairman of the MTN subcommittee for the President's Export Council, will soon seek clarification of the kinds of tax incentives, permitted under the code. He is interested in full reciprocal treatment so we get the benefits we thought we were going to get under the MTN.

Senator STEVENSON. I think he'll discover that the answer sometimes depends on who he talks with.

Dr. HUSZAGH. Yes, sir?

Mr. WALDMANN. Mr. Chairman, I would point out, as you recall, the MTN codes do not apply to service industries and, therefore, to the extent that any assistance is provided to service industries by legislation of the type being considered here, we would not be adversely affected by the new subsidy code.

Senator STEVENSON. I think the comments today, especially yours on services, are very well taken. Many of us are guilty of neglecting services and we'll have to take them into account in our consideration of all export proposals.

Now, there was another proposal that would substitute for EDA and SBA financing of trading companies for the Eximbank loan

guarantees and loans as proposed in S. 1663. Any comments on that suggestion?

Dr. HUSZAGH. I do think that if the trading corporation concept really works, it could bridge all of these various financial programs. Some of the programs you mentioned are now a little restrictive, although the anticipated stockholders in the trading corporation could use the trading corporation to determine when and how they can get production loans. We ought to more closely examine these various programs to see how they fit into a total export matrix. I think this needs to be done since programs like SBA and EDA are here to stay, at least for some period of time.

Senator STEVENSON. Similarly, it was suggested that trading companies might be an alternative to DISC. Do you have something on that possibility, since the administration might be a little more interested in supporting trading companies if it got its way on DISC?

[No response.]

Senator STEVENSON. Offhand it looks to me as if it would force companies to run their exports through trading companies instead of DISC's, which might not be acceptable. I'd welcome further thoughts on that as well.

ARE PROHIBITIONS NECESSARY

All of the bills would prohibit the use of Webb associations to export patents and technology. It wouldn't actually prohibit exports of technology, but do you feel that those prohibitions are necessary? Any comments from the witnesses?

Mr. MCDERMID. Mr. Chairman, I think I'd like to elaborate on that in writing, but my initial response to it is that there is a feeling in the business community that that should not be the case, that it should include patent licensing. From the perspective of one who has some antitrust experience, however, it might raise more questions than it's worth. The patent and licensing area is hundreds of times more complicated from an antitrust perspective than many others. It may undermine the thrust of the bill. That's only my initial gut response, if you will. And I would like to elaborate on that later.

[Information not submitted in time for publication.]

Senator STEVENSON. I think Dr. Huszagh made the point, too, that we may have left a number of antitrust questions unanswered in all these bills, including the trading company legislation. So if there are further suggestions from all of you as to how to answer those questions, eliminating uncertainty in the future, we'd be glad to have them, too. I don't know if you've looked into those questions, Mr. Waldmann, but maybe you could help us on the antitrust.

Mr. WALDMANN. Yes, Mr. Chairman, I might point out again that many of the service industries are regulated by one or more Federal or State agencies, and there are further complications with respect to antitrust in those regulated industries.

Senator STEVENSON. I have a statement here from the Governor of Puerto Rico, which is supportive of S. 1663. It will be entered into the record.

[Statement follows:]

STATEMENT OF CARLOS ROMERO BARCELÓ, GOVERNOR OF PUERTO RICO

Mr. Chairman and Members of the Subcommittee, I am very pleased to set before you my thoughts on Chairman Stevenson's legislation, S. 1663, to allow for the creation of trading companies in the United States. While I recognize the merits of the two other bills under discussion, I am most interested in the concepts embodied in S. 1663 and wish to confine my comments to that piece of legislation.

As Governor of Puerto Rico I represent 3.5 million American citizens living in Puerto Rico to whom exports are essential for the well-being of our Island, and also serve as Chairman of the Sub-Committee on Foreign Relations and International Negotiations of the National Governors' Association's Committee on International Trade and Foreign Relations. It is in this capacity that I wish to present my testimony to you today.

We in the NGA have been increasingly aware of the importance of trade and export to the economic health of our communities, our States, and our nation. Over the course of the past year, under the leadership of Governor George Busbee of Georgia we have investigated, or are in the process of investigating such diverse aspects of trade as export licensing, tax credits for research and development, disincentives to export for small and medium sized firms, trade reorganization, and the related problem of adjustment assistance.

Our interest stems from the vital role that exports play in our economy. The U.S. Department of Commerce estimates that one out of nine manufacturing jobs is based on export sales while the U.S. Department of Labor states that for every one billion dollars worth of trade 40,000 jobs are created. If we use last year's export level of $144 billion we find that almost 6 million jobs existed in our work force as a result of exports. Aside from job creation, export sales are important due to the taxes local and Federal governments collect on sales of products made by American firms whether sold domestically or internationally.

In spite of the obvious importance of exports to our economy, we have not done well in insuring that our once positive trade advantage remains. We have allowed other nations to enter the international marketplace and substantially rewrite the rules of the game. To date, our response has been half-hearted and at times seemingly contradictory. In a word; inadequate.

Each year has seen a slippage in our share of world trade. In the last eight years our share of world trade has decreased from 18 percent to 12 percent. Six points may not seem like much, but the 33 percent decline is enormous. For each *one-tenth* of one percentage point decrease we lose, according to your own figures; $1 billion in trade or 40,000 jobs, $2 billion additional GNP and $400 million in Federal tax revenues. Therefore, in the past eight years we have lost a potential $60 billion in trade or 24,000 jobs; $120 billion in additional GNP; and $24 billion in Federal tax revenue.

I find these figures frightening, and I hope you do as well. That is why I am pleased that Congress is now responding to our need to increase exports, and I am particularly happy that the Chairman has introduced his bill on trading companies. The ideas set forth in this bill have considerable merit and come at a very appropriate time. I support your efforts wholeheartedly.

Very few firms in the United States actually export. There are over 250,000 manufacturers in the U.S. Only 20,000 to 25,000 of them engage in sales overseas or 10 percent of the total. Of these twenty-five thousand, 107 account for 46 percent of all U.S. exports. As the Chairman himself has noted, the U.S. Department of Commerce has indicated that there exists between 18,000 and 20,000 *more* firms which could export profitably but at present do not. Many of these small and medium sized firms have a relatively thin profit margin, limited personnel, and therefore lack the resources to deal with the intricacies of the international market. It is unlikely that they will ever do so without additional help.

Trading companies could provide this help. By pooling resources, sharing information, directing expertise, conducting studies, following up market opportunities, and providing needed financial assistance, trading companies could significantly increase the volume of our exports.

While I believe the legislation is necessary in our attempt to create a better climate of trade and take advantage of the new MTN agreements, I am concerned that the bill makes no mention of the crucial role the individual states can play in the formation of trading companies and in promoting exports in general.

Many states already take an active role in promoting overseas sales by operating offices of export promotion as part of the State government. More than half of the States maintain representation overseas. Such States as Texas, Illinois, New York,

North Carolina, and Georgia run exemplary programs resulting in millions of dollars of additional export sales yearly. Given the interest, and in many cases, expertise which already exists, States should be encouraged to undertake some of the functions of trading companies.

Aside from the expertise two additional advantages can be brought to bear. First, by using State governments, there is a decrease on the reliance of Federal resources, and a corresponding closer relationship between the local government and the firms which operate within its borders. Second, the inclusion of State units means an increase in the number and type of resources dedicated to exports. Along with this comes an element of competition which, I believe, will further aid in the selling of American goods and services overseas.

It is my understanding that current laws encourage States to undertake many of the functions inherent in the trading company concept, but there is no specific mention of this in S. 1663. As a result of this lack of a clearly defined inclusion some confusion might result. It is my hope that the bill could be amended to specifically say that the legislation in no way limits States from undertaking those functions of the trading company concept which are essential for the promotion of a State's economic health, safety and welfare.

In closing let me commend Senator Stevenson for the good work he has done in this area. But, I should also like to provide a word of caution. Liberalized trade, as envisioned by the new Multilateral Trade Negotiations, cuts both ways. Not only will we be afforded the opportunity to enter foreign markets, but our trading partners will be freer to enter ours. If we do not adequately prepare ourselves to take advantage of the new rules we will find the potential gains from the MTN flowing to those who are better organized and better prepared. The formation of trading companies is one step in these preparations, but we have much to do.

Thank you.

Senator STEVENSON. Also, since Secretary Bergsten brought up the subject of bank participation in trading companies, I will enter into the record a list of foreign banks which own or otherwise participate in trading companies.

[List follows:]

FOREIGN BANKS OWN TRADE INTERMEDIARIES

Hong Kong & Shanghai Banking Corp., Hutchinson Whampoa Ltd.—33 percent (with control), Marine Midland Bank—51 percent (proposed).

Jardine Matheson & Co., Jardine Fleming & Co.—100 percent, Matheson & Co. Ltd.—100 percent.

Midland Bank Limited, London American International—75 percent, Export Credit Corp.—75 percent, Drake America Corp.—75 percent, European American Bank—one of six shareholders.

Barclay's Bank International, Tozer, Kemsley & Millbourn—24.5 percent.

Societe Generale, Sogexport—100 percent. Interests in other trading companies managed by Sogexport.

Credit Lyonnais, Essor PME—80 percent.

Banque Nationale de Paris, COMPEX—Joint venture with Inchcape & Co.

Banque de Paris et des Pays-Bas, Scoa—25 percent.

Banco de Brazil, Beke Co.—100 percent.

Mitsubishi Bank, Mitsubishi Corp.—Keiretsu affiliation.

Mitsui Bank, Mitsui & Co.—Keiretsu affiliation.

Fuji Bank, Marubeni Corp.—Keiretsu affiliation.

Senator STEVENSON. Three are Japanese.

Thank you. We are very grateful to you for your help. With that, the subcommittee is adjourned. We'll meet tomorrow, the time has been changed. No longer in the morning but at 2:30 in this room.

[Whereupon, at 12:45, the hearing was adjourned.]

EXPORT TRADING COMPANIES AND TRADE ASSOCIATIONS

TUESDAY, SEPTEMBER 18, 1979

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON INTERNATIONAL FINANCE,
Washington, D.C.

The subcommittee met at 2:30 p.m., in room 5302, Dirksen Senate Office Building, Senator Adlai E. Stevenson III (chairman of the subcommittee) presiding.

Senator STEVENSON. The subcommittee will come to order.

This afternoon, we continue our hearings on S. 864, 1499, 1663, and 1744.

S. 1663 would authorize the creation of U.S. trading companies. Our first witnesses are Members of the Senate.

I am delighted to welcome them to our hearing. Do you have any preference as to who should go first?

STATEMENT OF THE JOHN C. DANFORTH, U.S. SENATOR FROM THE STATE OF MISSOURI

Senator DANFORTH. Thank you. I have a prepared statement but I will not read it but just submit it for the record if that's satisfactory with the chairman.

Senator STEVENSON. The full statement will be entered in the record as though read.

[The statement follows:]

Senator DANFORTH. Mr. Chairman, first, I wish to commend you for holding these hearings not only on S. 864, legislation to amend the Webb-Pomerene Act introduced by myself and my colleagues, Senator Bentsen, Senator Javits, Senator Mathias, Senator Chafee, and Senator Heinz, but also on your trading company bill, S. 1663, and Senator Roth's amendments to the Webb-Pomerene Act, S. 1499. Under your leadership the Subcommittee on International Finance has displayed over the years an agressive willingness to seek and recommend steps which our Government should take to improve U.S. export performance.

In its report, "U.S. Export Policy," issued earlier this year, your subcommittee recommended that the Webb-Pomerene Act be amended—in particular to permit service industries to set up export trade associations under the provisions of the act. The report further recommended that the Department of Commerce be directed both to assist and encourage the formation of export trade associations and that the Department of Justice clearly specify, by

guidelines and advisory opinions, its enforcement intent under the statute.

The Webb-Pomerene law has been on the books since 1918. The law exempts from U.S. antitrust laws any trade association established for the sole purpose of engaging in export trade so long as the association does not restrain trade within the United States, restrain the export trade of any domestic competitor of the association, or influence artificially prices within the United States of commodities of the class exported by the association.

Even though the Webb-Pomerene law was passed over 60 years ago, it has been the subject of very little court construction and therefore only minimal judicial guidance exists. It has, however, been the subject of growing controversy as to its effectiveness in being a spur to U.S. export performance.

The critics of Webb-Pomerene contend that the law is unnecessary because an export agreement which produces no adverse effect on U.S. trade or competitiors would not violate the Sherman Act even if there were no Webb-Pomerene exemption. They also contend that, in practice, the act encourages an anticompetitive spillover effect on domestic markets and weakens U.S. credibility in international circles where we advocate strong international antitrust rules.

To understand these contentions, it is helpful to examine the history behind the enactment of Webb-Pomerene. In 1916, the Federal Trade Commission issued a report, mandated by the Congress, recommending legislation that would permit cooperation among domestic exporters. The recommendation was based upon the finding that American firms were forced to compete in the international marketplace with powerful foreign cartels. American firms, it was believed, had to be free to combine their efforts if they were to compete successfully with their foreign counterparts. It was also argued that U.S. export trade would be encouraged by allowing combinations of small American firms to share among themselves the high costs of marketing and transporting their goods in the international marketplace.

What has happened since passage of the law in 1918? At their high-water mark between 1930 and 1935, Webb-Pomerene associations numbered 57 and accounted for approximately 19 percent of total U.S. exports. Today, the number of associations has dwindled to 33 and their share of total U.S. exports has dipped to less than 2 percent. The Webb-Pomerene Act, over its 60-year history, has not realized its goal of significantly increasing the volume of U.S. export trade and particularly exports by small business.

Opponents of the act contend that today the vast majority of Webb associations are formed not because of the existence of competing foreign cartels, but rather to allow U.S. firms in concentrated markets to legally fix the price at which they sell overseas. I do not believe this to be the case, but if it is—and I would be happy to hear the evidence—then the solution is not to kill Webb-Pomerene. Instead, the Congress should reexamine the act with an eye toward making it a useful vehicle to encourage U.S. business to share the expense if export trade where otherwise they would not be inclined to export at all.

I believe there are three main reasons for the poor showing of Webb-Pomerene associations in the act's 60-year history. First, the U.S. business community, particularly small-to-medium size businesses, traditionally has placed top priority on tapping the vast domestic market and has not focused on the prospects overseas. Second, the ever-expanding U.S. service industry has been excluded from qualifying for the act's antitrust exemption. And, third, our antitrust enforcement agencies have not, until recently, afforded the business community any clear guidelines as to their enforcement intent under the statute. Therefore, with the business community perceiving governmental hostility toward Webb associations, there is a natural reluctance to form such an association and run the risk of facing Government and private antitrust litigation.

S. 864, the legislation I introduced along with a number of my colleagues, addresses these concerns. The bill would do the following:

It would require the Commerce Department to assist and encourage the formation of Webb associations. I would hope this effort could be concentrated on small and medium size businesses where the thrust and purpose of the association would be the joint sharing of mutually incurred costs.

It would expand the law to include the service industry.

It would clarify the language of the statute establishing antitrust immunity.

It would establish a process whereby companies desiring to combine for joint exporting purposes would be precleared by the Department of Commerce. This procedure would provide immunity from antitrust prosecution until the charter is revoked by applicable action on the part of the government.

Again, Mr. Chairman, thank you for holding hearings on this legislation. I would hope that after your committee has considered the arguments carefully, you will report a bill which encompasses the spirit and intent of S. 864. I would like to submit for the record, Mr. Chairman, a more complete section-by-section explanation of S. 864.

[Reprint of section-by-section analysis of S. 864 may be found at p. 115.]

I would also like to take the opportunity to comment briefly on S. 1663. It is my understanding that this legislation would encourage the formation of Japanese-type export trading companies. The Department of Commerce would be responsible for licensing of the companies. The formation of these companies would be encouraged by providing for loans and guarantees for startup costs; allowing participation by banks; placing limitations on antitrust liabilities; and affording the trading companies special tax treatment. I am told the formation of an export trading company and the use of the Webb-Pomerene Act to charter a joint venture are not mutually exclusive.

I commend the chairman of the International Finance Subcommittee for a thoughtful and far-reaching proposal.

Thank you.

Mr. Chairman, this month is the first anniversary of the President's announced national export policy. To date, really not much has materialized. It's obvious that something has gone very sour with our trade position.

That is, this month will be the 40th consecutive month of American trade deficits. Prior to 1971, we never had a deficit in trade in this country.

Now, we have gotten to a position where in 1977 and 1978, we had $30 billion deficits. It's easy to blame this on the energy situation. That certainly is a serious situation. But it can't really carry the whole burden of the blame.

In 1977, for example, Japan imported 100 percent of its petroleum. We import about 50 percent of ours. Japan imported 100 percent and yet maintained a $17.3 billion surplus in trade.

So our performance has been very bad. It's not solely a result of energy. The three of us here at the table are cosponsors of a bill to amend the Webb-Pomerene Act.

We are all members of the Senate Finance Committee. We spent on and off a couple of years working on the trade bill that eventually came out of the multilateral trade negotiations.

It was the hope in that trade bill to provide Americans with a better opportunity to compete in world markets and reduce some of the so-called nontariff barriers to trade.

We believe something more than that is necessary and therefore, we have introduced S. 864 to amend the Webb-Pomerene Act.

The Webb-Pomerene law has been on the books now for most of this century and yet, there have only been a total of something like 200 Webb-Pomerene associations ever formed.

I think there are only 30-some that are now in existence. It really has fallen into disuse.

The purpose of this bill, explained more fully in the statement, is to make the Webb-Pomerene Act more attractive, to provide the Commerce Department with an affirmative obligation to go out and promote the Webb-Pomerene Act and provide that it covers services, which is not now the case. It's simply manufactured goods.

And to provide further for a preclearance procedure so that companies that are interested in forming Webb-Pomerene associations can get a preclearance and, therefore, immunity until their clearance is revoked, so they have a greater degree of assurance that they are not going to get blindsighted once they enter into such an association.

Export Trade Association Act of 1979

Section - By - Section

Explanation

Section 1. Short Title: Export Trade Association Act of 1979

Section 2. Findings and Declaration of Purposes:

Section 2 sets forth the findings and declaration of purposes.

Section 3. Definitions

Section 3 defines the pertinent terms. The definition of "export trade" is expanded from the definition contained in the Webb-Pomerene Act (15 U.S.C. 61-66) to include services. The term "service" means intangible economic output, including, but not limited to business, repair, and amusement services; management, legal, engineering, architectural, and other professional services; and financial, insurance, transportation, and communication services. The term "export trade activities" includes any activities or agreements which are incidental to export trade. The term "association" refers to any combination of persons, partnerships, or corporations, all of which must be citizens of the United States or created under the laws of any State or of the United States. A foreign controlled subsidiary created under the laws of any State or of the United States, however, cannot be a member of the "association". The term "antitrust laws" means all antitrust laws of any State or of the United States.

Section 4. Exemption from Antitrust Law

Section 4 provides that an export trade association certified according to the procedures set forth in this Act is exempt from the

application of the antitrust laws provided that the association and its export trade activities (1) serve to preserve or promote export trade; (2) neither result in a substantial restraint of competition within the United States nor constitute a substantial restraint of the export trade of any domestic competitor of the association; (3) do not unreasonably enhance, stabilize, or depress prices within the United States; (4) do not constitute unfair methods of competition against domestic competitors; (5) are not reasonably expected to result in the consumption or resale in the United States of goods or services exported by the association; and, (6) do not constitute trade or commerce in the licensing of patents, technology, trademarks, or know-how, except as incidental to the sale of goods or services exported by the association or its members. Section 4 establishes that federal agencies shall have standing to bring an action against an association for failure to meet the requirements set forth above. Section 4 makes provisions for persons to petition a federal agency to bring an action against an association. It also describes the remedies available to the federal agency and creates jurisdiction in the federal courts for an action brought under this section.

Section 5. Redesignation and Amendment of Sections 3 and 4

Section 5 provides for conforming changes to Sections 3 and 4 of the Webb-Pomerene Act. Section 3 of the Webb-Pomerene Act is redesignated as Section 5 and is amended to prohibit an association from engaging in unfair methods of competition against domestic competitors only.

Section 6. Administration; Enforcement; Reports.

This section strikes Section 5 from the Webb-Pomerene Act and inserts in lieu thereof a new Section 5 and eight new sections.

A new Section 5 establishes the procedure for applying for certification as an export trade association. It describes the information to be included in the application for certification, most notable of which are an explanation of the conditions, circumstances, and factors which make an association useful for the purpose of promoting export trade; a description of the methods by which the association conducts its export trade; and any other information which is reasonably available to the applying parties and which is necessary for the certification of the prospective association. The new section requires that the Secretary certify an association within 90 days after receiving the association's application if the Secretary determines that the association, its members, and proposed export trade activities meet the requirements listed in the new Section 3. The section provides for an expedited certification process. An amendment procedure is another feature of this section. If there transpires a material change in circumstances which would cause an association to fail to meet any requirement of the new Section 3 of the Webb-Pomerene Act, the association must apply to the Secretary for an amendment of its certification within 30 days of the date of the material change. If the association fails to apply for an amendment within the thirty-day time period, its certification will be void as of the date of the material change. The Secretary, after notifying the association, may (1) require that an association's certification be amended, (2) require that the organization or

operation of the association be modified to correspond with the association's certification, or (3) revoke, in whole or in part, the certification of the association upon a finding that the association or its members or its export trade activities do not meet the requirements of the new Section 3.

A new Section 6 to the Webb-Pomerene Act requires that the Secretary, the Attorney General, and the Chairman establish guidelines for purposes of determining whether an association, its members and its export trade activities meet the requirements of the new Section 3.

A new Section 7 to the Webb-Pomerene Act stipulates that every certified association shall submit to the Secretary an annual report setting forth the information required in the application for certification.

A new Section 8 to the Webb-Pomerene Act establishes within the Department of Commerce an office to promote and encourage to the greatest extent feasible the formation of export trade associations through the use of provisions of this Act.

A new Section 9 to the Webb-Pomerene Act provides for automatic certification for existing export trade associations registered under current law. In order to obtain automatic certification, an existing export trade association must file an application for certification within 180 days after the date of enactment of this Act.

A new Section 10 to the Webb-Pomerene Act provides for the confidentiality of the information contained in an association's application for certification, application for amendment of certification, and annual report.

A new Section 11 to the Webb-Pomerene Act authorizes the Secretary of the Treasury to require an association to modify its operations so as to be consistent with future international obligations of the United States set by treaty or statute.

A new Section 12 to the Webb-Pomerene Act authorizes the Secretary, in consultation with the Attorney General and the Chairman, to promulgate such rules and regulations as are necessary to carry out the purposes of this Act.

A new Section 13 to the Webb-Pomerene Act requires the President seven years after the date of enactment of this Act to appoint a task force to examine the effect of the operation of this Act on domestic competition and on the United States' international trade deficit and to recommend either continuation, revision, or termination of the Webb-Pomerene Act.

Section 6 of the Webb-Pomerene Act is redesignated as "Section 14. Short Title.".

Senator STEVENSON. Senator Bentsen?

STATEMENT OF LLOYD BENTSEN, U.S. SENATOR FROM THE STATE OF TEXAS

Senator BENTSEN. Thank you very much, Mr. Chairman.

Coming here to testify before you is a bit like preaching to the choir in view of the amount of work you have done in trying to encourage exports for our country. I am delighted to join my colleagues in the sponsorship of this particular bill.

You have one quite similar in that regard. Here we have a staggering trade deficit of some $30 billion. One of every eight jobs today in the United States depends on export sales.

I am a little more optimistic than my colleague in this regard. I think we are beginning to make some headway. We did things in the Finance Committee working together to try to encourage exports and to see we were put on the same basic footing as some of our competitors.

That is what we are talking about here with Webb-Pomerene. That particular act, when passed back in 1918, was to help exports. It didn't turn out that way because of some of the ambiguities and threat of action by the Department of Justice and concerns of businesses in trying to go together in these associations.

We are trying to clarify it, deal with specificity, and assist putting these associations together to encourage American industry to be able to compete with some of these cartels we are seeing in other countries coming here and really giving themselves quite an advantage over some of our smaller companies.

Here we are trying to encourage the joint effort of our companies in services sold abroad and we think this is a positive step, one that

the General Accounting Office back in 1973 said we ought to be doing and we are only just now getting to it.

So we urge very strongly that this committee, with its great interest in encouraging exports for our country, give favorable consideration to this legislation.

I would also like, if I may, to introduce my full testimony for the record.

Senator STEVENSON. Thank you. That will be entered in the record as though read.

[The statement follows:]

Mr. BENTSEN. Mr. Chairman, I appreciate the opportunity to testify before your subcommittee in support of S. 864, the Export Trade Association Act of 1979. This legislation, which amends the Webb-Pomerene Act of 1918, would correct deficiencies in existing law so that American firms can engage in joint export activities, enabling them to benefit from economies of scale and pooling of market information. This legislation would enable American business to compete on a more equal basis with foreign competitors.

Enactment of this legislation would be a positive step to help increase exports and reduce the staggering trade deficit of some $30 billion. One in every eight jobs in U.S. industry now depends on export sales. Increased exports produce new job opportunities for the American people.

Mr. Chairman, in my testimony this morning I would like to make several points:

The Webb-Pomerene Act was enacted in 1918 to encourage joint export activities but ambiguities in the law and the threat of Justice Department prosecution have frustrated the objectives of that act. S. 864 would help carry out the intent of existing law.

A 1973 report of the General Accounting Office recommended that Congress clarify the Webb-Pomerene Act to help increase exports.

U.S. businesses face competition from hundreds of foreign cartels. Our companies cannot operate effectively at such a competitive disadvantage.

The United States is currently facing a staggering trade deficit with serious adverse consequences to the domestic economy.

It is essential that Congress now adopt a positive national export policy to reverse this trend.

Modification of the Webb-Pomerene Act to encourage joint export ventures, particularly for small- and medium-sized firms, can be an important component of such a positive national export policy.

WEBB-POMERENE ACT OF 1918

Mr. Chairman, I would like to briefly review the rules under existing law.

The Webb-Pomerene Act exempts from U.S. antitrust laws any association established "for the sole purpose of engaging in export trade," as long as the association does not restrain trade within the United States, restrain the export trade of any domestic competitor of the association, or influence prices within the United States of commodities of the class exported by such association.

Under present law, the Federal Trade Commission investigates the activities of joint export ventures if the FTC has reason to believe such acitivities have an adverse impact on domestic competition. If the export association fails to make any modifications recommended by the Commission, the FTC refers the matters to the Attorney General.

However, the Department of Justice is not precluded from bringing a suit against an association independent of the FTC and prior to the FTC recommending an adjustment of an association's practices. Such suits can be brought against an association without its being aware of violating the act and without its having an opportunity to adjust its activities.

The purpose of the act was to encourage American manufacturers and producers to compete in foreign trade. However, the vagueness of the law, the lack of adequate certification procedures and the threat of Justice Department prosecution have discouraged the use of this export promotion vehicle.

PROVISIONS OF S. 864, THE EXPORT TRADE ASSOCIATION ACT OF 1979

S. 864 has several features which would help restore the original intent of the Webb-Pomerene Act.

First, it expands and clarifies the act's antitrust exemption for export trade associations.

Second, it transfers the administration of the act from the FTC to the Department of Commerce.

Third, it establishes a specific preclearance procedure within the Commerce Department with time limitations for certification of export trade associations.

Fourth, it creates within the Department of Commerce an office to promote the formation of export trade associations.

Fifth, it makes the provisions of the Webb-Pomerene Act explicitly applicable to the exportation of services.

Under S. 864, an export trade association would be exempt for all antitrust laws, if the association (1) serves to preserve or promote export trade; (2) neither results in a substantial restraint of competition within the United States nor constitutes a substantial restraint of the export trade of any domestic competitor of the association; (3) does not unreasonably enhance, stabilize, or depress prices within the United States; (4) does not constitute an unfair method of competition against domestic competitors; (5) is not reasonably expected to result in the consumption or resale in the United States of goods or services exported by the association; and (6) does not constitute trade or commerce in the licensing of patents, technology, trademarks, or know-how, except as incidental to the sale of goods or services exported by the association or its members.

S. 864 establishes procedures for applying for certification as an export trade association. The bill describes the information to be included in the application for certification such as an explanation of the conditions which make an association useful for the purpose of promoting export trade and a description of the methods by which the association conducts its export trade.

In order to avoid excessive delays, the bill requires that the Secretary of Commerce certify an association within 90 days after receiving the association's application if the Secretary determines that the association, its members and proposed export trade activities meet the requirements of the act.

The bill also specifies a procedure for amending certifications. If there is a change in circumstances which would cause an association to fail to meet any requirement of the Webb-Pomerene Act, the association must apply to the Secretary for an amendment of its certification within 30 days of the date of the material change. If the association fails to apply for an amendment within the 30-day time period, its certification will be void as of the date of the material change.

In addition, the Secretary, after notifying the association, may (1) require than an association's certification be amended, (2) require that the organization or operation of the association be modified to correspond with the association's certification, or (3) revoke, in whole or in part, the certification of the association upon a finding that the association or its members or its export trade activities do not meet the requirements of the law.

Mr. Chairman, these procedures will help provide greater certainty for American businessmen and prevent abuses.

IMPORTANCE OF S. 864

The need for prompt enactment of this bill is clear.

In 1973 the General Accounting Office recommended that the Webb-Pomerene Act be clarified to help U.S. exports.

The GAO stated:

> Government and industry officials believe that Webb-Pomerene associations offer a means for expanding exports by aiding U.S. businesses to compete in international commerce if the uncertainties in operating under the act were eliminated * * *. We believe the critical U.S. export situation demands a positive approach—encouraging the formation and operation of Webb-Pomerene associations—so that the full potential of the Webb-Pomerene Act in promoting exports can be realized.

The 1973 GAO report concluded that export trade associations can be monitored to insure that the associations do not monopolize commerce within the United States:

> A Justice study and our discussions with FTC officials indicate that exploitation of the domestic market and the unfair advantage against competing domestic firms can be adequately policed under existing provisions of the Webb-Pomerene Act.

S. 864 would enable American business to compete on a more equal basis with foreign competitors. U.S. firms must constantly compete against the joint export activities of our competitors. Foreign cartels, often aided by their governments, effectively meld their activities into strong competitive forces, particularly in bidding on major construction contracts. It is not uncommon for foreign governments to actually direct the merger of several private business interests into one entity to restrict possible competition among these companies.

As a result, foreign businessmen are much freer to cooperate and join forces to compete in international trade than are U.S. businessmen. For example, in 1970 the United Nations reported over 300 foreign cartels operating overseas in competition with U.S.

firms; in 1971 the Organization for Economic Cooperation and Development reported over 500 foreign cartels.

STAGGERING U.S. TRADE DEFICIT

With a trade deficit of about $30 billion last year, Congress must act promptly to formulate a comprehensive export promotion policy. Our enormous trade deficit contributes to inflation, destroys the value of our currency and creates doubt about our free market system. Fundamental improvement in our trade position is critical to a healthy American economy.

The following statistics dramatize the seriousness of the problem. Prior to 1976, the largest U.S. trade deficit for a full year was the $6.4 billion deficit in 1972. In comparison, the trade deficits in 1976, 1977, and 1978 were $9 billion, $31 billion and an estimated $35 billion, respectively. The U.S. share of total manufactured exports of 15 industrial countries fell from almost 30 percent in the late 1950's to 19.2 percent in 1972. It rose to 21.1 percent in 1975 but has declined steadily since then, falling to 18.9 percent by the first quarter of 1978, the lowest since mid-1972.

Over the past 20 years, our exports have grown at only one-half the rate of other industrial nations.

The United States, once the world leader in international trade, is now in danger of falling to third place in exports of manufactured goods. West Germany took the lead in that field in 1970 and now Japan is almost even with the United States with respect to exports of manufactured products.

According to Commerce Department officials our current deficit of $30 billion can reach the staggering level of $40 billion a decade from now. This would indeed be alarming.

IMPORTANCE OF ADOPTING A POSITIVE NATIONAL EXPORT POLICY

Earlier this year Congress approved the implementing legislation for the multilateral trade negotiations—MTN. Since the entire purpose of MTN is to facilitate international trade and reduce inequities in the trading system, it follows that our own laws such as the Webb-Pomerene Act should be consistent with this objective and with our international obligations. We can be sure that our competitors in the international marketplace will not overlook any opportunity to give their exports a competitive edge.

In fact, Business Week magazine stated:

> The United States must look out for its exporters and push their interests in every way it can. If this country does not claim its fair share of expanding world markets, it can be sure that aggressive exporters from Europe and Japan will.

That same point was emphasized by the President's Special Trade Representative, Ambassador Robert Strauss, when he stated:

> The MTN is only a first, immediate, necessary step that will enable us to solve the problems over the next 5 or 10 years. We've now got to develop an export thrust.

Mr. Chairman, in conclusion it is clear that American business and Government must take a much more aggressive role in world trade. The United States has made a major effort to formulate the MTN and we should not forgo opportunities for the United States

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to take maximum advantage of these efforts. Clarification of Webb-Pomerene is one such opportunity.

The GAO study said:

> Because of uncertainty over possible antitrust implications, clarifying the provisions of the Webb-Pomerene Act would help create an environment in which U.S. firms might more readily join together and present a complete package, including financing, technology, equipment, and commodities, in competing for large-scale projects abroad.

Mr. Chairman, I urge the committee to act favorably on this important legislation.

Senator STEVENSON. If you can remain, we can complete the statements and then have some questions and answers and discussion.

Senator BENTSEN. I don't have a better offer, just an earlier one. [Laughter.]

Senator STEVENSON. Let's see if we can't continue with the statements before you have to accept the next offer.

Senator Chafee.

STATEMENT OF JOHN H. CHAFEE, U.S. SENATOR FROM THE STATE OF RHODE ISLAND

Senator CHAFEE. Thank you very much, Senator Stevenson.

I want to say how much I appreciate the efforts that you have made in the area of trade. You have been one of the leaders in trying to help our export situation.

We are in a very strange situation in the United States. In a bizarre reversal of the old-time charges of capitalist, industrialist, imperialism the United States is now the largest importer of manufactured goods and the world's largest supplier of corn, wheat, and farm products. This is completely different from what we learned about England durings the days of its empire.

The revisions to the Webb-Pomerene Act, that our bill makes, as Senator Danforth mentioned, will improve and expand the act in a variety of ways.

One change I would like to touch on is the inclusion of service industries in the act. Until a couple of years ago, the United States ranked first in its share of the construction market overseas.

That was 1976. Due to a variety of circumstances—including the Foreign Corrupt Practices Act and others—now the United States construction industry is in fifth place, trailing Japan, Korea, West Germany and Italy.

The National Construction Association has projected a sales increase of $2 billion annually if it could operate as a Webb-Pomerene association.

This is just one area that I think holds considerable promise in the export market for the United States.

I join my colleagues in urging favorable consideration and close attention by this committee to the legislation which we have submitted in S. 864.

Senator STEVENSON. Thank you. I want to thank all of you again and commend you for your attention to the trade deficit and for the proposals which you have made.

This is the second day in this hearing on those proposals and also S. 1663. During the first day, there was widespread support for

your suggestions for revision in the Webb-Pomerene Act for the reasons you have mentioned, including specially the strong feeling that the service industries ought to be made eligible for the Webb-Pomerene exemptions.

As you have pointed out, you can take out all the trade in manufactured goods—all the trade with OPEC, all the oil imports—and we still ran a deficit.

We ran a deficit in manufactured goods. It's fashionable to blame it on oil, but that is only one cause of the trade deficit. I think Senator Danforth mentioned other countries are more dependent on imported oil and food and ran a surplus.

They maintain relatively stable levels of wages and lower rates of inflation. The United States last year, depending on how you calculate it, suffered a $34 billion trade deficit.

There are those who think you can rely on a sinking dollar and no growth to rectify the trade deficit, but you have recognized more is necessary, including structural response from the United States.

I think it goes beyond export promotion. It goes very much to the larger question of the competitiveness of the United States in a competitive global marketplace.

You are all members of the Finance Committee. Senator Bentsen also chairs the Joint Economic Committee which made extremely significant proposals recently for improving the productivity of U.S. business and competitiveness, and would have an effect on the trade deficit.

I am optimistic about the prospects for your proposals. They will certainly receive sympathetic consideration by this subcommittee.

I hope that the other proposal to which you have not addressed your comments, S. 1663, will also receive your sympathetic consideration.

If reported by this committee, it must go to the Finance Committee. That is the proposal to authorize the creation of trading companies.

Other countries have them. Not only Japan. Many of the European countries have trading companies. The French have a slightly different formulation. But they have companies which can represent small as well as large businesses in all parts of the world every day, spiraling market opportunities, providing a full range of services and goods, putting together the packages, including financing.

All to our disadvantage. This would give the United States the same tool, trading companies. But to get them started, the evidence to date indicates they will need some help with startup costs.

So we propose in S. 1663 some tax concessions, which is what brings in the Finance Committee. Have you had a chance to review S. 1663?

It is complementary, it's not inconsistent but goes beyond the Webb-Pomerene suggestions in order to encourage trading companies.

Senator BENTSEN. I have not but I shall look forward to studying it. This may end up one of the more even deals I have been into up to date.

Senator DANFORTH. My staff now is reviewing your bill and the discussions to date are very favorable. I want to take a more

careful look at it. I think in this whole trade area, we have to look at a variety of approaches. This is true with many problems. There is not a single bill which suddenly can be enacted and solve everything.

A lot of it is a question of emphasis and a question of trying to focus our attention as a country on being much more aggressive in an area where we have been very, very unaggressive. Our Government has been unaggressive. Our STR, for example, we just had hearings in the Finance Committee on the new nominee, Governor Askew, but since the completion of the trade agreement in Geneva, the whole shop more or less folded, with very few exceptions.

I don't think that is true in other countries. I don't think they conclude a trade bill and just go home. I think the trade is something that on a day-in and day-out basis has very careful consideration. That is not the case in the United States. It has to be so. The Webb-Pomerene bill is a piece of a big picture, and your bill may well be too.

I would like to look at it more carefully. I am favorably disposed to that type of approach.

Senator BENTSEN. If you would excuse me, Mr. Chairman.

Senator STEVENSON. Thank you, Senator Bentsen. The Commerce Committee estimated there were about 20,000 businesses in the United States that were potential exporters that have no export business at all. Your proposals would have the effect of making it easier to export and so would the trading company proposal. Trading companies could represent both large and small businesses by providing services they otherwise can't obtain.

So that is all I expect and hope for, is that S. 1663 will, if reported by this committee, receive some attention in the Finance Committee. Some changes in the Internal Revenue Code may be necessary for success of American trading companies.

Senator Mathias, we welcome you.

STATEMENT OF CHARLES McC. MATHIAS, U.S. SENATOR FROM THE STATE OF MARYLAND

Senator MATHIAS. Thank you, Mr. Chairman. Sorry I was delayed.

I might ask if I could submit my statement for the record as though read.

Senator STEVENSON. The statement will be entered in the record.

Senator MATHIAS. I would only add that I think, as the Chairman himself knows and has expressed very eloquently on a number of occasions, we have some storm signals in this whole area of trade. In 1978 our exports were 6.7 percent of gross national product, while imports stood at 8.4 percent, which is certainly more than just a storm signal. We are into the storm. When you look at what has happened in the last 20 years, when our share of international commerce has fallen from just below 30 percent to below 20 percent, it's a very serious symptom. If we could ascribe that purely to the increasing prosperity of the rest of the world, perhaps we could put up with it. But, in fact, the rest of the world is doing more trade and we are doing less. These proposals will help us correct that problem.

Senator STEVENSON. One of the ironies is that in the name of competition we sometimes prevent ourselves from effectively competing. We have discussed this before. I know you are aware of the debate within the Senate Judiciary Committee. But the foreign dimension to competition is not always taken into account in enforcement of the antitrust law. The Japanese organize their electronics business, they centralize it at the same time we seek to break up IBM.

All of these proposals impinge to one degree or another on antitrust laws.

Senator MATHIAS. I would like to take this opportunity to express my thanks to Senator Danforth. In connection with the Senate Antitrust Subcommittee consideration of the *Illinois Brick* case legislation, we were, in fact, able to make some suggestions which are now embodied in the legislation which is pending, which would go a long way toward equalizing the position of American business and foreign companies in trade. It was a hard-fought battle, and we had to take on the whole of the State Department, in order to get it done. I think it was a blow struck for liberty, myself.

As the chairman suggests, we are constantly putting halters on our own people. It's not a good idea.

Senator STEVENSON. The disincentives are large. They include certain disincentives in the antitrust laws which are addressed by these measures. They need the attention of the Senate Judiciary Committee.

If there are no further questions, thank you. We look forward to working with you on these measures.

Any other suggestions you may have for improving the competitiveness of U.S. industry that fall within the jurisdiction of this committee are welcome. Thank you very much.

Mr. DANFORTH. Thank you. We really commend you for your leadership in this area and appreciate the hearings that you are holding.

Senator CHAFEE. I also have a statement.

Senator STEVENSON. That will be entered in the record as though read. In addition we'll insert Senators Mathias' and Javits' statements as well.

[The statements follow:]

STATEMENT OF JOHN H. CHAFEE, U.S. SENATOR FROM THE STATE OF RHODE ISLAND

Senator CHAFEE. Mr. Chairman, I would like to speak briefly about the nature and importance of S. 864, the Export Trade Association Act.

Two important events will occur next week that deserve mention:

First, next Wednesday marks the 1-year anniversary of the introduction of President Carter's "new" national export policy. Last September, President Carter announced his intention to develop a coordinated national export policy by reducing domestic barriers to exports, and by administering the laws and policies affecting American exports—including antitrust laws—firmly and fairly, but with a greater sensitivity to the importance of exports. To date,

this hasn't been done. Our bill seeks to give some impetus to the President's proclamation.

Second, at the end of next week the Commerce Department will announce the U.S. trade record for August. If our balance of payments shows another trade deficit for last month—and there is every evidence that it will—it will mark the 40th consecutive month of deficit trade. This is the longest period of trade imbalance in our country's history.

All sorts of items—sweaters, cameras, watches, jogging shoes, color TV sets—are now made largely outside the United States. In a bizarre reversal of old-time charges of capitalist imperialism, we are presently the world's largest supplier of wheat, corn, and farm products and the largest importer of manufactured goods. The large trade deficits that the United States has experienced in recent years have weakened the value of the dollar abroad and intensified inflationary pressures in our own economy. The burden is upon us to adopt a workable export stimulation program in an effort to reduce our trade deficit and restore stability to the dollar in international trade.

This morning, I had the opportunity to question Mr. Reubin Askew, President Carter's nominee to be the new chief U.S. trade negotiator, about export disincentives. He stated that it was time we reviewed all possible disincentives on American firms which attempt to compete for business abroad.

This is a major task. Our environmental, and safety requirements, as well as business code of conduct spelled out under the Foreign Corrupt Practices Act, all would come under study. While we attempt to generate new incentives for exporters, ought we not also take a closer look—an oversight—of current laws and regulations that may present unfair disincentives?

S. 864 represents the result of our efforts to take a "closer look" at one such law—the Webb-Pomerene Act.

With the enactment of the original Webb-Pomerene Act more than 75 years ago, Congress envisioned an eager and willing American business community taking advantage of the opportunity to pool facilities, resources and expertise to implement an ambitious joint exporting program. However, that vision never materialized.

Although the Webb-Pomerene Act was intended to provide a real boost to American export activity, defects in the original legislation have made it a relic of the past—a dated idea not good enough to be of great use, yet, not so useless to be abandoned.

There were 57 Webb-Pomerene trade associations at their peak in the mid-1930's, which accounted for 19 percent of total U.S. exports. Today, only 33 associations exist and they are responsible for less than 2 percent of exports.

There are four basic reasons for this poor showing. First, Webb-Pomerene associations have lacked sufficient market strength and discipline to exert adequate control of foreign prices. Second, the American business community traditionally has placed top priority on tapping the vast domestic market and has been much slower to focus on the prospects for exports. Third, the growing U.S. service industry has been excluded from the act's antitrust exemption. Finally, the Federal Trade Commission (FTC) and the Department

of Justice have been perceived by the business community as hostile toward Webb-Pomerene associations.

The changes made by our bill will assure a more hospitable government attitude toward the exporters of American goods and services, while protecting our domestic markets from any anticompetitive spillover from export trade associations.

Specifically, the bill:

One, extends the provisions of Webb-Pomerene export trade associations to the exportation of services;

Two, clarifies and thereby protects a user's antitrust exemption;

Three, provides that antitrust immunity is contingent upon a preclearance procedure to insure that domestic markets will not be injured;

Four, transfers the administration of the act from the Federal Trade Commission to the more export-minded Department of Commerce;

Five, creates within the Department of Commerce an office to encourage the formation of American export trade associations;

Six, provides for the establishment of a task force to evaluate the future effectiveness of the Webb-Pomerene Act.

At present, there are three companies in my own State of Rhode Island that belong to Webb-Pomerene associations. Together, these firms account for nearly 3,000 Rhode Island jobs and a large share of our State's exports. The Brown & Sharpe Manufacturing Co. of North Kingstown, is a member of the American Machine Tool Consortium, Inc. Leesona Corp. of Warwick, maker of textile winding machinery, and Marshall & Williams Co. of Providence, maker of textile finishing machinery and heat recovery systems, belong to Amatex Export Trade Association. Amatex is composed of a group of complementary manufacturers who can totally equip, re-equip, or construct overseas textile mills in package deals.

It is also worth noting that one of these companies, Marshall & Williams, is a smaller business with only 80 employees. One of the most promising aspects of the Webb-Pomerene Act is its applicability to smaller businesses. In passing the act, Congress was aware that individual businesses wishing to enter foreign markets could rarely each afford to sponsor their own foreign representation. the initial cost is an entry barrier to small firms; even when overcome, maintaining parallel marketing organizations puts Americans at a cost disadvantage when compared with the foreign cartels of producers.

This is an important assistance to my State, where 90 percent of the businesses are classified as small.

Although it is not possible to estimate precisely the impact of these changes on exports, one U.S. industry—the National Construction Association—projects a sales increase of $2 billion annually if it could operate as a Webb-Pomerene trade association.

This is especially important since the United States which ranked first in its share of the overseas construction market in 1976, has now dropped to fifth place trailing Japan, Korea, West Germany, and Italy.

Trade associations can be successful as demonstrated by the Webb-Pomerene Act. And the act can be made more useful to U.S. business. We believe that S. 864 is an important step toward a

strong and vigorous offensive trade policy, which the Nation still lacks a year after the President's announcement to improve America's export position, and that our bill will help to reduce our chronic and continuing trade deficit.

STATEMENT OF CHARLES McC. MATHIAS, JR., U.S. SENATOR FROM THE STATE OF MARYLAND

Senator MATHIAS. Mr. Chairman, thank you for the opportunity to testify today on S. 864, the Export Trade Association Act of 1979.

Your hearings are timely and important. The subcommittee is to be congratulated for taking the initiative in this critical area. If we are ever going to beat inflation and get our decelerating economy moving again, we've got to increase our exports.

The U.S. share of international commerce has decreased from 27.7 percent in 1958 to 19.3 percent in the first half of 1978. More than half of our 1978 trade deficit of $34 billion can be traced to the decline in U.S. manufacturing and agricultural trade.

American exports in 1978 were only 6.7 percent of gross national product while imports stood at 8.4 percent of GNP. Other major industrial nations in the world generally pay for the goods they import by what their exports earn. Our trade deficit has led to greater inflation and a dollar bleeding to death in world markets. The importance of exports to our economy cannot be overstated. One of every five production jobs in this country is involved with export; $1 of every $3 of U.S. corporate profits comes from international activities, and exports now contribute more to our GNP than private corporate investment does.

Much of the blame for our poor export performance can be pinned on the difficulties U.S. exporters face in foreign markets. The Webb-Pomerene Act was originally intended to make it easier for U.S. businesses—especially small U.S. businesses—to penetrate these overseas markets. Unfortunately, the act has not worked as well as had been hoped. Many of the provisions of our bill will help make the Webb-Pomerene Act less moribund, and will make it more useful to small businesses seeking to increase their exports.

The bill's other major provision, to extend the Webb-Pomerene exemption to the antitrust laws to include our service industries, is also of great importance.

In recent testimony before the Governmental Affairs Committee, the U.S. Chamber of Commerce representative urged that we give greater attention to the U.S. services industries. The United States has both the largest domestic services economy and the largest services labor force. It is also the largest importer and exporter of services and the largest overseas investor in services. Last year, our services trade totaled about $129 billion. Importantly, our services industry has a trade surplus of $23 billion, which helped offset the $34 billion deficit suffered in merchandise trade. For this reason, we should encourage the services industries by giving them equal footing with manufacturers in setting up Webb-Pomerene associations.

One segment of the services industry that was particularly hard hit by increased competition from abroad was the construction business. Until recently, the United States dominated the heavy construction industry. Each year, U.S. firms did over 10 billion

dollar's worth of business abroad, and this work resulted in another $4 billion in sales abroad of many other U.S. products used in construction work—heavy equipment like bulldozers and cranes, steel, and electrical equipment. I've heard rough estimates of up to 500,000 jobs that can be attributed to construction projects overseas.

Despite our great experience and know-how, 2 years ago the United States slipped from first place to fourth place in construction worldwide. We now rank behind West Germany, Italy, Japan—and Britain and South Korea are snapping at our heels. I think that our bill will enable U.S. companies to join together when necessary to meet this challenge head on.

I hope that this committee will find it appropriate to correct this anomaly in the law. Our service industry is striving to increase exports, and it deserves this vote of confidence.

STATEMENT OF JACOB K. JAVIS, U.S. SENATOR FROM THE STATE OF NEW YORK

Senator JAVITS. Mr. Chairman, today I am pleased to join with my colleagues, Senators Danforth, Bentsen, Mathias, and Chafee, in testifying before your subcommittee on S. 864, the Export Trade Association Act of 1979.

It is generally accepted that the post-World War II growth of world prosperity is closely correlated with the dramatic expansion of international trade and that the reversal of this trend could have disastrous economic and political consequences both at home and abroad. The unprecedented balance-of-trade deficits of the last 2 years have resulted in the steady erosion of confidence in the dollar and aggravated inflationary pressures at home. Additional setbacks perpetuated by chronic deficits include loss of jobs—exports currently account for one of every nine manufacturing jobs in the United States—and declining competitiveness of U.S. manufactured products in both the domestic and overseas markets. While we have seen some improvement in the trade balance in recent months, we should not be lulled into ignoring the underlying weaknesses that continue to exist. I cannot stress enough the urgency of developing a national export policy.

The long-term trends in U.S. export performance are not encouraging. Ironically, as the management of our domestic economy and the export sector have become increasingly interdependent, U.S. export growth in real terms has been slowing. According to a recent study released by this subcommittee, U.S. exports in real terms were only 1 percent greater in 1977 than in 1974.

While this softening in U.S. export growth can be attributed in part to the slow growth rates in the economies of the U.S. traditional trading partners, the failure of U.S. industries to expand exports in the faster growing economies of some of the newly industrializing countries at the same pace as our competitors has resulted in a steadily shrinking market share for U.S. products overseas.

As I have already noted, the management of our domestic economy and the export sector are inextricably interwoven. Each $1 billion of exports forgone represents a loss of $2 billion in GNP and $400 million in Federal tax revenues. Conversely, each $1 billion of

U.S. goods sold overseas generates 40,000 U.S. jobs. Export promotion must become a high priority initiative of U.S. Government policy.

Many experts contend that uncertainty or at least perceived uncertainty about the extraterritorial application of U.S. antitrust laws is one of the greatest single inhibitors to increased U.S. foreign trade and investment. The overwhelming handicap of not knowing how his operation will be looked upon by law enforcers here at home compounds the inherent problems resulting from the already uncertain and risky climate abroad which faces U.S. businessmen engaged in exports. This uncertainty results in the loss of new markets for U.S. exporters who forgo opportunities to be daring and innovative and rely instead on tried and true markets. Furthermore, even those businessmen who take advantage of the Webb-Pomerene Act maintain that the exemption presently provided is too narrow to allow them sufficient support to do battle in the fiercely competitive world marketplace of today.

The growing size of foreign conglomerates and the active participation of foreign governments in commercial activities make it very difficult for U.S. firms to compete effectively, for they are hindered by strict antitrust constraints which do not affect their foreign competitors. I am convinced that we must continue vigorously to enforce very high standards for business practices affecting U.S. citizens. On the other hand, we must not completely disregard pragmatic considerations when dealing with cartels and combinations created with either the support or the encouragement of foreign governments.

Under current export practices, the bids for a foreign construction contract in many cases will include several from small U.S. companies, but only one bid from each foreign country. That one bid is generally from a large consortium which has been organized with the approval of the foreign government and frequently with an active government role.

To cite a specific example, a single U.S. firm competing on certain foreign projects in the construction field is at a distinct disadvantage. The development of a large manufacturing complex involves a series of stages, from preliminary design to final construction. Large Japanese and South Korean trading companies are able to put together a unified package deal involving design, engineering, and construction with one contract, one price, and one group of businessmen. A small U.S. firm, bidding only for the design work, stands almost no chance of gaining the contract. The irony of this narrow Webb-Pomerene application is that by not allowing small service firms to form associations, we benefit those few U.S. firms that are large enough to compete. The result is a decrease in competition, not an increase.

I am convinced that U.S. export trade must have a firm foundation. When a company is not sure of its footing, it will not take the risk of antitrust prosecution in the United States or business failure abroad. We must begin to foster here at home, through greater Government-private industry cooperation, a more favorable climate in which U.S. companies, both large and small, can begin to expand their economic horizons through greater export sales.

The bill before you today, S. 864, is designed to lay the groundwork for this new export policy approach by expanding the antitrust exemption under the Webb-Pomerene Act to permit companies engaged in services to form export trade associations.

I am convinced that if the Webb-Pomerene Act is to serve the same purpose as it served in 1918, its scope must be broadened to include services as well as goods. In 1918, the United States was just beginning to develop manufacturing industries capable of competing with the established industries of European countries. Goods were our primary concern, today services are of equal importance, with service-related industries accounting for just under two-thirds of U.S. GNP. Given the close links between goods and services, it appears that the potential for increasing exports in this latter sector of the economy is just waiting to be explored.

Another provision of the bill which I support transfers the administration of the act from the Federal Trade Commission and establishes within the Department of Commerce an office to deal with the active encouragement and promotion of export trade associations. As you are well aware, a handful of major U.S. companies account for the lion's share of U.S. exports, and the Commerce Department has estimated that there exist about 20,000 companies which have the potential to export profitably but do not do so for a variety of reasons. A major obstacle for these firms is their lack of expertise with orchestrating export logistics, such as transportation, insurance, licensing, and general export know-how. By establishing an ongoing organization to push for greater export participation within the Department of Commerce—the Government agency in whose jurisdiction this responsibility properly falls—I am convinced that S. 864 will accomplish a major redirection in the course of present export policy.

Yet another provision of the bill which I support is the precertification provision in section 5 of the bill. This approach, I believe, will reduce uncertainty for potential Webb-Pomerene associations and will expedite procedures generally. However, I contemplate offering language which specifically and precisely states what is meant by "a material change in circumstances"—the phrase which triggers a voiding of the trading exemption given by certification.

Last year, I had the honor to serve for 6 months as a member of the National Commission for the Review of Antitrust Laws and Procedures. Regrettably, while our report did not address all aspects of U.S. antitrust laws as they apply to the practices of U.S. businessmen engaged in international commerce, it did focus on the Webb-Pomerene exemption. Among other suggestions, the Commission, together with the business advisory panel, which had been appointed to work with the Commission at the recommendation of the President's export policy task force, recommended that if, upon re-examination of the act, Congress agreed to retain the exemption for export associations, it should be expanded to include service businesses. I strongly support, as I did in my separate views to the Commission's report, this expansion of the act's coverage.

Mr. Chairman, if there are no objections, I ask that chapter 14 of the National Commission's Report, which relates to the Commission's findings on the Webb-Pomerene Act together with the business advisory panel's recommendations be included for the record.

[The information referred to is printed at p. 159.]

One of the major criticisms directed against modifying our laws to allow for the additional formation of export trade associations is that they are presently little used. We must be sanquine in this respect. In fact, one of the provisions of this bill requires that the Webb-Pomerene Act as amended be reviewed after 7 years to determine whether the export trade association model has worked to serve the purpose of heightened U.S. export activity and to make recommendations on whether the act should be continued, revised, or repealed.

Presently, export trade associations number approximately 25 to 30 and currently account for less than 2 percent of U.S. exports. However, the Department of Commerce considers these associations to be underutilized because the present legislation does not explicitly cover the export of services and other tangibles. The bill before you today, if enacted, will put this assertion to the test, and I am hopeful that we will begin to see a rising number of Webb-Pomerene associations entering the market.

Critics of export trade associations further argue that these associations act as an unwarranted spur to international cartel arrangements. I believe these critics miss the main point. Support of these associations should not be construed as an endorsement of international cartels; in my experience, export trade associations have been used defensively rather than offensively to provide individual U.S. corporations with the legal protection better to compete in third markets with foreign competitors, whether they be large nationalized industries or foreign export cartels. These export trade associations serve a useful purpose to many exporters, and if the Federal Government undertook to educate business owners, particularly small business owners, on the benefits of forming associations, I feel it could play an even more important role in our efforts to increase exports.

Support for the expansion of the Webb-Pomerene Act is emerging on various fronts. Recently, the economic declaration of the Senate Republican Economic Subcommittee, which I chaired, in its recommendations on international trade and monetary policy prepared by the relevant task force, proposed the expansion of the act to stimulate greater export activity among small and medium-sized businesses. The impact of the Webb-Pomerene Act on export promotion is also a topic of review by a subcommittee of the President's Export Council, on which I serve together with the chairman of this subcommittee, Senator Stevenson.

Mr. Chairman, if I may, I would also like to comment briefly on a related piece of legislation that I believe deserves this committee's favorable consideration. I refer you to the bill which I have cosponsored with Senator Stevenson, the Export Trading Company Act of 1979, which will facilitate the formation of export trading companies. The bill would require an antitrust immunity for these companies and would offer some far-reaching provisions for Government financing, private ownership participation and more liberal tax treatment for these export companies. I view this bill and the Webb-Pomerene bill as complementary rather than mutually exclusive. To my mind, this bill is yet another effort to grapple with the problems of encouraging greater export participation and

thereby to materially enhance our balance of payments position, lessen inflationary pressures at home, expand employment, and strengthen the dollar.

Senator STEVENSON. Our next witness is Mr. Ky P. Ewing, Jr., Deputy Assistant Attorney General for Antitrust. Mr. Ewing.

STATEMENT OF KY P. EWING, JR., DEPUTY ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION, DEPARTMENT OF JUSTICE

Senator STEVENSON. I will say to you what I will say to all the witnesses. If you have a full statement and are prepared to summarize it, I would be happy to enter it in the record.

Mr. EWING. I would appreciate you letting me submit the full statement. I have a brief summary.

Senator STEVENSON. That will be entered in the record.

VIEWS ON PENDING BILLS

Mr. EWING. I welcome this opportunity to present the Justice Department's views on the pending bills dealing with export cooperation and antitrust. Let me begin by emphasizing the Department of Justice's belief that exports are absolutely vital to this country. Indeed, it's important for us to recall the context in which we are all now considering these bills, the object of which is to enhance our export capability. Ever since the Reciprocal Trade Agreements Act of 1934, the United States has been a leader in opening up world trade by removing governmental restraints of a tariff or nontariff nature. Recently, the successful completion of the multilateral trade negotiations reflects this country's continuing commitment to free and fair world trade.

We have also long recognized that free trade is in danger if private monopolies, cartels and restrictive business practices are used to allocate markets and prevent competition.

In the period immediately after World War II, we encouraged creation of antitrust laws in Germany and Japan. We decartelized their industries and undertook antitrust prosecution of major international cartels. This November we will be engaged in the first UNCTAD diplomatic conference on restrictive business practices. This is an exercise in which we hope, however gradually, to influence other nations toward procompetitive free market principles. They, in turn, have asked us to endorse the principle that no nation should foster the participation of its enterprises in export cartels and enterprises which will adversely affect world trade or the trade and development of developing countries.

Mr. Chairman, I note that the European Common Market which now has the most significant antitrust laws in the world, in terms of geographic coverage, has no special antitrust exemption for foreign or export activities. Instead, the Common Market's rules rely on particularized analysis of whether any particular restraint is injurious to their markets.

Now given this context, it seems to us the first fact to be borne in mind in our consideration of these bills is this: Webb-Pomerene associations have played an extremely minor role in this Nation's world trade. The 1967 FTC study noted that export associations

under the act accounted for less than 3 percent of U.S. exports. Today based on 1976 figures, registered Webb-Pomerene associations account for only 1.5 percent of U.S. exports.

The significance of the Webb Act then is obviously closely related to the issue of the antitrust legality of exporting activities. Our position is one we held and disseminated for many years. It warrants my emphasizing it again strongly in your hearing.

In general, American businesses don't require antitrust exemptions or clearance to engage in joint exporting ventures or any other joint activity, the sole purpose of which is to sell goods or services for consumption abroad. Accordingly, it has been the consistent position of the Department of Justice that the antitrust exemption found in the Webb-Pomerene Act of 1968 is unnecessary to provide protection for export trade associations, because in general, the normal activities undertaken by such associations have as their exclusive focus markets abroad.

Whatever the claimed benefits of these associations, I think we should realize there are some side effects to the creation of this kind of regulatory apparatus. In the words of the President's National Commission for the Review of Antitrust Laws and Procedures in its report of January of this year, I quote:

> It (the Webb-Pomerene Act) creates an adverse environment for procompetitive diplomatic initiatives. It would seem, moreover, that the procompetitive purposes of Webb associations should be accomplished without antitrust immunity. In short, the methodological approach utilized by the Commission when applied to the Webb-Pomerene Act immunity would on the current record counsel its elimination. As a result, a number of Commissioners favor outright repeal of the Act.

The Commission itself recommended reconsideration of the act by the Congress and suggested that if the Congress is to continue it, it should be amended by inclusion of a particularized needs test and by extention of the services. Two of the items covered in some of the proposals pending before you.

In our view, relevant to your reconsideration of the issues underlying the Webb-Pomerene exemption is the work of the interagency export policy task force this past year. It worked to identify export disincentives and formulate policy recommendations for the President.

I think it's important that we realize that a full hearing was given in that export policy task force. The argument of those who assert antitrust enforcement actually impedes our effort to sell goods and services abroad. There was no substantial evidence of lost business because of antitrust laws or evidence of foreign projects promotion which would have been undertaken absent antitrust prohibitions.

We did find admittedly persistent misperception on the part of some segments of the business community as to the reach of the antitrust laws. The President in his September 26, 1978, export message addressed that perception issue and also expressed what we consider a basic Department of Justice position.

PRESIDENT'S EXPORT MESSAGE

With your permission, I would like to quote from the President's statement at that time. He said,

There are instances in which joint ventures and other kinds of cooperative arrangements between American firms are necessary or desirable to improve our export performance. The Justice Department had advised that most such foreign joint ventures would not violate our antitrust laws and in many instances would actually strengthen competition. This is especially true for one-time joint ventures created to participate in a single activity such as a large construction project. In fact, no such joint conduct has been challenged under the antitrust laws in over 20 years.

Nevertheless, many businessmen apparently are uncertain on this point, and this uncertainty can be a disincentive to exports. I have, therefore, instructed the Justice Department in conjunction with the Commerce Department to clarify and explain the scope of the anitrust laws in this area with special emphasis on the kinds of joint ventures that are unlikely to raise antitrust problems.

Now, as part of the measures we have taken to carry out the President's directive, we have announced last November that we would provide export related business reviews within 30 days after the requestors provided us with all the requisite information about their proposal.

More recently, in a joint letter from Assistant Attorney General, John Shenefield, and Assistant Commerce Secretary, Frank Weil, we describe the expedited review procedure, included a copy of our anitrust guide for international operations, and sent this to over 35,000 business and trade associations in this country. We are trying to tackle quite directly the misperception that the antitrust laws may be an export disincentive.

Finally, to finish what I hope is a short summary of a longer statement, let me get to the specific bills before you in terms of your bill, Senator Stevenson, which proposes the creation of trading companies, I will particularly note Assistant Treasury Secretary Bergsten's testimony which in my view succinctly pointed out the difference between the trading companies of Japan, for example, and those already operating in the United States.

I particularly agree with his observations that U.S. business developed its own models for trading corporations based on its own extensive experience in world trade and with a minimum of Government involvement.

Finally, I would point to his comment that there are some notable U.S. trading companies that have not needed special legislation to encourage their formation, nor have they needed a Webb-Pomerene type exemption to be both legal and successful.

NO LEGISLATION NEEDED

My prior statements about the proper interpretation of the reach of antitrust law as it applies to the Webb-Pomerene context is equally applicable in the trading company context. Consequently, at this time the Department of Justice believes that no legislation is needed to create an antitrust exemption for trading companies.

As to S. 864 and S. 1449, my full statement comments on five aspects of those bills. First, the Department of Justice would favor the imposition of a needs test in the Webb Act. Second, we would not object to the specific addition of services to the act's coverage. Third, while in general the Justice Department has historically been concerned when promotion and regulatory functions are combined in one entity, we don't object to a transferring of the Webb-Pomerene licensing action away from an antitrust enforcement

agency provided such is coupled with a needs test and with opportunity for the Department of Justice and FTC to take part in the development of the administrative regulations to be promulgated by the Secretary of Commerce. We note that Senator Danforth's bill seems to provide a start in the right direction on that.

Fourth, we note both S. 864 and S. 1449 would require that a restraint of U.S. domestic trade be substantial before the exemption would disappear. The purpose of this proposal, as we understand it, is to bring the act into what we conceive to be the current state of antitrust laws interpreted by the courts. Thus we have no objection to this clarification of the legal standard even though it's perhaps redundant.

OPPOSED TO PORTIONS OF BILLS

Fifth, the Department of Justice is opposed to those portions of S. 864 and S. 1449 that would provide for exemption revocation proceedings to be managed by the Commerce Department and which would completely oust the Justice Department from Sherman Act enforcement during that proceeding.

In short, we oppose the creation by these bills of a novel adjudicative procedure which would add a new regulatory layer where, in our view, the legal standards to be applied are already well known and adequate remedies at law are available under the Sherman and Federal Trade Commission Acts.

We are hopeful our presentation and prepared statement can assist this committee in its very important work. I would like to assure you and the other members of the committee again that we in the Justice Department share this committee's concern that our companies' spirit of innovation will not be stifled and that they will be free to compete with vigor in all markets of the world.

Thank you.

[Complete statement of Mr. Ewing follows:]

STATEMENT OF KY P. EWING, JR.

DEPUTY ASSISTANT ATTORNEY GENERAL

ANTITRUST DIVISION

DEPARTMENT OF JUSTICE

The Department of Justice welcomes the opportunity to respond to the request of the Subcommittee on International Finance for our views on the three pending bills dealing with the relationship between export cooperation and antitrust. In addition, at the Subcommittee's request, we have added brief comments on a similar bill Senator Inouye proposes to introduce. Two of the bills, S 864 and S 1449, seek to aid exports by expansion of the antitrust immunity presently contained in the Webb-Pomerene Act and by creating a new regulatory structure to confer the exemption and perform other administrative and oversight functions. S. 1663 is a measure to license export trading companies and confer on them a broad antitrust exemption similar in scope to that which the other bills would provide.

I would like to begin today by emphasizing our concurrence in the importance of export trade and giving our views on the question of how the antitrust laws generally relate to foreign trade. I will also discuss their effect on the formation and use of export trade associations and trading companies. I plan to address the following specific questions of the Subcommittee:

1. What antitrust constraints currently exist on exports and export-related activities of U.S. persons?
2. What changes, if any would be needed to facilitate formation of U.S. export trade associations or trading companies?
3. What antitrust restraints do other countries impose on the export activities of similar associations?

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Ever since the Reciprocal Trade Act of 1934, the U.S. has been a leader in opening up world trade by removing governmental restraints of a tariff or non-tariff nature. Our recent successful completion of the Multilateral Trade Negotiations and endorsement of the results reflects our continuing commitment to free and fair world trade. We have long recognized that free trade is endangered if private monopolies, cartels and restrictive business practices are used to divide up markets and prevent competition.

In the period after World War II, we encouraged the creation of antitrust laws in Germany and Japan, decartelized their industries, and initiated antitrust prosecution of those major international cartels which lingered after the end of the war. It is interesting to note that it was in this period that the U.S. enjoyed its largest trade surplus.

In recent years we have encountered a major problem of trade deficits. The primary causes of this are well known. We have believed ourselves an affluent nation capable of purchasing large quantities of energy and of other foreign "luxury" goods. Many of our industries, because of the large size of our domestic market or the attractiveness of direct foreign investment, have failed to become export-oriented by making their goods meet foreign specifications and training their sales personnel in foreign customs and languages. Nevertheless,

with the encouragement of this Administration our export performance has been substantially improved, though it remains over balanced by price increases for imported energy.

The role of U.S. antitrust law in this period is well known -- to keep our trade free of private conspiracies restraining export and imports.

What role have national export associations played in world trade, and how is this affected by antitrust law or antitrust exemptions? All available comparisons indicate that the role played by export associations in international trade has been declining, and is minor. The great successes of this era in international competition have been multinational corporations selling highly differentiated brand name goods. In countries such as Japan, export cartels have been more frequently used to curb exports than to increase them.

Most nations with antitrust laws either do not apply those statutes to the foreign or export activities of their firms, or apply their laws only when such activities produce an adverse affect on the interests of their nation. The European Common Market, which now has the most significant antitrust laws in the world in terms of geographic coverage, has no special exemption for foreign or export activities, relying instead on analysis of whether a restraint is injurious to their markets. Japan requires the registration of export cartels, approving

them only upon a showing of need, and reserves the right to dissolve them if their activities abroad are abusive, injure the foreign relations of Japan, or are inconsistent with any international obligations Japan may undertake. Thus, we cannot agree with the proposed "finding" in Senator Inouye's bill that our laws are significantly more stringent than those in other countries.

We will be engaged this November in the first United Nations diplomatic level conference on restrictive business practices. This is an exercise in which we hope, however gradually, to influence other nations toward pro-competitive, free-market principles. They in turn have asked us to endorse the principle that no nation should foster the participation of its enterprises in export cartels which will adversely affect world trade or the trade and development of developing countries.

It is in this context that we come to a discussion of the Webb-Pomerene Act of 1918. The Webb Act was attacked at its inception as being unnecessary because the conduct it seeks to exempt would normally not violate American antitrust laws anyway. A 1967 FTC study concluded that the Act was unnecessary and was not achieving its desired goals since it was not being used very much by small firms and since export associations using it accounted for less than 3% of U.S. exports. Today

registered Webb-Pomerene associations account for only 1.5% of U.S. exports. In January, 1978, President Carter's National Commission for the Review of Antitrust Laws and Procedures concluded about the Webb-Pomerene Act:

> It creates an adverse environment for pro-competitive diplomatic initiatives. It would seem, moreover, that the procompetitive purposes of Webb associations could be accomplished without antitrust immunity. In short, the methodological approach utilized by the Commission, when applied to the Webb-Pomerene Act immunity, would on the current record counsel its elimination. As a result, a number of Commissioners favor outright repeal of the Act.

The Commission went on to say that if the Act were retained, it should be amended so that immunity is granted only in situations where the public benefits outweigh the potential harm, which at a minimum should involve a showing of specific need.

The significance of the Webb Act obviously is closely related to the issue of the antitrust legality of joint exporting activities. Our position is one which we have held and disseminated for many years, and I want to emphasize it strongly. In general, American businesses do not require antitrust exemption or clearance to engage in joint exporting ventures or any other joint activity the sole purpose of which is to sell goods or services for consumption abroad.

A myriad of normal joint export activities can be and are constantly being carried on by groups of American companies without fear of antitrust prosecution. To be actionable, joint activity must have a substantial and foreseeable effect on United States domestic or foreign commerce. Joint activity intended to impact outside the territory of the U.S. and carried on so as not to affect competition between the parties in the United States is unlikely to raise any question under American antitrust law. Accordingly, it has been the consistent position of the Department of Justice that the antitrust exemption found in the Webb-Pomerene Act of 1918 is unnecessary to provide protection for export trade associations since the normal activities undertaken by such associations have as their exclusive focus markets abroad.

The judicially accepted legal threshold test for applicability of the Sherman Act to activity abroad places a heavier burden on government and private plaintiffs than that applicable domestically. The presence of a substantial and foreseeable effect on U.S. domestic or foreign commerce is required, not merely some minimal effect. Thus, the answer to the Subcommittee's first question is that the antitrust constraints on joint export activities of American business are no greater than those imposed on joint domestic activities, and in fact are substantially less.

In 1918, when Congress passed the Webb-Pomerene Act, it provided that the antitrust exemption conferred by the Act is revoked when the joint activities of associations formed under its provisions restrain trade within the U.S. or restrain the export trade of a domestic competitor of the association. Thus, it has been the consistent view of the Antitrust Division and of most commentators that the supposed protection from antitrust liability conferred by the Webb-Pomerene Act is illusory, since it is inoperative in situations where the Sherman Act applies - that is, when the joint activities have a deleterious impact on U.S. commerce. We hold to that position today.

In the past, when proposals for the alteration of the Webb Act have been made, we have also noted that the Webb Act may even deter unregistered activity that is quite legal, and clouds the legality of some activity -- a clouding that could be harmful to our national interests.

In short, the Webb-Pomerene antitrust exemption contributes to the exaggerated antitrust fears of business people engaged in clearly legal activity. They reason that there must be some antitrust worry in exporting jointly if the Government wants to give immunity for it. Moreover, some may conclude that they may not export jointly unless they register and comply with other administrative requirements of the Webb

Act.

The Interagency Export Policy Task Force worked last year to identify export disincentives and formulated policy recommendations for the President to begin dealing with disincentives which could be traced to public sector regulation. It is important to note that though a full airing was given in that context to the arguments of the critics who assert that the threat of antitrust enforcement actually impedes joint efforts to sell goods and services abroad, no substantial evidence of lost business or of foreign projects which would have been undertaken absent antitrust prohibitions was produced. From our participation in that process and our contacts with business people, we agree that there is in some business circles a persistent misperception of the reach of the antitrust laws as far as foreign projects or export activities are concerned. The President in his September 25, 1978 Export Message made specific reference to that perception problem. It is worth repeating here a part of the President's statement, for he correctly set out the state of the law and aptly paraphrased the position of the Justice Department as set forth in the 1977 Antitrust Guide for International Operations. The President said:

> There are instances in which joint ventures and other kinds of cooperative arrangements between American firms are necessary or desirable to improve our export performance. The Justice Department has advised that most such foreign joint ventures would

> not violate our antitrust laws, and in many instances would actually strengthen competition. This is especially true for one-time joint ventures created to participate in a single activity, such as a large construction project. In fact, no such joint conduct has been challenged under the antitrust laws in over 20 years.
>
> Nevertheless, many businessmen apparently are uncertain on this point, and this uncertainty can be a disincentive to exports. I have, therefore, instructed the Justice Department, in conjunction with the Commerce Department, to clarify and explain the scope of the antitrust laws in this area, with special emphasis on the kinds of joint ventures that are unlikely to raise antitrust problems.

A persistent contention we believe demonstrably wrong based on available evidence is the assertion that U.S. firms exporting services, such as engineering and construction firms, have been impeded from competing abroad by the reach of American antitrust laws to their actions outside this country. The hundreds of American construction and engineering consortia operating abroad in the past 25 years give the lie to this assertion. It is simply not so. We have said so in our past public statements. In 1970, for example, we gave a business review clearance to such a venture among eleven U.S. consulting engineering firms exporting their services to Southeast Asia. These firms wished to export their services and they needed no antitrust exemption to do so legally.

As part of the measures taken to carry out the President's directive to us to clarify the reach of the antitrust laws to exports, we announced last December that we would provide

export related business reviews within thirty business days after the requesters provided us with all the necessary information about their proposal. A joint letter from Assistant Attorney General Shenefield and Assistant Commerce Secretary Weil describing the expedited business review procedure, as well as a copy of our Antitrust Guide for International Operations, was sent to 35,000 businesses and trade associations this year.

As the Department of Justice has stated in the Antitrust Guide:

> The "joint venture" is a particularly common form of business organization in the international field, for a variety of entirely legitimate reasons. Some joint ventures are . . . essentially "one shot" consortia engaged in a single venture limited in time and scope. Others may involve what are essentially permanent combinations for the production or distribution of products and services.
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> * * *
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> Normally, the Department would not challenge a joint venture whose only effect was to reduce competition among the parties in a foreign market, even where goods or services were being exported from the United States. The rules are even less stringent where a limited "one shot" type of venture is involved . . . Such short-term consortia are useful where large risks or dollar amounts are involved (as with a multiple bank loan or securities underwriting) or where complementary skills are required (as with the typical construction joint venture). (Emphasis added.)

We make it clear in our Guide that where there is no reason to suspect that the joint venture or the export project

would eliminate competition in the U.S. domestic market or foreclose export opportunities for non participating U.S. firms, a project is not an antitrust problem.

The Antitrust Division has worked steadily during the past two years to clarify its foreign commerce enforcement policy at every opportunity, and we have reason to believe we have succeeded in dispelling some of the uncertainties of the business community. The Guide itself was produced as a joint effort by the President's Export Council and the Department of Justice. It was intended as a general statement of enforcement policy for use by company executives and their attorneys. We have been gratified by the attention the Guide has drawn and by the positive response to it as a substantial step toward reducing the uncertainty as to the applicability of the law in foreign commerce jurisdiction.

Let me move to a more particularized discussion of the pending bills.

First, let me turn to S. 1663, Senator Stevenson's bill to create federal regulatory procedures for the organization and licensing of export trading companies. Assistant Secretary Bergsten's testimony has succinctly noted the differences between the trading companies evolved by Japan, for example, and those already operating in the United States. I particularly agree with his observation that U.S. business has developed its

own models for trade operations based on extensive experience and a minimum of government involvement, and that some notable U.S. trading companies have not needed special legislation encouraging the formation of trading companies or a Webb-Pomerene type exemption in order to be both legal and successful.

While we applaud the bill's intent of boosting U.S. export performance, we note that several significant questions are presented. The most important for the Department of Justice is the grant of antitrust immunity for licensed export trading companies which this bill would provide. Our problem is that, to our knowledge, there is nothing inherent in the nature of export trading companies that requires them to engage in activities which would violate the antitrust laws in order to function effectively or efficiently. My prior statements about the proper interpretation of the reach of antitrust jurisdiction to joint exports generally and to Webb Associations specifically are equally applicable in this context. The operations of properly organized trading companies should create no more risk of antitrust liability than properly operated export associations. There are numerous American export agencies and trading companies currently operating without any felt need for antitrust exemption. Why create doubts about their legality similar to those perpetuated about export associations by the availability of the Webb-Pomerene exemption? If such entities can presently be organized

perfectly well without federal supervision under current law, why is a complex licensing and regulatory structure needed at all? The Department of Justice believes that none is needed.

Let met turn now to S. 864 and S. 1449.

The recent report of the National Commission for the Review of Antitrust Laws and Procedures (NCRALP) made findings and recommendations on the Webb-Pomerene exemption. After reviewing the historic justifications for the exemption, the Antitrust Review Commission recommended that Congress re-examine the need for its continuation. The Commission said if the determination was made to retain the exemption, it should be amended in the following two ways: (a) the antitrust immunity for export associations should be made contingent on a showing of particularized need, and (b) services should be included within the act's coverage.

The main aspects of S. 864, Senator Danforth's bill, on which I would like to offer comments are its adoption of a need test and its extension of specific Webb-Pomerene coverage to export of services as recommended by the NCRALP, its transfer of the administration of the Webb-Pomerene Act from the Federal Trade Commission to the Department of Commerce, and its alteration of the current statute's standards for exemption to clarify that the exemption is not lost even where some effects on domestic U.S. commerce or the export trade of domestic

competitors is present.

As to the provision of a need test in the Webb Act, the Department of Justice would favor such a measure. Without conceding that the current Webb-Pomerene antitrust exemption provides any meaningful protection, it nonetheless is a free exemption, available for the asking by the simple procedure of registering an association with the Federal Trade Commission and filing annual reports. It is the only antitrust exemption in U.S. law of which we are aware which imposes no obligation on those who seek it to make a showing of the public interest reasons justifying suspension of normal antitrust coverage for their joint activities. Especially useful in this respect is Section 5(a)(6) of S. 864 which would place some affirmative obligation on the association seeking an exemption to indicate beforehand the methods by which it proposes to operate, including agreements to sell exclusively to or through the association, agreements with foreign persons acting as joint sales agents and territorial, price maintenance, membership or other restrictions to be imposed by or upon members of the association. Provision of such information would help to assure that legitimate export related activities are conducted. An antitrust exemption should be conditioned upon some initial demonstration of benefits to be obtained by joint activity.

All of the pending bills would add the export of services in specific terms to the Act's coverage. The addition of services to the present statute is a measure which the Antitrust Division regards as inconsequential, since our view and that of most antitrust lawyers is that services may be exported jointly -- and completely legally - without any need for recourse to the Webb-Pomerene antitrust exemption. However, we would not object to the specific addition of services to the Act's coverage, for whatever comfort it may provide.

The transfer by S. 864 of responsibility for oversight and for licensing of export trade associations to the Department of Commerce is based upon the logic that Commerce has as part of its mission the promotion of exports, and accordingly would be better equipped by obligation and temperment to promote the use of export trade associations. In general, the Justice Department has historically been concerned when promoting and regulatory functions are combined in one entity. Thus, in our view, a transfer of the Webb-Pomerene licensing function away from an antitrust enforcement agency makes sense only if coupled with installation of a need test and with an opportunity for Department of Justice and the FTC to take part in development of the administrative regulations to be promulgated by the Secretary of Commerce. If an administrative procedure as proposed in Section 6 of S. 864

involving some assessment of the antitrust risks involved in certification of an export association is put in place, an adequate opportunity for consideration of the public interest would be necessary before any exemption were granted. It is essential that any regulatory structure which operates to confer some immunity from antitrust suits contain adequate opportunity for case by case consideration of the possible competitive harm. Senator Danforth's bill seems to provide such standards, but the additional authority also conferred by it upon the Secretary of Commerce in conjunction with the Department of Justice and the FTC to develop guidelines for the operation of the regulatory scheme and to jointly review them periodically is essential to guarantee that antitrust principles are adequately considered.

S. 864 as well as S. 1449 would alter the present provisions of the Webb-Pomerene Act relative to the degree of permissible effect on U.S. commerce before an exemption would be lost. Essentially, both bills would require that a restraint of U.S. domestic trade be "substantial" before the exemption disappears. The evident purpose of this change is to bring the Webb-Pomerene Act into line with the current state of antitrust law as interpreted by the courts. As I had said earlier, the Department of Justice has long predicated its enforcement efforts in export related matters upon the ability

to prove a substantial and foreseeable affect on U.S. commerce. Thus, clarification of the legal standard, though redundant, would present little concern to us if these bills also relied on the Federal courts to interpret the law. However, other portions of S.864 would provide for exemption revocation proceedings to be managed by the Commerce Department in the event an assertion was made that a certified association failed to meet the requirements of exemption; and S. 1449 would completely oust the Department of Justice from Sherman Act enforcement against Webb-Pomerene exempt associations by giving exclusive jurisdiction to the FTC.

The Department of Justice opposes the creation by these bills of a novel adjudicative procedure which would add a new regulatory layer to an area where the standards to be applied are already well known and adequate remedies at law under the Sherman Act and the Federal Trade Commission Act are available. It is one thing to promulgate a new standard by which an antitrust exemption is to be conferred, but to bestow jurisdiction to hear evidence and make a quasi-judicial determination of facts which are also possible violations of existing antitrust laws is unnecessary and unadvisable.

The present Webb-Pomerene Act as interpreted by the courts contains no requirement for cumbersome administrative findings prior to a consideration by a court of an antitrust allegation to which a Webb exemption may be interposed as a defense.

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The present law's structure should be continued. Creation of this new adjudicative function in the Commerce Department with respect to export trade associations would raise undesirable questions about primary or even exclusive jurisdiction over alleged antitrust violations involving export associations. As with other regulatory schemes which do not clearly delineate the division of responsibilities between the administrative agency and the courts, the mischievous potential for unnecessary confusion and duplicative litigation is created.

I hope our presentation today has been of help to the Subcommittee in its work, for we share the Subcommittee's concern that this nation's spirit of enterprise and innovation must be free to compete with vigor in the markets of our modern world. Thank you for the opportunity to appear.

Senator STEVENSON. Thank you. Mr. Ewing, could you wait? I would like to slip Senator Javits in now but I have questions for you later.

Our next witness is Senator Javits of New York.

STATEMENT OF JACOB K. JAVITS, U.S. SENATOR FROM THE STATE OF NEW YORK

Senator JAVITS. I ask unanimous consent that my testimony may follow that of my colleagues or cosponsors of S. 864, the Export Trade Association Act of 1979.

Senator STEVENSON. Without objection. We will insert Senator Javits statement earlier in the hearing as though read (see p. 131).

Senator JAVITS. Also that my whole statement be inserted in the record. I will only take a few minutes. May I say, too, my assistant who has been monitoring the hearings tells me the Chair asked my colleages whether they favored his bill, to which he referred, and I might say I am a cosponsor of the Senator from Illinois' position on the Export Trading Company Act of 1979.

My purpose in testifying is simply to emphasize the problem relating to the antitrust laws which is subsumed under the exemptions of our antitrust laws, of which the Webb-Pomerene Act is one. I raised this question last year as a member of the National Commission for the Review of the Antitrust Laws and Procedures which operated under the chairmanship of Mr. Shenefield of the Justice Department; and it has also been raised very interestingly by a business advisory panel which we caused to be organized to give us business advice with respect to this question, and is well worth the attention of this committee, as it was of the Commissions'.

EXPORT BUSINESS CREATES EMPLOYMENT

The essence of my view, Mr. Chairman, is that the Webb-Pomerene situation is but the tip of the iceberg. It deals with only 2 percent of the exports of the United States. It involves only a limited number of such organizations—approximately 25 to 30. It omits the fact that the real problem with our export drive—and I am a member of the President's Export Council which is chaired by Reg Jones of General Electric—is that it is not yet a drive. Unless we find a way to bring more than the preestimated 20,000 companies into it, and there is a great potential for export in our country, it just isn't going to work. We are not export minded, except in certain sectors of the economy. Yet the combination of export services and export transportation, as well as the actual exports, result in giving employment to about one out of eight Americans. And in States like mine, New York, and I have little doubt in States like Illinois, especially in view of the enormous amount of agricultural exports which are now 25 percent of all the exports of the United States, they are matters of burning interest economically.

In order to get this export drive moving, in order to bring a large number of people into the export business and to make our own exports more competitive, we are going to have to review the antitrust laws in their extraterritorial application.

My appearance here today is designed to urge the passage of our bill, which makes a little beginning in that regard, by including services as well as goods as the proper subject for Webb-Pomerene activity.

Second, to buttress the case for export promotion generally. We find ourselves constantly frustrated in dealing with cartels, and they are very tight abroad, and dealing with other actions which we consider in restraint of trade, and yet which are freely engaged in by others—not only aided and abetted by government, but promoted by government in other parts of the world among trading nations.

I was a member of this committee in the fifties when we repealed so elementary a section of the law as would have permitted, under government authority and with government control, the oil companies of the country band together to face the oil embargo of 1973. I have little doubt that the government had a big hand in what they did even though there was no law to cover it, so backward are we in recognizing more than just economic conditions.

I urge the bill which we have introduced be passed. I urge that your bill, Senator Stevenson, be passed likewise, because it moves exactly along the same lines, as our bill, to wit, the furtherance of our national export drive.

In respect to the antitrust situation, I urge that we use this occasion as another opportunity to review the bidding, in which we are way out in left field, tying our own right hand behind our backs at the very moment when we need a change in this area more than lifeblood itself.

I ask unanimous consent that the Report of the National Commission for the Review of Antitrust Laws and Procedures as it relates to the Webb-Pomerene exemption may be made part of our remarks directly on this bill and also the report of the business advisory panel, which as I say, is a very high-level operation, involving Mary Gardiner Jones of Western Union; William F. Kennedy of General Electric; Otis M. Smith of General Motors; Jack Valenti of Motion Picture Association of America; Rufus Phillips of Airways Engineering; Robert P. Beshar of National Semiconductor; Seth M. Dabney of Caterpillar Tractors; and Barry E. Hawk of Fordham Law School.

Senator STEVENSON. They will be made part of your statement.

[The documents follow:]

REPORT TO THE PRESIDENT AND THE ATTORNEY GENERAL

of the

NATIONAL COMMISSION FOR THE REVIEW OF

ANTITRUST LAWS AND PROCEDURES

January 22, 1978

CHAPTER FOURTEEN: EXPORT ASSOCIATIONS

Recommendations

The Webb-Pomerene exemption should be reexamined by the Congress. If it is retained, it should be amended in at least two ways:

(a) The antitrust immunity for export associations should be made contingent on a showing of particularized need.

(b) Services should be included within the Act's coverage.

Historical Background

In 1914, Congress authorized the FTC to investigate "trade conditions in and with foreign countries where associations, combinations, or practices of manufacturers . . . may affect the foreign trade of the United States . . . . "[1] In this legislation, Congress was responding to concerns that certain conditions in the export market placed American firms at a competitive disadvantage vis-a-vis foreign cartels.

After more than a year of gathering information, the FTC released a two-volume report detailing its findings and recommending legislation that would permit cooperation among domestic exporters.[2] The FTC called attention to the existence and practices of the many powerful foreign cartels with which American companies were forced to compete overseas. It also noted the existence in various markets of highly effective buying cartels with which U.S. manufacturers had to deal. The Commission concluded that American firms should be free to combine their efforts for exports if they were to trade successfully in the world market on more equal terms with their organized competitors and buyers. Since the small businessman would then be able to share with others the

relatively high costs of exporting, export trade would be promoted.

The FTC Report noted that considerable doubt existed within both the business and legal communities as to the application of the antitrust laws to export trade. This uncertainty, with the attendant possibility of prosecution, prevented American companies from cooperating in export activities and hindered a needed expansion of U.S. exports. In order to clarify the situation, the Commission recommended that legislation be enacted to remove this doubt.

The FTC Report led to the Webb-Pomerene Act of 1918.[3] The main provision of the Act is Section 2, which declares that the Sherman Act shall not prohibit associations that are formed solely for the purpose of engaging in export trade. This exemption is conditioned upon the proviso that the association does not restrain the export trade of any domestic competitor of the association. Further, an association cannot "enter into any agreement, understanding, or conspiracy, or do any act which artificially or intentionally enhances or depresses prices within the United States of commodities of the class exported by such association, or which substantially lessens competition within the United States or otherwise restrains trade therein."[14] The Act also provides for FTC oversight of Webb associations.

Although the Webb-Pomerene Act has been in existence for 60 years, it has been subjected to FTC or judicial interpretation infrequently. The most significant interpretation of the Act by the FTC is contained in an advisory opinion issued in 1924, known as the "Silver Letter."[5] In that letter, the FTC declared that the membership of Webb associations could exist for the sole purpose of fixing prices and allocating sales for export markets. Most associations formed after the "Silver Letter" have limited their commercial activities to fixing prices rather than performing

selling and exporting functions which are now usually handled by the individual members.[6] Thus, the common feature of export associations today is not their performance or efficiency or cost-reducing functions, but rather the pursuit of traditional cartel-related activities.

During the 60 years of the statute's existence, only two major judicial decisions on the subject have been rendered. In *United States* v. *United States Alkali Export Association,*[7] the court held that the Webb Act did not immunize from antitrust prosecution cartel agreements between export associations and foreign competitors; therefore, such associations could not lawfully agree with any individual or group of foreign producers or sellers to fix prices, set quotas, or allocate customers abroad.[8]

In *United States* v. *Minnesota Mining and Manufacturing Co.,*[9] the court held that the Webb exemption is not available to members of an export association who jointly establish and operate manufacturing companies abroad. The greater significance of this case, however, is its identification of conduct that is permissible under the Act. In denying the Government's plea for dissolution of the defendant association, the court found that a Webb association could: (1) agree to export only through that association, (2) agree that the association would purchase goods only from member producers, (3) refuse to deal with nonmembers, (4) fix prices for goods bought for export, (5) fix prices at which foreign distributors could sell the product, (6) agree not to withdraw from the association at will, (7) require its foreign distributors to refrain from handling the relevant product of competitors, and (8) charge higher prices to American exporters than to foreign distributors.[10]

The Exemption in Practice

Despite the high expectations at the time of its enactment, it is generally agreed today that the Act has failed to promote U.S. exports materially during its 60 years of existence.[11] The hope that the antitrust exemption would result in the formation of hundreds of associations serving as joint selling agencies for small firms has not been realized.

The 1967 FTC study shows that from 1918 to 1965, there were only a total of 130 active associations registered with the FTC.[12] As of November 1978, there were only 29 active Webb associations.[13] Membership in these currently active associations consists of approximately 300 firms, although this figure includes duplications resulting from multiple association membership by some firms. More than one-third of Webb associations have four or less members, while two-thirds have nine or less members.

The 1967 FTC study revealed that successful export associations are usually characterized by a membership consisting of the leaders of an oligopolistic industry involving a homogeneous product. The results also indicated that large firms were the most common beneficiaries of the Webb-Pomerene Act.[14] Of the 465 companies that were members of export associations during the 1958-1962 period, only 79 members (17%) had assets of one million dollars or less, and only 101 members (22%) had assets of one to five million dollars. In contrast, larger firms accounted for nearly 80 percent of all exports assisted by the Webb exemption.[15]

"One of the most striking findings" of its 1967 survey, the FTC stated, was the "comparative insignificance" of the contribution of Webb associations to total U.S. exports over the years.[16] During the 1958-1962 period, Webb-assisted exports accounted for only 2.4% of total U.S. merchandise exports.[17] In 1967 the FTC concluded that "[i]n no major area of the world is the total amount of U.S. exports increased

to a significant degree by Webb-Pomerene association activity."[18] It further stated that the Webb Act provided notable assistance to only a few "[a]mong the myriad products in foreign trade channels."[19]

The latest FTC studies confirm these conclusions. Assisted exports in 1976, the latest year for which the FTC has data, were only 1.5% of the total U.S. exports, relatively one-third less than in 1962.[20]

The FTC empirical review in 1967 established that, in the majority of cases, firms seeking the antitrust exemption have been those "least in need of it, being capable of supporting export programs on their own accounts and, in fact, typically doing so."[21] Moreover, associations that have been formed basically represent only a few products of a standardized nature.

A principal criticism directed against the WebbPomerene Act is that Webb association activities adversely affect domestic markets.[22] Opponents of the Act argue that, by encouraging anticompetitive combinations in export trade, it invites the opportunity for similar restraints in domestic trade.[23] While there have been instances of an export agreement being overtly extended to the domestic market,[24] the more likely "spillover" effect of export associations relates to the exchange, among domestic producers in oligopolistic markets, of export information on future prices, costs, and production. The exchange of such information regarding foreign markets, all of which the Webb Act permits, can facilitate parallel pricing in the domestic market, or enable large oligopolists to coexist both at home and abroad.

Another objection is that the exemption is too broad to accomplish the stated objectives of the Act. The Sherman and Clayton Acts might not prevent the type of procompetitive joint export ventures that are set up by sellers to

derive economies of scale or to create countervailing market power.[25] Furthermore, other means are available to achieve the desired results without compromising this country's basic attitudes toward competition. For example, export agents or brokers could be used to provide most, if not all, of the same services export associations were originally designed to provide.

A further criticism of the exemption is the questionable theoretical basis for allowing American firms to cartelize United States export trade.[26] A major premise of the Act was that the existence of foreign selling cartels placed domestic firms at a competitive disadvantage. It is not clear, however, why U.S. companies should be considered disadvantaged and in need of protection under such circumstances. Traditional cartel theory shows that firms operating outside of cartels often benefit from the high prices set by the cartel. A nonmember American exporter would be free to charge a lower price and take business away from the cartel. This theoretical argument is further strengthened by the fact that seldom has a Webb association member cited protection from a foreign cartel as its reason for joining the association.[27]

Finally, opponents also object that the exemption undermines United States Government credibility in advocating strong international antitrust rules.[28] As Robert Beshar, a witness appearing before the Commission, described it, "Webb-Pomerene is a bloody embarrassment" to the United States.[29] In foreign markets, U.S. Webb associations are rightly regarded as cartels. As a result, some nations have authorized the formation of national import or buying cartels to offset the market power of Webb associations.[30] Such a consequence can have an adverse effect on American competitors of the Webb association, who must then deal as individuals with the foreign import cartel.

Arguments in Favor of Retention of the Act

Supporters of the Webb exemption argue today, as they did in 1918, that there is nothing inherently anticompetitive about Webb associations and that real benefits can accrue to small manufacturers who operate in a highly concentrated market if they join together for purposes of export.[31] The argument is advanced that many American firms continue to need today, as they did in the past, a means by which they can attempt to eliminate the economic disparity that exists between themselves individually and monopsonistic foreign buyers. The joint negotiating posture permitted by the Act might also be useful in dealing with foreign governments concerning trade or tax matters.[32] The argument also is made that, in order for firms to compete effectively in foreign markets, they need to obtain the economies of scale achieved by their larger rivals, both domestic and foreign, and that such advantages can be provided through the use of Webb associations.[33]

Supporters of the exemption thus maintain that the Act remains useful. It removes uncertainty concerning the legality of joint exporting arrangements and, at least for some companies, actually encourages export activity. Supporters believe the Act would be even more useful in increasing the volume of U.S. export trade, if the antitrust immunity applied to services as well as goods.[34] It is argued that one of the main reasons the Webb Act has been underutilized is that the export of services has been excluded from the Act's exemption. Adding services to its coverage would be useful, especially to small and medium-sized companies interested in bidding on larger foreign contracts.[35]

In order to broaden the Commission's perspective, a Business Advisory Panel was established to consider the Webb Act exemption and report to the Commission.[36] The Panel recommended that the exemption should be retained.

The Panel found that several industries rely heavily on the Act and concluded that the present foreign trade deficit made this an inopportune time for repeal of the Act. The Panel thought that increased antitrust enforcement and a minor amendment to deal with potentially inconsistent international treaty obligations would effectively deal with the major objections to the Act.

Conclusions

The Commission, because of time constraints and competing priorities, was not able to examine these issues at length. While all the answers are not clear, the questions raised concerning the exemption as presently drafted are substantial. The Act as drafted creates opportunities for significant anticompetitive spillover effects in domestic commerce. It creates an adverse environment for pro-competitive diplomatic initiatives. It would seem, moreover, that the pro-competitive purposes of Webb associations could be accomplished without antitrust immunity. In short, the methodological approach utilized by the Commission, when applied to the Webb-Pomerene Act immunity, would on the current record counsel its elimination. As a result, a number of Commissioners favor outright repeal of the Act.

A majority of the Commission, however, is unable to support such a definitive recommendation. Because of the limited time available to the Commission for study of this issue, and especially in light of the Business Advisory Panel's conclusion that the exemption is important to some industries, the Commission believes that a legislative reexamination of the necessity of such an exemption is warranted.

If the Congress concludes that some exemption in this area is desirable, any reformulated immunity statute should be limited to situations where the public benefits outweigh the potential harms. While the exact reformulation must await a

more complete examination of the issues, the Commission offers the following general recommendations.

Currently, the virtually automatic nature of the exemption for export associations — regardless of such factors as the existence of foreign buying cartels, the competitive structure of the U.S. industry, and the antitrust and trade policies of the relevant foreign governments — makes its scope overbroad. As the FTC concluded in 1967, "[t]he circumstances under which Webb associations are in the national interest appear to be limited, and therefore blanket exemptions which allow firms to increase their market power in international trade should be treated judiciously."[37]

Before American firms receive antitrust immunity for export business activities they should at a minimum be required to make a showing of need. The burden of proof justifying special treatment ought to be on those seeking such treatment. Whether this showing can or should be case by case, or whether particular categories of industries or types of associations could be dealt with as a group, is a subject that requires further study.

Any showing of "need" should be related to the Act's original purpose to enable entry by American companies in the world market on equal terms with combinations of their foreign competitors or customers. It was originally believed that cooperation among American exporters would help them reduce their export costs, expand effective demand for their products abroad, and gain access to export markets on improved terms. And while larger firms were not to be excluded from forming export combinations, the proponents of the original legislation heavily stressed the benefits which such combinations would provide small firms that were financially unable individually to engage in exporting. These considerations are legitimate matters for attention, and therefore, an appropriate "need" could be shown to exist where

associations can provide genuine economies in the promotion and conduct of U.S. export trade or where associations are needed for the defense of legitimate commercial interests.

To guard against the costs of any particular association outweighing any public benefits, any immunity grant should require a demonstration that the proposed association would not adversely affect either the domestic or international trade of the United States. In addition, any exemption granted should permit the President or his representative to prohibit or modify an export agreement if he finds that it may be in violation of treaties or other international obligations. The exemption could then become a bargaining tool in bilateral negotiations with other countries.

Finally, if after legislative reexamination a reformulated Webb exemption is retained, the Commission finds no basis for distinguishing between goods and services, especially since projects combining goods and services are an increasingly important form of exports.

* * * * *

Commissioner Javits filed separate views on this chapter, which are contained in Appendix B.

FOOTNOTES TO CHAPTER FOURTEEN

[1] Federal Trade Commission Act § 6(h), 15 U.S.C. § 46(h) (1976).

[2] Federal Trade Commission, Report on Cooperation in American Export Trade (1916). The Report summarized its findings and recommendations at 370-81 of Volume I.

[3] 15 U.S.C. §§ 61-66 (1976).

[4] 15 U.S.C. § 62 (1976).

[5] *See* Staff Report to the Federal Trade Commission, Webb-Pomerene Associations: A 50-Year Review 102-06 (1967) [hereinafter cited as FTC Webb-Pomerene Report] (Appendix D), where the Silver Letter is reprinted in full.

[6] Allison, *Antitrust and Foreign Trade: Exemption for Export Associations,* 11 Houston L. Rev. 1124, 1130 & n.50 (1974); Larson, *An Economic Analysis of the Webb-Pomerene Act,* 13 J. Law & Econ. 461 (1970). The FTC has on several occasions studied the functions of Webb associations. In 1929, one of its studies concluded that most of the associations formed since the Silver Letter had price-setting as their primary function. This was also the finding by the FTC in studies made in 1945, 1953, and 1963. *See FTC Webb-Pomerene Report, supra* note 5, at 28-30, 48-49.

[7] 86 F. Supp. 59 (S.D.N.Y. 1949).

[8] Id. at 70.

[9] 92 F. Supp. 947, 963 (D. Mass. 1950).

[10] *Id.* at 964-65.

[11] *See, e.g., Antitrust Commission Hearings* 103 (July 27, 1978, afternoon session) (testimony of Emil Finley, President, International Commodities Export Corp.); FTC Webb-Pomerene Report, *supra* note 5, at 23.

[12] FTC Webb-Pomerene Report, *supra* note 5, at 23.

[13] Federal Trade Commission, Summary and Analysis of Survey of Webb-Pomerene Associations 6 n.13 (Nov. 9, 1978) (staff memorandum) [hereinafter cited as 1978 FTC Survey].

[14] FTC Webb-Pomerene Report, *supra* note 5, at 32-34, 44-45; *see also Antitrust Commission Hearings* 95 (July 27, 1978, afternoon session) (testimony of Robert P. Beshar, New York, N.Y., and former Dir., Bureau of Int'l Commerce, Dep't of Commerce); *id.* at 105 (testimony of Emil Finley).

[15] FTC Webb-Pomerene Report, *supra* note 5, at 44.

[16] *Id.* at 35, 42.

[17] *Id.* at 36.

[18] *Id.* at 42.

[19] *Id.*

[20] 1978 FTC Survey, *supra* note 13, at 15.

[21] FTC Webb-Pomerene Report, *supra* note 5, at 59.

[22] *See, e.g.*, Larson, *supra* note 6, at 497-98; Diamond, *The Webb-Pomerene Act and Export Trade Association*, 44 Colum. L. Rev. 805, 826-32 (1944); Note, *Webb-Pomerene vs. Foreign Economic Policy*, 99 U. Pa. L. Rev. 1195, 1212-15 (1951).

[23] *See, e.g., Antitrust Commission Hearings* 100 (July 27, 1978, afternoon session) (testimony of Emil Finley); Allison, *supra* note 6, at 1138-39; *International Aspects of Antitrust, 1967: Hearings Before the Subcomm. on Antitrust and Monopoly of the Senate Comm. on the Judiciary*, 90th Cong., 1st Sess. 124 (1967) (statement of Donald F. Turner, Ass't Att'y Gen., Antitrust Div., Dep't of Justice) [hereinafter cited as *International Antitrust Hearings*].

[24] *See* United States v. United States Alkali Export Ass'n, 86 F. Supp. 59 (S.D.N.Y. 1949).

[25] *See, e.g., International Antitrust Hearings, supra* note 23, at 123 (statement of Donald F. Turner); K. Brewster, Antitrust and American Business Abroad 455 (1958).

[26] Larson, *supra* note 6, at 485.

[27] *Id.* at 486.

[28] *International Antitrust Hearings, supra* note 23, at 124 (statement of Donald F. Turner).

[29] *See Antitrust Commission Hearings* 97 (July 27, 1978, afternoon session) (testimony of Robert P. Beshar).

[30] FTC Webb-Pomerene Report, *supra* note 5, at 58.

[31] Letter from Frank A. Weil, Ass't Sec'y for Industry and Trade, Dep't of Commerce, to the Antitrust Commission 17 (Nov. 20, 1978) [hereinafter cited as Weil Letter]; United States v. United States Alkali Export Ass'n, 86 F. Supp. 59, 70 & n.17 (S.D.N.Y. 1949); Note, *supra* note 22, at 1196-97.

[32] Weil Letter, *supra* note 31, at 5.

[33] *See id.* at 1-2.

[34] *Antitrust Commission Hearings* 90-91 (July 27, 1978, afternoon session) (testimony of Frank A. Weil, Ass't Sec'y for Domestic and International Business, Dep't of Commerce).

[35] *See* Weil Letter, *supra* note 31, at 9-11. *But see Antitrust Commission Hearings* 103-04 (July 27, 1978, afternoon session) (testimony of Emil Finley).

[36] Press Release of the Antitrust Commission (Oct. 27, 1978). The Panel grew out of an interagency export policy task force chaired by the Department of Commerce.

[37] FTC Webb-Pomerene Report, *supra* note 5, at 69.

Attachment A

BUSINESS ADVISORY PANEL ON ANTITRUST EXPORT ISSUES

December 5, 1978

John H. Shenefield, Chairman
National Commission for the Review
of Antitrust Laws and Procedures
Department of Justice Building
Washington, D.C. 20530

Honorable Members of the Commission:

The Business Advisory Panel on Antitrust Export Issues was named by the President on October 27, 1978,* to report to this Commission in time for its views to be considered in the Commission's final deliberations. The Panel met twice, on November 3 and on December 1, 1978. At its December 1 meeting, the Panel learned that on December 7 the Commission would be meeting to consider its findings and recommendations on antitrust immunities and exemptions. Because it is

* The members of the Panel are:

Rufus C. Phillips, III, Chairman, President of Airways Engineering Corporation;

Robert P. Beshar, Attorney, Director, National Semiconductor, and former Deputy Assistant Secretary of Commerce, Director of Bureau of International Commerce and National Export Expansion Coordinator;

Seth M. Dabney, General Counsel and Secretary, Caterpillar Tractor Co.;

Professor Barry E. Hawk, Fordham Law School, and Chairman, International Trade Committee of the Section on Antitrust Law, American Bar Association;

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not possible to complete a report in time for that meeting, the Panel has decided to summarize its conclusions in this letter.

The Panel was asked by Commission Chairman Shenefield to concentrate its efforts on issues pertaining to the Webb-Pomerene Act. The Panel accordingly focused on proposals to repeal, to modify or to expand that Act. However, the Panel noted that, although the Act is of significant importance to certain industries such as the movie industry, existing Webb-Pomerene associations account for only 1.5 percent of total American exports. The Panel was of the view that there exist other more significant antitrust export issues which the Panel did not have sufficient time to explore.

The Justice Department, Commission staff members and other experts in the field provided considerable oral and written information to the Panel. This included the staff options paper, a newly completed FTC report summarizing information provided in questionnaires sent to Webb-Pomerene associations, information from the Justice Department concerning past business review letters, and letters from the Commerce Department, two Webb-Pomerene associations, and a law firm representing Webb-Pomerene associations supporting retention of the Act, as well as a letter from a constructors association urging extension of the Act to include services. In addition, various other statements for and against the Act, including the testimony and documents presented to this Commission, were reviewed by the Panel. Finally the Panel heard presentations by Mr. Frank Weil, Assistant Secretary of Commerce for Domestic and International Busi-

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Mary Gardiner Jones, Attorney, Vice President, Western Union, and former Commissioner of the Federal Trade Commission;

William F. Kennedy, former International Counsel, now Counsel, General Electric Company;

Otis M. Smith, General Counsel, General Motors Corporation; and

Jack Valenti, President, Motion Picture Association of America, and President, Motion Picture Export Association of America.

ness, Mr. Douglas Rosenthal, Chief of the Foreign Commerce Section of the Antitrust Division of the Justice Department, and Mr. Joel Davidow, Director of Policy Planning at the Antitrust Division.

After considering all of the above evidence and after considerable discussion and debate, the Panel reached the following conclusions, which were unanimous.

Recommendations:

1. The Panel recommends that the Webb-Pomerene Act be retained at the present time. The Panel was persuaded that several industries rely heavily on the Act and that the business advisory process, although of some value, is not an acceptable substitute. In view of the present foreign trade deficit, the Panel concluded that this is a particularly inopportune time for unilateral repeal of the Act. The Panel determined that the two major objections against the Act, its alleged anticompetitive spillover effect in the United States and its alleged hindrance to international negotiations, could be brought into better focus by the means suggested in recommendations 3 and 4 below.

2. The Panel recommends that the Webb-Pomerene Act cover the export of services as well as goods. The Panel found no reason to exclude services from the Act and noted that projects combining goods and services are an increasingly important form of export. The Panel concluded that the present Act could properly be interpreted to cover services or could be amended to make the coverage explicit.

3. The Panel recognized that operations of Webb-Pomerene associations can have domestic anticompetitive spillover effects. Although no hard evidence of such effects was presented to the Panel, neither was there any demonstration of systematic surveillance. The Antitrust Division and

the FTC presently have sufficient investigative powers under the Act to deal with this problem. Accordingly, the Panel recommends that these agencies use their powers fully, particularly to obtain economic data such as the international market participation and the export prices and price changes of Webb-Pomerene associations and the domestic market participation and prices of the members of such associations. Where appropriate, action should be taken against Webb-Pomerene associations which misuse their antitrust exemption.

4. The Justice Department has represented to the Panel that the existence of the Webb-Pomerene Act poses some problems in international negotiations at the United Nations concerning international codes of business conduct. To deal with any such difficulties, the Panel recommends that consideration be given to an amendment to the Act along the following lines: "At such time as the United States undertakes international obligations by treaty or statute, to the extent that the operations of any Webb-Pomerene associations are inconsistent with such international obligations, the Justice Department shall be authorized to seek a declaratory order from a United States District Court directing that those associations thereafter modify their operations so as to be consistent with such international obligations." Such a statutory provision in the Act could serve to blunt foreign arguments opposing American free trade initiatives on the ground of their inconsistency with internal American law.

In conclusion, the Panel would like to assure the Commission that, although the time for deliberations was relatively short, the Panel was able to devote sufficient time to consideration of the Webb-Pomerene Act to conclude unanimously that the Act should be retained at the present time and that it should cover services. At the same time the Panel wishes to emphasize that there are other more significant antitrust issues related to exports which require attention if the President's objective of lowering barriers to exports is to be achieved.

The Panel appreciates the opportunity to provide its views to the Commission.

Sincerely,

Rufus C. Phillips, III
Chairman

Senator JAVITS. Thank you for allowing me to break in to interrupt Mr. Ewing's testimony, and let me explain that I was caught in debate on the floor on defense expenditures.

Senator STEVENSON. We are deeply grateful to you, Senator Javits. You have been as interested in international trade and the international monetary system over the years as anybody in our Government. So we are grateful and your support will be helpful.

I might add that your appearance is timely. It comes in the middle of the opposition of the Justice Department to these bills. Let me ask, if I might, one question before you leave.

I sense, and it hasn't been mentioned, that the focus of antitrust concern should be shifting to the global marketplace. Under the dangers of divided markets, cartelization, and so on, in one-world marketplace, we don't give much attention to the effect of foreign competition in our own so-called relevant domestic marketplace. But if that sense is right, would we not be in a stronger position to negotiate against antitrust abuses in the global marketplace, and also in behalf of continued efforts to bring down nontariff barriers to trade in that marketplace, if this legislation were adopted.

INVOLVEMENT WITH DEVELOPING COUNTRIES

Senator JAVITS. We certainly would. We aren't nearly aware of the fact as we should be, considering our economic strength and considering the amount of interest which we have in the world where we not only have an interest in buying and selling, but where, let us remember, we are heavily involved with the developing countries who are also striving to fight exactly that same type of constraints in the global marketplace that we are. Now over 25 percent of our exports are going to the really developing countries, so we have not only the usual interest, but we are having a totally new interest in their future.

Senator STEVENSON. If we give ourselves the same tools as our competitors, we would be in a stronger position from which to negotiate.

Senator JAVITS. Exactly. I may say to the chairman that we have tried that technique for loosening up a bit. In the trade adjustment assistance area, we are giving more discretion in tools we use. Similarly, in the MTN bill we just passed we gave a lot of discretion to the President and the tools he can use. Why can't we apply a different standard in antitrust? After all, the antitrust laws weren't written in the Old Testament or the New. I think you are certainly right about that and I hope you carry it through here in this Committee, and I will help you on the floor.

Senator STEVENSON. Thank you. If you would like to stay around and help us with the Justice Department——

[Laughter.]

Senator STEVENSON. Mr. Ewing, I sense from the testimony of many of our witnesses the concern of businesses over the uncertainty that is inherent in antitrust law and its application to the Webb-Pomerene associations. If I understand you, you recognize that concern and attempt to address it with the business review procedure you referred to. But will that procedure bind the Federal Trade Commission? Will it bind potential plaintiffs in treble dam-

age suits or even the courts? If not, how effectively will it reduce the uncertainties which now discourage industries, perhaps, for example, including services, from forming Webb-Pomerene associations?

NO LEGAL CHALLENGES

Mr. EWING. Mr. Chairman, it would not legally bind the Federal Trade Commission or private plaintiffs. The practical effect, however, over the last decade or so, has been 180 degrees from that. To the best of my knowledge, neither the Justice Department nor the FTC has ever challenged a transaction or venture that we have cleared under our business review procedure. To our knowledge, there has not even been a private challenge to such transactions.

We know there has been no successful challenge to any procedure we have cleared, any transaction we have cleared under our procedure. So it is a question of the degree to which there is uncertainty of business. If there is, in most cases I believe, really no question it will be legal under the antitrust laws, private counsel to a company will say that. The company will go forward and not even bother to ask for a business review. It is only where you get into the fringe area we would be called upon. In those instances we certainly do contribute a degree of certainty to that business by giving that clearance.

Senator STEVENSON. The indications we have are there would be more associations but for these uncertainties. You do recognize these and you have your own response to them. That being the case, what is wrong with preclearance? You suggest that your assurances ought to be adequate. What is wrong with making sure they are adequate through a preclearance procedure.

Mr. EWING. Let me make plain I am not here urging repeal of the Webb-Pomerene exemption. I said that earlier and in my prepared statement. I also said that if the Congress considers that it is needed, or to provide certainty or any other factor, then we would not object to its being broadened to include services.

We do support that portion of two of the bills that would require particularized need showing by applicants for antitrust exemption. Applicants should have to come in and explain what it is about the way they propose to offer this that would be questioned and for which this need for an exemption. Thus, in a large measure, I am in fact in support of certain portions of these bills.

Senator STEVENSON. Could you tell us a little about what the record has been as far as challenges to Webb-Pomerene associations or other joint exporting activities over the last 30 years?

Mr. EWING. The only challenge brought by the Justice Department to a Webb-Pomerene activity was a case that went to the Supreme Court in the sixties. The last one before that would have been Minnesota Mining, which was 1950.

I don't think we are guilty of some charges, namely people who want to sabotage or do in the Webb-Pomerene associations. Our record doesn't bear that out at all. We are aware of the fact that Congress passed not only the Sherman Act, but the Pomerene Act as well.

Senator STEVENSON. How about private treble damage suits or FTC cases?

Mr. EWING. I could supply an answer. I don't have it with me at the moment.

Senator STEVENSON. Thank you. Could you?

Mr. EWING. Yes.

Senator STEVENSON. Now the President in the statement you referred to on export policy said:

> I have also instructed the Justice Department to give expedited treatment to requests by business firms for guidance of international antitrust issues under the Department's Business Review Program.

What has the Justice Department done in conjunction with the Commerce Department to describe the kinds of joint ventures unlikely to raise antitrust problems?

JOINT VENTURES

Mr. EWING. We have recirculated the international guide to some 35,000 businesses and trade associations this summer. That guide attempts to cover as hypotheticals some joint bidding and joint venture arrangements. We believe that is a means of clarifying the legality of business activity abroad.

We are now in the process of working through some guidelines on joint ventures in the research area which, if we can get them satisfactory to us, I hope we will shortly make public. These are areas in which we start with a proposition that we need a particularized analysis of the venture to see whether the context in which it operates, the world context, in which it operates, is needed or whether on the other hand its purpose will be simply that of the ordinary monopolist or cartel which is either to raise price or reduce output, not to ship more goods but rather achieve higher private profit of the individuals concerned.

We have to make a balance in joint venture analysis, where you start with a proposition that you have to have a particularized analysis. We are trying to do enough of these analyses to give further clarification to businessmen kind of activity which is clearly legal under the antitrust laws.

Senator STEVENSON. This guide was issued January 1977 and revised March 1977. The President's statement was September 1978. Are you suggesting that his instructions to the Justice Department will be complied with by reissuance of this 1977 guide plus the clarification with respect to research?

Mr. EWING. I am suggesting that those are two of the principal tools we have that we are using in order to carry out his directive. It is a matter of clarification. It is a matter of carrying a message, even if the message was written in 1977, to make certain it is properly perceived by the business community.

The President recognizes in his remarks a great part of the problem is perception.

Mr. STEVENSON. Let me conclude with a more general question.

As I indicated earlier, I sense that foreign competition is not given full credit by the Justice Department when it assesses competition in a relevant market. Leaving aside the global marketplace, foreign competition is frequently the most effective competition in our domestic market.

Chrysler is discovering how effective it can be, and I gather there are some indications that General Motors may be less concerned about the application of U.S. antitrust laws because of foreign competition in the domestic market.

It has been a long time since I studied antitrust law, but my sense is the Justice Department doesn't give much credit to foreign competition in the domestic market.

Take IBM as another example. The Japanese semiconductor and electronics industries are organized and subsidized by their government. This year they are going to produce fourth generation computer technology. That is about the highest of the high technology. It will hit IBM.

In the meantime the Justice Department is still prosecuting IBM. Is that kind of development, namely the introduction of competitive technology in the U.S. market taken into account by the Justice Department in determining when to prosecute and when to continue prosecution?

Mr. EWING. I think I can answer the question by saying yes. We certainly attempt to evaluate any particular market in terms not only of the U.S. companies competing in it but also in terms of the foreign companies competing in it. We like to see what the actual competitive situation is, whether the product is being produced by a domestic entity or a foreign company.

To the extent that any relevant market may in fact be larger, if someone could prove that to us we would be glad to examine it and consider it. In fact, in at least one merger situation where we didn't prosecute, we did hear arguments about the world market.

I am not saying we agreed with them but we certainly are perfectly content to have people come and argue that position to us. If those are the facts of the world we live in today, we want to know those facts. To the extent there has been a change in perception of markets in the last few years, I would say, I think the Justice Department moved with it since we understand more than we are perhaps given credit for about the international implications of what this country's businesses are doing.

20,000 POTENTIAL EXPORTERS

Mr. STEVENSON. Well, one last somewhat general question.

I was not surprised by the position of the Justice Department on the trading company bill. Another branch of the Government, the Commerce Department, has indicated that there are 20,000 potential exporters in the United States—potential, including very small companies.

These companies feel at least that they can't compete in foreign marketplaces effectively because they don't have the services available to them. Their competitors in other countries are represented by trading companies. One of the purposes of the trading company legislation is to involve smaller companies in competition in foreign markets.

If the Commerce Department, which supports this legislation, feels that effective competition by small American companies requires trading companies to represent them, and in fact trading companies do involve the smaller companies of other countries

effectively in world commerce, how will the position of the Justice Department help those small companies survive in the local marketplace, which I assume is an objective of the Justice Department and antitrust laws?

Mr. EWING. Let me clarify our position on that issue.

We are not arguing here at all that this country doesn't need trading companies. We are not in any way commenting for example on the tax aspects as to which we defer entirely to the Treasury Department.

Our only comment was as to the creation of a special antitrust exemption for any trading companies that are registered under the act. We don't under traditional antitrust analysis see where any legitimate activities of trading companies would run afoul of the antitrust laws.

Consequently, before we would support or cease to object to creation of a new antitrust immunity, we would like to know about the specific activities in which those trading companies are expected to engage in that would violate the antitrust laws and which would have a substantial adverse effect on the foreign or domestic commerce of the United States—that elements you would have to have in order to violate the antitrust laws.

We want to know in short what it is those trading companies would be doing that would violate our laws and thus restrain our foreign and domestic commerce to the United States before we could state we support or could not object to an exception. That is all we are saying in this testimony.

Senator STEVENSON. I am delighted to have that clarification. We already told you what they will do. They will do what other trading companies of other countries do to us. They will represent competing product lines, and do it in all parts of the world. We don't have any trading companies. The large grain trading companies aren't trading companies, Mr. Bergsten notwithstanding. These trading companies might compete with the grain companies.

We have some export management companies. They could provide a full range of services, from banking to contract services to market analysis to the sale of products, including competing products. They could offer different prices to meet the price competition in different parts of the world, obsorbing exchange rate fluctuations as they go.

We don't have any trading companies in this country with which to compete effectively for basically two reasons, although there is a lot of interest in industry and the banking community in creating them. The two reasons are, leaving aside banking laws, antitrust prohibitions or uncertainties and some problems in the internal revenue code.

Now I can tell you more about what they will do but I suspect you already know.

Mr. EWING. I am not certain by any means that I have in my head the kind of detailed knowledge of what you contemplate. I would say that if the bill contemplates large multinational corporations, conglomerate corporations, banding together and deciding how to divide up the world, then we certainly do oppose the antitrust exemption for that.

I would also emphasize that this country is founded on the idea that competition, even among companies abroad, will sell more goods and services than is competition is absent.

Senator STEVENSON. Now you are getting to what Senator Javits and I were talking about. I share that concern—dividing up the world, dividing markets—that is a legitimate concern.

But we were suggesting to you that that concern requires an international response. Our antitrust laws aren't extraterritorial. We can only prevent multinationals from dividing up foreign markets. They interfere with and prevent the United States from effectively trading. There are prohibitions apparently against trading companies.

But with a stronger competitive position in the world as a result of fewer disincentives and some incentives for trading companies, we might be in a stronger position from which to negotiate an international response to the problem you are concerned with, which is a very legitimate concern, but one we can't extraterritorially solve and are in a very weak position to attempt an international solution.

Mr. EWING. I felt right at home this afternoon in having Senator Javits give his presentation in the middle of our discussion. As you know, Senator Javits and Assistant Attorney General John Shenefield have engaged in quite a dialog in this area for some time at the National Commission for the Review of Antitrust Laws and Procedures and elsewhere.

I think it has been useful. One of the comments made in rely to Senator Javits at one point was to say that it was odd when we were faced with a cartel abroad we responded by a cartel instead of responding by having our two or more independent companies compete vigorously by lowering the price below what the foreign cartel was selling at and thus gain the business in the United States.

There is a bit of that kind of analysis that has to go on when you think about creation of trading companies if you are considering allowing our large conglomerate enterprises to create cartels on our side in order to meet cartels abroad.

COMPETITION ON PRICE AND QUALITY

You need to remember the best way to get our exports flowing from this country to another country is to compete on price and quality and have a better product and undercut the price being charged by the foreign cartel.

Senator STEVENSON. That is a purpose of the trading company.

Mr. EWING. To the extent that we are to survive today as individual concerns, to mount a campaign on a scale necessary to accomplish this, that is possible under existing antitrust laws and existing antitrust analysis. That approach would point toward some kind of particularized need to test for any particular trading company in which case you could utilize the business review procedure.

For example, in 1970, 11 construction companies came to us and stated they wanted to get together to bid on a massive project. We said fine. We gave them a clearance very quickly and they went and engaged in it jointly.

Senator STEVENSON. I don't see how that will help with 20,000 small potential export businesses. Well, there is enough common ground here to continue the discussion. Maybe we can come up with some safeguards that would satisfy your concern and do what we want to do, which is to improve competitiveness in the United States and the world over the long haul and prevent anticompetitive behavior.

We may have additional questions. If so, I will send them in writing. Thank you very much.

Senator STEVENSON. Our next witness is Mr. Daniel Schwartz, Deputy Director of Bureau of Competition, FTC.

Welcome. You, too, are welcome to summarize your statement if you would like to enter it in the record.

STATEMENT OF DANIEL SCHWARTZ, DEPUTY DIRECTOR, BUREAU OF COMPETITION, FEDERAL TRADE COMMISSION, ACCOMPANIED BY CARL HEVENER, ATTORNEY, BUREAU OF COMPETITION

Mr. SCHWARTZ. Thank you. I have brought with me to the table Mr. Carl Hevener, staff attorney responsible for administrating this program that you have been discussing today and yesterday, to answer any specific questions you might have.

In light of the testimony that occurred, I would like to only very briefly summarize my statement and respond to questions you might have.

I am pleased to have this opportunity to present our views concerning proposed legislation to encourage export trade. The important questions being considered here relate to whether antitrust immunity is necessary to encourage this and, if so, whether any revisions are required to insure that an acceptable level of export trade is achieved.

I discussed in my statement a number of aspects of the specific bills before the subcommittee. I would like, if the Chairman would permit, to go directly to the conclusion.

Senator STEVENSON. Please do. The full statement has been entered into the record.

Mr. SCHWARTZ. Each of the bills under consideration offers useful suggestions concerning the promotion of export trade and the administration of a limited antitrust immunity for export trade organizations. Several suggested modifications in the laws relating to export trade organizations should be given serious consideration.

REGISTRATION OF EXPORT TRADE ORGANIZATIONS

First, we recommend that the Secretary of Commerce or some other agency be assigned the lead role in promoting trade by encouraging the registration of export trade organizations. Administrative functions related to registration of export trade organizations should also be performed by that agency.

We support the proposal to transfer the responsibility for Webb-Pomerene organizations to the Department of Commerce.

At the same time, care should be taken to insure that export trade organizations don't pose an undue threat of restraints of trade in domestic commerce. Antitrust protection should be grant-

ed only if necessary to promote export trade and only to the extent necessary for that purpose.

The subcommittee should consider proposals that provide limited certification and immunity based on a showing of need.

In addition, we are concerned that domestic trade restraints falling outside the limits of antitrust immunity should be subject to meaningful penalties in order to deter such restraints. Thus, we support provisions—such as that in S. 1663—that would leave intact the full range of government enforcement of the antitrust law against organizations whose activities unduly restrain domestic trade or the trade of a competing exporter.

It may also be appropriate to provide for private damages in cases where export associations restrain domestic trade. Consideration should be given to insulating export trade organizations from criminal penalties and treble damages only when they act within the scope of their certification.

LIMITED ANTITRUST IMMUNITY

We also endorse the inclusion of services within the scope of any limited antitrust immunity. However, we suggest that trade in patents, licenses, and know-how should be included only when incidental to the sale of goods.

Finally, we urge the subcommittee not to lose sight of the very basic question before it, that is, whether any antitrust immunity ought to be granted to encourage export trade. The Congress should reexamine the necessity of antitrust immunity for export trade associations.

The National Commission for the Review of Antitrust Laws and Procedures cited spillover effects on domestic competition and the availability of export agents or brokers that could provide many of the services export associations were designed to provide as factors arguing against the wisdom of an export trade association immunity.

In addition, that body questioned the theoretical basis of an immunity being necessary to counteract the power of foreign cartels. The report pointed out that individual American firms selling abroad may benefit from high prices set by foreign cartels; they are free to charge lower prices and take business away.

Let me make clear that we don't necessarily reach any conclusions but encourage the subcommittee to inquire as to whether a basis for the need for an exemption is there.

No matter how this issue is resolved, I agree the issue raised by the National Commission deserves very serious consideration.

I will take any questions.

[Complete statement of Mr. Schwartz follows:]

STATEMENT OF

DANIEL C. SCHWARTZ
DEPUTY DIRECTOR
BUREAU OF COMPETITION
FEDERAL TRADE COMMISSION

I am pleased to have this opportunity to present our views concerning proposed legislation to encourage export trade expansion. The important questions considered here relate to whether antitrust immunity such as that contained in the Webb-Pomerene Act is necessary to encourage export trade expansion and, if so, whether any revisions are required to ensure that an acceptable level of export trade is achieved with the least anticompetitive results.

Briefly, our principal recommendations are:

(1) The Subcommittee's first order of business should be to determine whether antitrust immunity for export trade associations is really necessary. The primary recommendation made by the National Commission for the Review of Antitrust Laws and Procedures concerning the Webb-Pomerene Act was that Congress should carefully examine the need for antitrust immunity for export trade associations. We agree with that recommendation and believe it constitutes a necessary first step.

(2) The Secretary of Commerce or some other agency should be given primary responsibility for promoting export trade expansion and the formation of export trade organizations. To the extent that such activities continue, we support transferring export trade association registration and related administrative functions to the Secretary.

(3) The antitrust enforcement agencies should be given primary authority to develop guidelines outlining the

circumstances under which antitrust immunity is afforded to export trade associations. Antitrust immunity should be granted only upon a showing by an association that the immunity is reasonably necessary to promote the export trade expansion objectives of the Act, and that those objectives cannot be achieved in some other manner that poses less danger of restraint of domestic trade.

(4) If the facts warrant granting limited antitrust immunity to export trade associations, the definition of export trade should be expanded to include services. We oppose, however, any effort to lessen antitrust protection where there is a danger of an anticompetitive impact on domestic trade or restraints against competing exporters in the absence of a strong showing that export expansion cannot be attained without some form of antitrust immunity.

(5) At the very least, activities not primarily related to export trade and willful or knowing restraints of domestic trade should remain subject to stringent penalties and to private civil remedies. In all cases, penalties should be sufficient to deter domestic restraints.

THE WEBB POMERENE ACT

The Export Trade Act, also known as the Webb-Pomerene Act, was adopted in 1918 during a period of resurgent interest in foreign trade. The basic purpose of the Act is to increase exports by granting antitrust immunity to domestic competitors for joint activities in export trade that might otherwise be

illegal. For example, the Webb-Pomerene Act allows firms that are competitors in domestic markets to jointly fix export prices and allocate foreign markets -- activities that could in some circumstances violate the antitrust laws in the absence of an exemption.

The Webb-Pomerene Act provides that any two or more persons may form an incorporated or unincorporated association, the sole purpose of which is to export merchandise. The formation of such an association is immune from application of the federal antitrust laws, and each subsequent agreement or act by the association in the course of export trade is also exempt unless it adversely affects domestic trade or constitutes an unfair method of competition directed against domestic export competitors.

In exchange for this narrow antitrust immunity, associations and their members are required to file simple registration statements (and annual updates), and furnish any additional information requested by the Federal Trade Commission. Associations are subject to readjustment proceedings initiated by the Commission when necessary to maintain compliance with the Act and the antitrust laws.

If the Commission finds that an association is not in compliance, it may make a recommendation for readjustment of the association's organization or activities. Upon failure of the association to accept its recommendation, the Commission may refer the matter to the Attorney General, who may bring proceedings pursuant to the antitrust laws.

A federal court held in the 1944 Alkali opinion that this administrative readjustment proceeding is not a prerequisite to enforcement action by the Attorney General pursuant to the antitrust laws.[1] No readjustment proceedings have taken place since the 1940's. Since that time, governmental enforcement has been through direct action pursuant to antitrust and trade regulation laws.

The Webb-Pomerene Act has been of very limited success in promoting export trade. As part of the Commission's responsibility to administer the Webb-Pomerene Act, the staff of the Commission published in 1967 a staff report entitled Economic Report on Webb-Pomerene Associations: A Fifty Year Review. The report concluded that Webb-Pomerene associations were relatively unimportant to the goal of increasing export trade and were likely in the future to contribute even less to that end. A brief staff analysis of special reports filed by export trade associations at the end of 1977, entitled Webb-Pomerene Associations: Ten Years Later, does not suggest any significantly changed conditions since the time of the 1967 report that would alter its conclusions. For example, in 1976, Webb-Pomerene associations assisted in only 1 1/2% of United States exports. At the same time, the 1967 report warned that antitrust enforcement could be necessary to prevent the effects of collusive export practices from spreading to the domestic economy.

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1. United States v. United States Alkali Export Ass'n, Inc., 58 F. Supp. 785, 787 (S.D.N.Y. 1944).

Some critics charge that the limited success of the Webb-Pomerene Act in encouraging exports is an indication that the antitrust immunity contained in that Act does not provide meaningful antitrust protection for export trade associations. Two reasons are frequently cited. First, it has been asserted that the present antitrust immunity is not sufficiently well-defined to provide clear guidance of which activities are immunized and which may still be subject to the antitrust laws. An association must conduct export trade activities at peril that these activities might result in substantial adverse effects within the United States. Even an unintended effect on domestic trade could subject the association to antitrust enforcement; and whether or not a substantial effect on domestic commerce exists may sometimes be uncertain. Second, some critics assert that the antitrust enforcement agencies have been too prone to challenge the activities of export trade associations. Government suits, along with the threat of private treble-damage actions have been asserted to be serious concerns of prospective members of export trade associations that may hinder the formation of such associations and prevent existing associations from more effectively promoting export trade.

Another frequently cited criticism of the export trade association immunity is its limitation to goods, wares, and merchandise. The Act provides no immunity for joint exporting of services. As a result, construction and engineering firms indicate they can find no benefit from the Act, while many other exporters may be apprehensive that the Commission or a court will

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find that the ancillary services they provide connected with export sales are outside the course of export trade protected by the Act.

NEED TO IMPROVE THE WEBB-POMERENE ACT

Before discussing the three bills before the Committee, I would like to outline broadly some areas in which we believe the present law could be improved. First, transferring the responsibility for registering export trade associations and promoting export trade from the Federal Trade Commission to another branch of government could contribute both to the goal of export trade expansion and to protecting the domestic economy from trade restraints. Transfer of administrative functions to the Secretary of Commerce or some other Executive department concerned with exports would facilitate more effective export expansion efforts by the government, and remove the tension the FTC experiences between its dual roles as gatekeeper of an antitrust immunity and antitrust enforcement agency.

Second, we endorse limiting antitrust immunity to the activities of associations that are demonstrated to be reasonably necessary to expand export trade. This recommendation was contained in the FTC's staff report, A 50-Year Review, and was reiterated in the Report of the National Commission for the Review of Antitrust Laws and Procedures. The 50-Year Review emphasized the danger that collusive practices in export trade may spread to the domestic economy; and in our view, sound antitrust and competition policy dictates that enforcement not be

relaxed beyond the point that is reasonably necessary for attainment of other legitimate policy objectives, such as export trade expansion. These objectives should be pursued in the least anticompetitive manner available, and in no instance should they be permitted to create a danger of competitive restraints in the domestic economy without offsetting export benefits.

Third, we support the recommendation of the 50-Year Review that the Commission be given clear authority to take preventive action to eliminate activities that would probably result in anticompetitive effects in domestic commerce if they were to continue. Clarifying the authority of the Commission to take prophylactic action would help provide the guidance that export trade associations require to avoid serious violations at the same time that it helps achieve export objectives with the least anticompetitive results.

For example, in a readjustment proceeding concerning the Carbon Black Export Association, the Commission recommended that the association establish separate offices and staffs from a related domestic trade association, apparently solely to eliminate the appearance and potential of anticompetitive activity.[2] Had the association refused to comply voluntarily, it is questionable that the Attorney General could have successfully undertaken enforcement action pursuant to the Sherman Act.

Fourth, the antitrust immunity of export trade associations should be defined as precisely as possible consistently with

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2 Carbon Black Export, Inc. 46 F.T.C. 1245, 1414-15, 1417 (1949).

effective antitrust enforcement. Moreover, the parties who may sue and the penalties for antitrust violations by export trade associations sould be clearly delineated. Associations and their members will feel confident about administration of an export trade association antitrust immunity only if they understand what activities may be outside the immunity and what action may ensue for activities outside the scope of their authorizations.

A certification procedure might provide the means for balancing export associations' need for certainty against the need for antitrust enforcement to protect domestic trade. Relatively greater protection from antitrust penalties could be given for activities that are within the scope of a certification (but with an incidental anticompetitive effect on domestic trade) than for activities outside the scope of such a certification. For example, civil suits by the government or private single-damage actions could be appropriate for activities within the scope of the certification, and full antitrust penalties -- including criminal penalties and treble damages -- could be made available for activities outside the scope of the certification.

Finally, we recommend that the scope of any antitrust immunity for export associations that may be appropriate be expanded to include services. The Act's antitrust immunity is now limited to "goods, wares, or merchandise." In our view, adding "services" to the definition of export trade would both alleviate existing uncertainties and open up a wider range of exports to expanded sales effort pursuant to the Act. A strong consensus appears to exist in support of this modification. We

add only one caveat. Trade in patents, licenses, and know-how should be immunized only when incidental to the sale of goods, wares, merchandise or services. Otherwise, the Act could encourage frustrating the goal of export trade expansion by facilitating the transfer of know-how abroad even when the effect was to stimulate foreign production at the expense of American exports.

I will now turn to the three bills being considered by the Subcommittee.

S. 864

The Export Trade Association Act of 1979 (S. 864), introduced by Senator Danforth for himself and others, places primary policy emphasis upon export expansion. It transfers administrative responsibility to the Secretary of Commerce and charges him with encouraging the formation of export trade associations. It also adds services to the definition of export trade and establishes a requirement that export trade associations demonstrate that their activities serve to preserve or promote export trade in order to qualify for registration. The Secretary, Attorney General, and Chairman of the Federal Trade Commission would be equally responsible for publishing guidelines to determine compliance with the standards for certification. Other less significant provisions include a ban on participation in export trade associations by U.S. subsidiaries controlled by foreign entities, more or less automatic certification of associations already registered

pursuant to the Webb-Pomerene Act, and an evaluation study to be conducted at the end of seven years.

S. 864 could be interpreted to severely limit antitrust enforcement. The only remedy it would provide for private parties injured by restraints of domestic trade by export associations apparently would be to petition the Secretary of Commerce to conduct a proceeding to determine whether the activities of the association failed to meet the requirements for certification. If the Secretary, in consultation with the Attorney General and Chairman of the Federal Trade Commission, determined that the allegations state a basis for investigation, he would be required to conduct an adjudicatory proceeding to ascertain the validity of those allegations. Upon finding that the allegations were true and that the association had failed to meet the requirements for certification, the Secretary would initiate a court action for injunctive relief to revoke or amend the certification. In addition, the Secretary and other unspecified government officials would be empowered to undertake this type of court enforcement action on their own initiative. In addition to these judicial remedies, Section 5 of the bill would give the Secretary administrative jurisdiction to require amendment of an association's certification, require that the organization or operation be modified to correspond with the certification, or revoke the certification, in whole or in part, upon a finding made in an adjudicatory proceeding that the association, its members, or its export trade activities do not meet the requirements for certification and exemption.

S. 864 does not make totally clear whether or to what extent antitrust enforcement agencies might bring civil or criminal enforcement proceedings against an association and its members pursuant to the antitrust laws for activities having substantial restrictive effects within the United States. The remedies available to private parties petitioning the Secretary of Commerce appear to be limited to the civil action for revocation of a certification or an injunction authorized by Section 4 of the bill. In addition, S. 864 could be interpreted to limit the remedies available in government suits to those enumerated in Section 4 of the bill. As we read the bill, existing antitrust remedies would remain available to the government; however, it could be argued that given the bill's apparent purpose to encourage export trade associations by insulating them from antitrust liability, limiting remedies to those contained in the bill is necessary for accomplishment of that purpose and therefore intended.

S. 864 also prohibits disclosure of any information concerning an application and certification except pursuant to court order. Such an order is available only upon application authorized by the head of a department or agency undertaking an enforcement investigation or proceeding.

S. 864 would substantially alter the terms of the Webb-Pomerene Act. The Webb-Pomerene Act defines the export trade in terms of an exemption for agreements and acts that may lessen competition in export trade, unless those activities substantially lessen competition within the United States (or

with other domestic exporters) as well. As I have already noted, it has been criticized as providing insufficient guidance to exporters of the precise scope of the antitrust immunity it creates and insufficient protection from liability for associations that may restrain domestic trade. S. 864 seeks to reduce the level of uncertainty by providing a more explicit certification authorizing immunity for particular export trade activities and by reducing the antitrust sanctions available.

Four of the standards for certification and exemption provided in S. 864 are essentially equivalent to the standards of the Webb-Pomerene Act. In addition, however, S. 864 provides antitrust immunity only for activities that preserve or promote export trade and includes a prohibition against licensing patents, trademarks, and technology or know-how other than when incidental to the course of export trade in some product or service.

S. 864 would require the Secretary, the Chairman, and the Attorney General jointly to promulgate guidelines to be used by the Secretary in determining whether an association, its members, and its activities qualify for the antitrust immunity created by the bill. The Webb-Pomerene Act provides no guidelines for registration, other than that an association consist of two or more persons and be formed solely for the purpose of export trade. Pursuant to Webb-Pomerene, whether the organization and activities of the association exceed the bounds established for immunity may be determined after registration.

Although S. 864 embodies some improvements to the Webb-Pomerene Act, we would prefer to see some changes in the bill in order to prevent any unwarranted threat of domestic trade restraints by export trade associations. First, as I have noted, S. 864 could be interpreted to limit the antitrust liability of export trade associations (and, presumably, their members) to injunctive relief prohibiting activities that restrain domestic trade and modification or revocation of the associations' certifications. Under this interpretation, no civil damages or criminal enforcement would be available, regardless of whether the association's conduct was within the scope of its certification. Such a scheme would in our view be undesirable; in effect, export trade associations would be invited to violate the antitrust laws without penalty. If this result is not intended, S. 864 should be modified to make clear that all antitrust remedies are available in government suits. At least in the case of associations that act outside the scope of their certifications, the deterrent effect of potential treble damage and criminal actions should not be abandoned. Some penalty -- although perhaps less stringent -- should be available to deter restraints of trade by associations acting within their certifications.

Second, S. 864 should provide a mandate to the Secretary of Commerce to approve certification for only those activities that promote export trade with the least danger of domestic anticompetitive effects.

Finally, we have significant difficulties with the strict limits S. 864 would place on the availability to the antitrust enforcement agencies of information contained in applications for certification. S. 864 would undermine our existing ability to monitor export trade associations and prevent restraints of trade by severely restricting accessibility to information concerning association organization and activities. If an adequate antitrust immunity is provided for export associations, we see no need to restrict access to information contained in applications for certification.

S. 1499

The Export Trade Activities Act (S. 1499), introduced by Senator Roth, would make the Federal Trade Commission solely responsible for certification of export trade associations and for administrative proceedings to enforce compliance based on guidelines promulgated jointly with the Attorney General. Services would be added to the definition of export trade, with the express exclusion of patents, licenses, trade secrets, or technology except to the extent that such technology is incidental to the sale of products or covered services.

S. 1499 would provide for certification of export trade associations and an antitrust immunity for their activities unless they restrain trade within the United States, substantially decrease competition within the United States, or substantially restrain the export trade of domestic competitors. The Commission would issue certifications subject to reasonable terms

and conditions designed to ensure compliance and equitable treatment.

Commission enforcement would be directed at either failure to comply with the terms and conditions of an association's certification or conduct inconsistent with the requirements for certification. Once a determination was made by the Commission that an association had exceeded the boundaries of its authority, a variety of administrative remedies would be available. In addition, injured persons would be able to bring private actions if the unlawful activities had as a purpose or as a primary effect a result prohibited by the requirements for obtaining immunity. This remedy would be limited, however, to single, compensatory damages.

The creation of an exclusive administrative remedy and a limited right of private civil action apparently would cover only anticompetitive effects with respect to "export trade activities of [an] association" (Section 5(d)(1)). Criminal and civil antitrust enforcement proceedings apparently would remain available if an association engaged in non-export-related activities that restrained trade, lessened competition, or injured domestic competitors in the export market.

Existing export trade associations would be certified upon filing applications that did not reveal on their faces that the associations were not qualified.

S. 1499 differs from S. 864 most importantly in that it would provide for certification by the Federal Trade Commission, would require the Attorney General and Chairman to publish

guidelines for certification, and would give the Commission exclusive primary jurisdiction over export trade association organization and activities, at least with respect to export trade activities.

The Commission would in the first instance determine whether an association had failed to comply with the terms and conditions of its certification or had restrained domestic trade, decreased domestic competition, or restrained the export trade of a domestic competitor. If an association exceeded the authority of its certification, the Commission would have authority to amend or revoke that certification or to refer the matter to the Attorney General for prosecution -- presumably, including criminal prosecution -- under the antitrust laws. In addition, following a Commission determination that an association had exceeded the scope of its certification, private parties would be able to sue for compensatory damages, but only when the association's purpose or primary effect was to restrain domestic trade.

S. 1499 also differs from S. 864 in that it would expressly include members of associations as well as the associations themselves within the protection of the Act, it would establish no requirement of a showing that joint export activities immune from the antitrust laws serve to promote export trade to qualify for certification, and it would make no specific provision for future evaluation of the Act. S. 1499 would establish no requirement to demonstrate necessity as a prerequisite to certification, and would leave administrative responsibility in the hands of the Federal Trade Commission.

The principal merits of S. 1499 are that it would expand the definition of export trade to add services, would make more specific the precise scope of each export trade association's antitrust immunity, and would authorize the Commission to prohibit activities that are inconsistent with the requirements for immunity.

We see several problems with S. 1499. It is not clear to us that the Commission is the best place to lodge responsibility to administer an export trade expansion act. I have already pointed out that we have some trouble adequately administering both an antitrust enforcement and an antitrust exemption program. We would prefer to give the export trade expansion program a true test by placing it in the hands of an agency, such as the Department of Commerce, committed to its success.

Some other points should be made. First, conditioning private suits on a prior determination by the Commission that an export association had acted outside its authority could result in involving the Commission in private litigation of allegations that export trade associations have committed antitrust violations. This problem could arise, for instance, in situations where private plaintiffs believe that export associations are violating the antitrust laws but private actions are barred because the Commission either has not instituted investigations of the associations or has investigated and decided that there have been no violations. Frustrated plaintiffs could possibly have actions against the Commission, either to compel it to institute proceedings to determine whether

an association has exceeded its certification, or to review a decision in favor of the association. As a result, the Commission could be compelled to expend substantial resources in proceedings that are basically private, and which it had determined not to be in the public interest. Indeed, the Commission could possibly be put in the position of defending export associations against charges of unlawful conduct. We do not believe this would be a beneficial use of the Commission's resources.

Second, S. 1499 could result in an inefficient allocation of antitrust enforcement responsibilities between the Commission and the Department of Justice. To avoid wasteful duplication of effort, the two agencies have cooperated to allocate civil antitrust matters between themselves. In cases where an export trade association may have participated in illegal conduct which is part of an industry-wide investigation by the Department of Justice, it would be wasteful of time, resources, and expertise to require the Department to transfer that aspect of the investigation to the Commission for independent proceedings pursuant to the Export Trade Activities Act.

S. 1663

Chairman Stevenson has offered in S. 1663 a totally different approach to the export expansion question. His proposal, which would neither amend nor repeal the Webb-Pomerene Act, would create a new program for licensing export trading companies through the Secretary of Commerce. The trading company

proposal would not assign any new responsibilities to the Federal Trade Commission; my discussion of it will therefore be limited to its antitrust consequences.

An export trading company licensed under this bill would enjoy antitrust immunity except to the extent that the activities in which it is engaged constitute or result in substantial restraint of trade within the United States, substantial restraint of the export trade of a domestic competitor, an unfair method of competition against a domestic competitor, or an unreasonable effect upon the domestic prices of goods or services of the class exported by the company. S. 1663 would also provide special tax treatment as an incentive for the formation and operation of export trading companies.

The bill also contains a prohibition against participation by any person owned or controlled by a foreign corporation or other entity, a limitation on the amount of ownership by any one person, and a restriction on covered export trade to products and services receiving within the United States 75% or more of their total value or value added.

S. 1663 apparently would permit export trading companies to engage in limited import activities to the extent necessary to encourage and facilitate exports. Exclusive administrative enforcement authority would be assigned to the Secretary of Commerce to ensure compliance with a license, or to revoke or amend a license, and to determine whether an export trading company has taken any action inconsistent with the provisions of the bill. Antitrust enforcement would be limited to government

actions; no private antitrust actions would lie against export trading companies. However, all remedies available to the government in antitrust proceedings would be available in suits against export trading companies that exceed the bounds of the bill's antitrust immunity.

S. 1663 includes services in export trade, provides a reasonable degree of certainty to licensees concerning the scope of their particular immunities, assigns administrative responsibility to the Secretary, and provides a means to eliminate activities that unnecessarily threaten anticompetitive effects in domestic trade before they become restraints of trade. It pursues its objectives without broadening the scope of the export trade antitrust immunity to any substantial degree.

Significant differences between S. 1663 and other proposals are that S. 1663 would enlarge coverage of the immunity to encompass a limited amount of import activity, and it would invite participation by increased numbers of non-producers. We do not know whether these changes are capable of producing the desired export benefits. Absent such a showing, however, we feel that extending antitrust immunity -- particularly to limited import activities -- is not warranted. Where there are no trade benefits, there is no justification for tolerating an increased danger of anticompetitive effects in domestic markets. S. 1663 may create a danger that companies will engage in reciprocal trading practices which might have adverse effects upon other exporters and importers.

CONCLUSIONS

Each of the bills under consideration by this Subcommittee offers some useful suggestions concerning the promotion of export trade and the administration of a limited antitrust immunity for export trade organizations. Several suggested modifications in the laws relating to export trade organizations should be given serious consideration.

First, we recommend that the Secretary of Commerce or some other agency be assigned the lead role in promoting export trade by encouraging the formation and registration of export trade organizations. Administrative functions related to registration of export trade organizations should also be performed by that agency.

At the same time, care should be taken to ensure that export trade organizations do not pose an undue threat of restraints of trade in domestic commerce. Antitrust protection should therefore be granted only where necessary to promote export trade, and only to the extent necessary for that purpose. Thus, the Subcommittee should give serious consideration to proposals that provide for a limited certification -- and immunity -- based on a showing of need.

In addition, we are concerned that domestic trade restraints falling outside the limits of any antitrust immunity should be subject to meaningful penalties in order to deter such restraints. Thus we support provisions -- such as that in S. 1663 -- that would leave intact the full range of government enforcement of the antitrust laws against export trade

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organizations whose activities substantially restrain domestic trade or unduly restrain the trade of a competing exporter. It may also be appropriate to provide for private damage actions in cases where export trade organizations restrain domestic trade. If necessary to encourage their formation, consideration could be given to insulating export trade organizations from criminal sanctions and treble damages when they act within the scope of their certification.

We also endorse the inclusion of services within the scope of any limited antitrust immunity enacted for export trade associations. However, trade in patents, licenses, and know-how should be included only when incidental to the sale of goods.

Finally, I urge this Subcommittee not to lose sight of a very basic question before it: whether <u>any</u> antitrust immunity ought to be granted to encourage the formation of export trade organizations. The primary recommendation of the National Commission for the Review of Antitrust Laws and Procedures concerning Webb-Pomerene was that Congress reexamine the necessity of an antitrust immunity for export trade associations.[3] The National Commission cited threats of "spillover" effects on domestic competition and the availability of export agents or brokers that could provide many of the services export associations were designed to provide their members as factors arguing against the wisdom of an antitrust

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3. Report of the National Commission for the Review of Antitrust Laws and Procedures, at 295, 302 (Jan. 22, 1979).

immunity for export associations. In addition, the National Commission's report questioned the theoretical basis of justifying export associations as necessary to counteract the market power of foreign cartels. The report pointed out that individual American firms selling abroad may benefit from high prices set by foreign cartels; they are free to charge lower prices and take business away from the cartels.[4] Of course, many justifications for the antitrust immunity have also been asserted. No matter how this issue is resolved, I agree with the National Commission that it deserves serious consideration.

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4. Id. at 300.

Senator STEVENSON. Thank you, sir.

Let me be certain I understand what you are saying. You question the need for an exemption. Yet, I thought I understood you to say that you supported a preclearance procedure on a showing of need in the Commerce Department.

Mr. SCHWARTZ. Excuse me. The point about the National Commission is as follows: This was a body of varying membership which considered the Webb-Pomerene Association exemption along with many others and suggested that Congress look carefully at whether the need is there.

If Congress determines the need is there, we don't oppose in any way the continuation of the exemption, or consideration of the various bills before the subcommittee following that showing of need.

We are not questioning the basic issue, and provide no opinion as to the basic issue of whether an exemption is needed. We just suggest that it is a serious question that needs to be addressed and the conclusions shouldn't be assumed.

Senator STEVENSON. Assume for the sake of argument that the Congress does establish the need for the exemption. What procedure then would you support to eliminate the uncertainties associated with the present exemption?

TRANSFER OF RESPONSIBILITY

Mr. SCHWARTZ. We support the notion of transferring the responsibility for this program to the Department of Commerce and we support the notion of a limited immunity granted on a showing of need on specific bases under a system that hopefully would include the Justice Department and the Federal Trade Commission in promulgation of the certification procedures.

Senator STEVENSON. Where do you draw the line between Justice and Commerce Departments? I understand you to say this review procedure would be within the Commerce Department.

Mr. SCHWARTZ. All we are suggesting is that to the extent that the Secretary of Commerce establishes procedures for showing the need for an exemption, the antitrust enforcement agencies should be included in promulgation of those regulations to assure, frankly, that our interests are fully considered.

Senator STEVENSON. And then the exemption granted would exempt the association from treble damages? What about damages in civil suits?

Mr. SCHWARTZ. We have suggested that there are different ways to do this, depending on how the certification procedure works. In those areas in which activities occur which are not covered by the certification, activities by an association, that those activities, to the extent they violate the antitrust laws, should be subject to the full limit of the antitrust laws.

To the extent that the activities are covered by the certification, one proposal we have made is that perhaps some lesser liability could accrue, if any. I think that depends on how much immunity is needed. How much protection, et cetera.

Senator STEVENSON. Finally, let me ask you—I apologize if I missed it—have you addressed yourself to S. 1663?

Mr. SCHWARTZ. I do briefly in my full statement. Basically, our views are the same. That is, to the extent that there is need for a trading company kind of organization to promote export trade, we think the same standard should apply.

Senator STEVENSON. And a similar procedure?

Mr. SCHWARTZ. I would suggest a similar procedure would assure that all of the various concerns are met, yes.

Senator STEVENSON. Is FTC currently investigating any Webb-Pomerene Associations?

Mr. SCHWARTZ. Yes.

Senator STEVENSON. Were the activities in question covered by the Justice Department business review procedure?

Mr. SCHWARTZ. I don't believe so, no.

Senator STEVENSON. Is that the Motion Picture Association?

Mr. SCHWARTZ. That is the investigation underway, yes.

Senator STEVENSON. Is that the only one underway now?

Mr. SCHWARTZ. That's correct.

Senator STEVENSON. Have there been any in the past?

Mr. SCHWARTZ. There have been a number of investigations since the late 1940's. There have been only two during this decade.

Senator STEVENSON. Can Webb-Pomerene or potential Webb-Pomerene Associations come to the FTC like they can to the Justice Department and get some kind of letter?

ADVISORY OPINIONS AVAILABLE

Mr. SCHWARTZ. They can obtain formal advisory opinion from the Commission or staff and quite frequently obtain informal advice from the staff.

Senator STEVENSON. That doesn't protect them against civil suits.

Mr. SCHWARTZ. No; again, I wish to subscribe to Mr. Ewing's comments about that problem.

Senator STEVENSON. It wouldn't be in the Justice Department either.

Mr. SCHWARTZ. No, though again, it doesn't seem to be that much of a problem.

Senator STEVENSON. We may have additional questions, Mr. Schwartz. Thank you very much for your help. We appreciate it.

Senator STEVENSON. Congressman Jenrette had to go to South Carolina. His statement will be entered in the record as though read.

[The statement follows:]

STATEMENT OF CONGRESSMAN JOHN W. JENRETTE, JR.

Mr. JENRETTE. Mr. Chairman, and members of this committee, the rapid decline of the U.S. dollar on international currency markets combined with other factors as the increasing trade deficit has awaken, throughout the country, a genuine interest in the developing of ways to strengthen our currency and improve our position in international trade. One of the most promising areas in which this interest is being focused involves stimulating American commercial activity in foreign commerce so as to promote new and expanded channels of access for small businesses, and enable existing businesses to participate on a more competitive basis with foreign producers.

On March 22, 1979, I introduced legislation in the House, H.R. 3190, a bill to amend the Export Trade Act of 1918, which in my opinion, could radically improve our trade exchange by promoting the use of the Export Trade Act. The introduction of the bill was in response to the administration's request for help in reducing the U.S. balance of trade deficit. H.R. 3190 is currently pending in the House Subcommittee on Monopolies and Commercial Law, and thus far, no action has been taken on the bill. In this connection, I would applaud this subcommittee's decision to hold hearings on the subject of export trade associations, and I certainly hope that this action will generate a similar interest in the House.

When the Webb-Pomerene Export Trade Act was enacted in 1918, the opponents of the legislation, at that time, thought the legislation was completely unwarranted, and that it cut too severely against America's strong antitrust tradition. Today, as we again address the subject of providing limited antitrust exemption for trade association to engage in export trade the opposing sentiments appear just as strong, and the issue, remains surrounded by controversy. But at this point, I hear an urgent request by the people of our Nation to impress upon this subcommittee the need to reassess not only the longstanding need of America's businessman to be able to compete on an equal footing in export markets with their foreign counterparts, but the people are requesting as well that those of us charged with the administration of Government examine critically the course of events, both political and economical, which are restructuring world politics and the relative economic strength of our Nation. Just one factor alone, our dependence on foreign sources of energy, has reordered the life style of every single American. The accelerating cost of energy has, and from all indications will continue to manipulate the cost-profit ratio of all U.S. commodities and services. The spiraling cost increases range downward on the economic spectrum from substantial increases in the cost of manufactured goods to the extremely high cost of farm

produce. Yet farmers, who supply the backbone of our economy and most of whom I can speak for directly, are finding it increasingly difficult to absorbe the cost of fertilizer to plant their crops.

It is my firm belief that what this country needs now more than ever, is a reduction in cost levels. Such a reduction can only be achieved when our Nation, as a whole, begins exporting the same or a greater amount of goods than it consumes. I think there is now appropriate legislation before the Senate to accomplish this objective. While recognizing that there are some differences in the bill which I have proposed in the House and the legislation now before this committee, proposed by Senator Danforth, the primary concerns is the evolving of a congressional directive to an agency of the Government to affirmatively encourage formation and proliferation of export trade association. With such a development, small business could join together with superior bargaining power and compete more effectively in foreign markets.

I have examined very carefully Senator Danforth's export trade bill and find particularly attractive the provision of the bill vesting in the Department of Commerce the responsibility of administering the Export Trade Act. Equally responsive to current needs is the provision which grants to those association covered by the act, immunity from private civil suits. I believe that this provision in particular will provide the incentive necessary to attract those businessmen who shied away for the advantages available under the 1918 Act, fearing the uncertainty of antitrust violations.

Senator STEVENSON. Now, it's a particular pleasure for me to call Mr. Harvey Kapnick, chairman and chief executive officer of Arthur Andersen & Co.

He and his firm have been of great assistance to this subcommittee. Much of that help has been addressed to S. 1663.

Thank you for joining us. We would be happy to have you summarize your statement.

STATEMENT OF HARVEY KAPNICK, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, ARTHUR ANDERSEN & CO., ACCOMPANIED BY WILLIAM PENICK, MANAGING DIRECTOR, TAX POLICY; AND RICHARD HOEFS, DIRECTOR, INTERNATIONAL TAX POLICY

Mr. KAPNICK. Thank you. I hope our full statement would be included in the record.

Senator STEVENSON. It will be.

Mr. KAPNICK. I am Harvey Kapnick, chairman of Arthur Andersen & Co., an international accounting firm.

My firm has more than 100 offices in 38 countries. Our clients include many businesses of all sizes and many nationalities.

Many of them carry on business activities in world trade. I personally have been concerned for several years about the steady deterioration of the competitive position of U.S. business in world markets and the price our society has paid as a result of that deterioration.

DECLINE OF U.S. BUSINESS ABROAD

In the immediate post-war period, U.S. business dominated world trade. Beginning in the mid-1960's, this dominance began to erode quite dramatically.

In 1965, 68 of the top 100 companies of the world were U.S.-owned. By 1978, that number had fallen to 48. The only other major commercial nation to show a decline during this period was the United Kingdom, which suffered a loss of about the same proportion as did the United States.

Japanese and French companies showed astonishing growth with Japan's share of the world's top 100 companies increasing about 400 percent and France's increasing about 300 percent.

A change of this type and magnitude should not be of concern to our Government if it represents only the result of better management and better-run businesses.

However, when important factors in the change are not caused by the basic inadequacies of U.S. business, our Government should be concerned.

If we are to bring our $16 billion 1978 balance-of-payments deficit into balance, I would like to emphasize that increased exports and increased success for U.S international business must be a prime concern of the Government.

In the best interests of all segments of our diverse society, Government should be an advocate for U.S. business, not an adversary, especially where such U.S. business is operating abroad.

Many factors have contributed to the shift of economic power among nations, not all of them bad. The change partially results from improvement in the economies of other countries, growth of the general world economy and the aggressive competition from companies in other nations to take advantage of the many opportunities presented.

All of these are positive developments. In this effort, foreign governments generally have encouraged and often have actively assisted domestic businesses in their efforts to get a greater share of the world market.

Many governments provide incentives to give a competitive advantage to their businesses. Certain factors that directly involve the United States also have contributed significantly to the drop of the economic strength in U.S. companies—an inflationary spiral exceeding that of other major trading countries, loss of productivity in the U.S. economy, weakening of the dollar and the ever-increasing role of Government in regulating American business.

In the international trade arena, the U.S. Government has not only failed to act as an advocate for American business, but has clearly deterred the ability of American companies to compete in world markets. Seemingly arbitrary export controls, complex anti-boycott rules, poorly defined sensitive payment standards applied retroactively, stringent environmental standards, some applied on a worldwide basis, the tightening and ever-more-zealous application of tax laws—these and other governmental actions have significantly restrained the ability of U.S. business to sell and operate in world markets.

Not all these actions are bad and some had sound objectives. However, such actions have effectively restricted the competitiveness of U.S. business at a cost that our society as a whole must bear.

Other nations have not applied similar restrictions on their business. It should be no surprise to anyone that the businesses of those nations have used their greater freedom to strengthen their position in world markets.

It's time for the U.S. Government to change the nature of its involvement and actively assist the world trading activities of U.S. business.

Mr. Chairman, the Export Trading Company Act by itself could be very helpful. Even of more importance, it might start a positive trend.

JAPANESE TRADING COMPANIES

As we describe in considerable detail in our written statement, Japanese trading companies have served a vital role in expanding the Japanese economy.

You are familiar with Japan's rise from the ashes of World War II to become a major world economic power. Trading companies played a key role in that achievement.

More than 50 percent today of all Japanese exports are currently channeled out through trading companies. Total business activities in exporting, importing and third-country remarketing exceeds $200 billion per year.

Of the 9 Japanese companies in the world's top 100, 4 have captive trading companies that are among Japan's and the world's largest.

Japanese trading companies are unique in the world. They buy, sell, barter, put together deals, form joint ventures, finance, warehouse, and transport.

In short, they provide virtually every commercial service needed to get goods produced by one party sold to another party somewhere in the world. They are true experts in their field of exporting goods.

Every major commercial nation including Japan has developed governmental aids to exports. Our written statement summarizes export aids that other nations offer domestic businesses and those that the United States doesn't provide.

I will mention only two. Most nations allow their companies to establish tax haven foreign subsidiaries to sell exports in world markets free of national income tax. Subpart F of our Internal Revenue Code imposes U.S. income tax on such activities.

Second, many countries, particularly those in Europe, make tax adjustments designed to impose local tax on imports and rebate local tax on exports. Our tax system contains no such features. The tax incentives in S. 1663 offset in part this disadvantage for U.S. companies.

After you review our written statement, I believe you will agree that U.S. business faces export competition in many parts of the world that is greatly assisted by the action of the competitors home governments.

U.S. business does have the DISC provisions to assist it in exporting. While benefits are limited, they clearly aid many businesses, particularly larger ones in export endeavors.

The DISC provisions are highly complex, difficult to meet and often of limited help in developing a new export business. As a result, they have minimal value to small and medium-sized businesses in our society.

If the United States is going to meet the balance-of-payment challenge and help to strengthen the dollar, it must rely upon the skills of all segments of the business community.

We could significantly enhance our export position by involving much more actively the thousands of successful small- and medium-sized manufacturers in the great effort required. Then small businesses could continue to expand which might reverse the trend that they must sell out after they reach a certain level of activity.

Small businessmen usually recognize that market conditions for manufactured products around the world differ significantly from those of the United States. Differences in culture, customs, taxes, local business practices, legal system and many other factors make foreign markets seem very strange to American businessmen that are not active in exporting.

These conditions along with political uncertainty, foreign currency considerations, and import restrictions make such markets high risks for the inexperienced.

As a result, small- or medium-sized U.S. businesses either enter the market at great cost because of learning through mistakes or don't enter the market at all.

A trading company system comparable to that of Japan would clearly make overseas market opportunities much more attractive for these companies. Smaller businesses could turn over their entire export potential to a trading company instead of staying out of the export maket or deciding to start small and hope exports grow in time.

S. 1663 ENCOURAGES U.S. MANUFACTURERS

S. 1663 contains many desirable features that should encourage the mass of U.S. manufacturers to begin or expand exporting and stimulate creative entrepreneurs to enter the export field. With economic activity reaching a critical stage here in the United States, now is the time to develop new markets to offset unemployment. If the bill is enacted, it will take some time to assess its effectiveness. We believe, however, that the basic concept can provide a vehicle by which U.S. businesses that either are not exporting or are exporting little, can enter world markets in a big way.

If the results even approach the 50 percent of exports handled by Japanese trading companies, it's logical to expect U.S. exports to increase by the 11 percent needed to balance our 1978 payment deficit. We are pleased to support the Export Trading Company Act.

Our written statement suggests some modifications in the bill that in the interests of time I won't discuss here. They are not material on an overall basis.

Thank you for this opportunity to appear. I have with me today also Richard Hoefs, director for international tax policy and William Penick, managing director for tax policy. These gentlemen assisted in the preparation of our written statement submitted for the record, and they and I would be happy to answer any questions you may have.

[The complete statement follows:]

ARTHUR ANDERSEN & CO.

Statement on

U.S. Companies in International Markets — The Role of Trading Companies in Stimulating Exports

before

The Subcommittee on International Finance

of the

Committee on Banking, Housing and Urban Affairs

of the

United States Senate

Public Hearing on S.1663,
"The Export Trading Company Act of 1979."

Submitted by
Arthur Andersen & Co.
September 18, 1979

EXECUTIVE SUMMARY OF STATEMENT

I. Since the early 1960s the competitive posture of United States business has been steadily eroding in the world marketplace. As a result United States exports have not kept pace.

II. Japanese trading companies have served a very important role in the Japanese economy and are a key factor in Japanese exporting success. Such companies are real experts in all facets of world trade--they operate worldwide and can handle virtually any responsibility in the buying and selling of goods. Other countries have started to emulate the Japanese trading company approach.

III. Businesses of other nations are very advanced in the art of exporting and are provided invaluable aid by their governments in their endeavors. Such aids take many forms--tax and nontax, aid directly given and aid provided indirectly.

IV. The DISC is very useful to many U.S. businesses, particularly large ones, in assisting their export efforts. It is of limited use to small and medium-sized businesses.

V. Most U.S. small and medium-sized businesses face almost insurmountable difficulties in entering the export market.

VI. The trading company concept of Senate Bill 1663 could be a very important aid in helping U.S. businesses, particularly small and medium-sized ones, expand greatly their export markets.

I. OUR DECLINING ROLE IN INTERNATIONAL TRADE

During the past decade a significant shift has occurred in the economic balance among major industrial nations. The U.S. government, by a number of actions, has made American business less competitive in world markets, and multinational companies based in other countries have moved in quickly to exploit the opportunities created. In some cases, state-owned companies from other countries have moved into the world marketplace, but in many cases the strongest international competitors are privately owned with an active government partner that aids them with effective economic, political and tax policies.

Throughout most of the 20th century, U.S. business has dominated world markets. Statistics for recent years, however, show that this dominance no longer exists. The relative position of U.S.-based multinational companies has declined significantly. During the last few years, foreign-based companies, especially those from Europe and Japan, have become increasingly competitive and increasingly effective in international markets.

Since the mid-1960s, an important trend has developed. Foreign-based companies have been rapidly overtaking and replacing U.S. companies in their relative position as the major commercial forces in the world.

Many factors have contributed to this -- the rapid economic recovery of Japan and the European countries from World War II, the varying effects of changing economic factors -- such as government fiscal policies, inflation, depression and currency adjustments -- and, of course, political factors. We have not attempted to quantify these factors, but do wish to present a picture of what has happened to the relative position of U.S.-based international companies in relation to their foreign-based international and local competitors as that position appears today and as the trend to the current position has occurred over the last five to ten years.

The downward trend in competitive ability of U.S. companies in relation to foreign competitors can be demonstrated by a review of annual sales of the 100 largest firms in the world. The following table shows that, in 1965, 68 U.S. corporations were among the 100 largest companies in the world, ranked by sales. In 1978, the number of U.S. companies in the top 100 had dropped to 48.

DISTRIBUTION OF THE WORLD'S 100 LARGEST
INDUSTRIAL COMPANIES

(Ranked by Sales)

	Number of Companies			
	1965	1970	1973	1978
U.S.-based companies	68	63	50	48
Foreign-based companies	32	37	50	52
Total companies	100	100	100	100

Source: Fortune, various issues.

Note: Appendix A provides a summary of the number of companies by country.

Excluded from the foreign-based companies in our tables and data are the government-owned petroleum companies of Iran, Brazil, and Venezuela which generally are not in a direct competitive position with other foreign or U.S. companies. Inclusion of these national petroleum companies would increase the position of the foreign companies relative to U.S. companies in the various statistics presented here.

If oil companies in the top 100 are excluded, the decrease is from 57 in 1965 to 32 in 1978. This represents a reduction of 23 percentage points, from 66% (in 1965) to 43% (in 1978) of the total number of companies.

DISTRIBUTION OF THE NONPETROLEUM COMPANIES
AMONG THE WORLD'S 100 LARGEST
INDUSTRIAL CORPORATIONS

(Ranked by Sales)

	Number of Nonpetroleum Companies Among 100 Largest			
	1965	1970	1973	1978
U.S.-based companies	57	49	36	32
Foreign-based companies	30	33	45	45
Total companies	87	82	81	77

Source: Fortune, various issues.

Note: Appendix B provides a summary of the number of companies by country.

These tables clearly demonstrate that U.S. companies are being displaced by foreign companies as worldwide leaders in their industries.

From 1965 through 1978, sales of the 50 largest foreign industrial companies increased 595% (from $68.4 billion in 1965 to $475.6 billion in 1978). The corresponding increase for the 50 largest U.S. companies was only 317% (from $147.2 billion in 1965 to $613.4 billion in 1978). Stated another way, in 1965 total sales of the foreign companies were 46% of the sales of their U.S. counterparts; by 1978, foreign companies' sales had increased to 78% of the U.S. companies' sales.

Most of these large corporations, which compete with U.S.-based companies in world markets, are based in Europe (primarily West Germany) and Japan. The only other major country that showed a decline in competitive position was the United Kingdom.

We believe that this data, which has been extracted from accepted and reliable published sources, shows that the relative position of the U.S. companies in international markets has declined substantially during the years surveyed. The data shows that the competition faced by the U.S. companies in overseas markets is of substantial economic strength; it shows further that the large companies outside the United States are growing faster than their U.S. counterparts.

Included in the forty-three foreign nonpetroleum companies among the world's top seventy-five such companies are four Japanese companies which have major trading companies; those trading companies are Mitsubishi, Toyota Motors, Matsushita Electric and Hitachi, each of which is among the top twenty of Japanese trading companies. Thus four major competitors of U.S. business are assisted directly in their competitive endeavors by significant trading company activity.

This data relates to very large U.S.-based and foreign-based companies engaged in competition for world markets. It is clear that, for this group of companies, U.S. entities have lost a substantial part of their position in international trade. It is logical, and our experience confirms, that small and medium-sized companies have had even greater difficulty holding their position or even being able to enter into world trade activities.

A key question then becomes, what steps can Congress take to assist companies, particularly small and medium-sized businesses, that are not active in export markets to become more involved in exports? Furthermore, Congress should consider steps to help larger companies avoid further erosion and even regain part of the position they have lost. A principal objective of the Export Trading Company Act is to establish a vehicle that will assist small and medium-sized

companies to enter the world trade scene through exporting. If American trading companies could begin to match the success of Japanese trading companies, the result should be a substantial improvement in U.S. exports or in our overall competitive position in world markets.

Very importantly, it is apparent that significant markets exist outside the United States. If U.S. companies are to avoid relative growth stagnation and increase their export activities, they must take steps to increase their participation in those foreign markets.

Our balance of payments and the strength of our economy are directly related to our ability to sell American products in international markets. In 1975, our surplus of international payments totaled nearly $18.5 billion. In 1978, however, this had spiraled downward to a deficit of more than $16 billion. Suggestions that our deficit stems chiefly from oil are not sustainable. Both West Germany and Japan import greater percentages of their oil than we do, and both have strong economies, sound currencies and favorable world trade balances.

It is primarily on the export side of our international trade picture that we have lost competitive ground to other nations.

A number of proposals have been made for stimulating exports by U.S. companies. A particular problem exists for small and medium-sized companies, which do not have the know-how to enter export markets and may lack the financial resources inherent in undertaking a risky program to develop foreign markets. The trading company concept embodied in S.1663 is designed to assist such companies, and we are pleased to present our views on it.

II. BACKGROUND ON TRADING COMPANIES IN OTHER COUNTRIES

The stated purpose of the "Export Trading Company Act of 1979" (S.1663) is:

> "To encourage exports by providing for the licensing of export trading companies by the Secretary of Commerce, and by otherwise facilitating their formation and operation."

This act would provide the vehicle for the creation of trading companies to assist U.S.-based businesses in increasing exports, whereas many of them are not in a position to engage in export activity today. This is particularly important to small and medium-sized companies, many of which do an excellent job of developing and manufacturing useful and attractive products but are not knowledgeable at all in how to penetrate export markets. To place

this concept in perspective, some background and discussion of how trading companies have been used by other countries might be helpful.

History of Trading Companies in Japan

The general trading company is a uniquely Japanese innovation that has its roots in pre-World War II days. However, the tremendous growth in activities of trading companies in Japan has occurred subsequent to World War II.

The original trading houses were known as Japanese Zaibatsu, which originally were large conglomerates controlled by powerful families. These conglomerates dominated Japanese industry and finance prior to World War II. Immediately after World War II, antimonopoly legislation put an end to these large family trading houses. However, with the passage of time, the Japanese relaxed their antitrust laws and these once-powerful trading houses rose from the ashes and began operating again. This time, the trading houses were not solely family-controlled entities but represented diversified interests.

For the sake of organizational efficiency, these trading firms generally dealt in commodities and products where volume transactions created economies of scale. In response to both internal and external business fluctuations, as well as the need to increase exports, smaller trading companies banded together to create general trading companies capable of doing business on a global scale.

Japanese general trading companies are not granted specific tax or other growth-stimulating incentives that are not granted to other Japanese companies involved in export operations. As noted, however, trading companies are permitted to function without antitrust problems.

What Do Trading Companies Do?

The Japanese trading company is more than a simple intermediary handling a broad spectrum of products. It not only functions as a bridge between suppliers and users of products but also provides many other services. It might, for example, anticipate needs for raw materials and invest in resources in many parts of the world. Or it might make economic analyses and predict changes in the course of industrial development to assist in the growth and development of new industries to meet future needs. One of the most important roles of the trading company is to organize large projects, drawing upon the resources of various companies in major industries. The basic concept of a Japanese trading company differs from that of a manufacturing company since it is supply-demand oriented rather than user- or maker-oriented.

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Trading companies are extremely important in Japanese export and import activities, although a variety of other trading methods exist side-by-side in Japan. Direct sales contacts between Japanese manufacturers and foreign users are not common, and most manufacturers prefer to deal through intermediaries. In most cases, the average small Japanese manufacturer has neither the financial resources nor the technical competence to enter foreign markets. The nearly 6,000 trading firms now operating in Japan meet his export needs. These firms range from large, diversified, multifunctional organizations to small specialized exporter/importer firms operating in narrow commodity areas.

In Japan, about 10 trading companies account for a substantial part of the exporting and importing of products. The impact of these firms is very significant. In the year ended March 31, 1977, the combined sales of these companies totaled nearly $200 billion. Of this amount, roughly 50% was for domestic sales (goods produced and sold in Japan), 21% for exports of Japanese products, 21% for imports and the balance for offshore trade. These sales were equivalent to about 12% of the gross sales of all Japanese industry for that year and roughly 30% of gross national product.

Many observers credit the Japanese general trading company with Japan's climb to third place in world trade. They have been effective not only because of their economic power but also because of their wealth of talent, expertise and organization.

Types of Trading Companies

Trading companies in Japan may be divided into three groups: general trading companies, specialized trading companies and captive trading companies. A general trading company may handle up to 10,000 different items for export and provide a wide variety of services, including financing, transporting, warehousing, wholesaling and servicing of exports. These companies have offices in nearly all major cities. One Japanese trading company has 50 domestic and more than 125 overseas branches and subsidiaries. These companies may employ as many as 8,000 people to service both domestic and foreign markets. Between 8% and 33% of the shares of the four largest trading companies (Itoh, Marubeni, Mitsui and Mitsubishi) is owned by the public.

Specialized trading companies limit themselves to a narrow range of products and services. Most of these companies handle all phases of product transport through customs to the end consumer or user. For example, sophisticated industrial items

(such as electronic instruments) are quite often handled by specialized trading companies.

Trading companies may also take the form of captive entities. These are companies that handle exports, imports and marketing for individual manufacturing companies. Often they also handle exports to foreign affiliates of manufacturing companies.

The general trading company performs functions that make it unlike any other entity presently operating in the world economy. Aside from its substantial size and its network of offices around the world, it possesses expertise in all areas needed to export, much beyond the capabilities an individual company could provide for itself. The network of worldwide offices maintained by trading companies eliminates the need for expensive and time-consuming overseas travel by representatives of individual companies. Trading companies already have well-established contacts and in-depth knowledge of local practices and regulations that facilitate the export of goods. Multinational staffs employed by the trading companies are able to speak local languages and are knowledgeable about local customs so they can exploit trading opportunities expeditiously. These companies use extensive telecommunications systems to provide the immediate transfer of information necessary to effect an export/import transaction.

Trading companies also stay alert for potential new trading opportunities. Once the company knows an exporter's requirements, it may be able to locate a suitable market and structure a transaction that fits the manufacturer's objectives. The trading company may participate in the preliminary planning and undertake negotiations between the parties involved. On occasion, a trading company may act on its own responsibility, not as a broker or middleman.

An American company, for example, might need to import a certain type of engine block castings for further manufacture. The trading company is able to find the world's best supply source for this particular type of engine blocks. Based on its contacts worldwide, it learns that Brazil is the best source available. The Brazilian supplier, however, lacks the necessary dies to produce the castings as well as the capital required to invest in the new tooling. The trading company locates a source of dies in Argentina and loans the Brazilian manufacturer funds to purchase the dies. The Brazilian source is then fully capable of satisfying the American manufacturer with the needed engine blocks. The various business entities involved in the transaction could not have put the pieces together to carry out this transaction on their own.

Trading companies handle many of the detailed operations necessary in international business transactions. The exporter or importer may be able to reduce its risks because the trading company

can deal at its own risk. Trading companies exporting goods usually buy the goods from the manufacturer or purchase goods from foreign exporters to sell domestically, handling all transportation, insurance, customs clearances and foreign exchange rates and assuming all risks.

Trading companies are also familiar with complex transactions that may involve unconventional types of trading. They have set up barter and production-sharing arrangements in order to consummate a particular transaction. One such case occurred whereby Romania wanted to acquire a paint manufacturing plant. A trading company set up a barter transaction under which the plant was exchanged for Romanian chemicals and machine tools.

Trading companies also promote trade through financing and investment. The process by which goods travel from producer to consumer in international trade is often complex. Trading companies often supply the needed financing to a manufacturer to ensure the export of its goods. A Japanese trading company for example, financed the purchase of fishing boats and equipment for a company involved in shrimp fishing. The trading company also committed itself to purchase and market the entire catch of shrimp.

Trading companies also participate in substantial joint ventures. While trading companies usually supply marketing expertise, they may also find suitable partners for a joint venture. An example of a common form of joint venture in one where a U.S. manufacturer joins with a foreign company that has specialized technological competence, and the trading company provides the marketing expertise in a three-way partnership. Some pesticides now being produced in the United States are a product of such a three-way partnership. A Japanese company supplies the technology, the American company provides the capability for domestic production and the trading company provides international marketing facilities.

Trading companies are also presently involved in natural resource development. Japanese trading companies are particularly active in this area..

Trading companies may coordinate large-scale industrial projects. Many industrial and construction projects are so extensive and complicated that no single enterprise can complete them alone. A trading company will coordinate the various business entities, utilizing different specialties from different nations to carry out such projects. An aluminum smelting facility that will produce 200,000 tons of ingot annually is being built with the help of a large Japanese trading company that is coordinating the construction of a dam and a hydroelectric power station as well as the plant itself. The trading company has coordinated a group of more than a dozen individual companies to complete this complex job.

Trading companies sometimes promote technology exchanges between nations. Trading companies may sell or license technology, offering the same comprehensive services as they do for products. They draw on their experience to determine the technical and commercial value of know-how to meet the objectives of both the exporter and importer. Some time ago, U.S. technology was licensed to a Japanese manufacturer that produced one of the world's largest power shovels. A Japanese trading company was an invaluable party to this transaction.

Trading companies may consult with companies on whether overseas expansion might be appropriate for them. Since the trading companies understand local situations in various areas, they can provide practical business advice to the business entities considering such expansion.

To summarize, trading companies as developed in Japan are unique business institutions combining many features of other businesses including finance. They are fundamentally oriented toward facilitating trade flows and developing trade and industrial activity. The companies handle paperwork for export and import transactions, finance exports and imports, provide transportation and storage services, invest in production processing facilities, establish integrated sales systems, expand market activities, develop large bases for integrating the processing of raw materials, negotiate agreements involving different countries and arrange export and import licenses. Although this list seems comprehensive, it is not a complete compilation of the many functions of large Japanese trading companies.

As a point of further interest, Japanese trading companies have expanded their horizon to serve markets all over the world. Through their locations in many countries, they are in a position to service the needs of exporters everywhere. Recently they have shown an interest in helping American companies in their business needs, including increasing American exports.

Without question, Japan's present economic position has been greatly enhanced by the use of these large general trading companies. Japan is the envy of many nations for its economic development and is clearly an economic leader in the world. Whether the Japanese approach and the activities of its trading companies would be appropriate to the U.S. export situation is arguable. However, there seems little argument that the United States clearly needs to act now to stimulate exports, and some of the approaches utilized by Japanese trading companies might assist significantly in that effort.

Korean Trading Companies

While not as old as the Japanese trading company concept, Korean trading companies have become substantial in scope and size

in recent years and have contributed significantly to the remarkable economic development of South Korea. The Korean Trade Promotion Corporation (KOTRA) is a nonprofit government agency created in 1962 to promote Korea's international trade. Its primary function involves research and exploration of overseas markets. Additionally, KOTRA assists in specific export-import transactions.

Aside from KOTRA, there are presently 11 Korean trading companies doing business in the United States. Modeled after the Japanese trading companies, most of these entities maintain branch offices throughout the world.

In 1975, the Korean government adopted a general trading company development system to support these trading firms. While we lack definitive information on all of the techniques used to facilitate development and operation of these trading companies, there are indications of indirect Korean government assistance through favorable loans and by other means.

The Korean trading companies have experienced tremendous growth over the last few years. This is a result of aggressive sales techniques and a constant search for new customers and profitable foreign markets. These entities have developed an overall favorable reputation in the business community and pride themselves on being able to provide prompt and complete delivery, reasonable prices based on high volume and significant sales discounts. They supply large U.S. retail chains with a number of products, including television receivers and consumer products marketed by Sears, Wards and K-Mart under their own brand names.

One of them, Daewoo Industrial, has experienced a tenfold sales increase within the last three years, dealing with one major U.S. retailer. Its 1978 export sales were $705 million. Another huge trading company, Sansung, has experienced great increases in its electronics division and has opened a number of divisional branch offices throughout the United States. These companies have sales lines ranging from simple consumer goods to complex industrial plants and heavy machinery. While their primary objective is to stimulate exports of Korean goods and materials, they also import raw materials and heavy machinery into Korea.

Other Countries

Brazil has also utilized the trading company concept to some extent, although the activities of the Brazilian companies have not been as significant as those of Japan and Korea. Furthermore, France is undertaking a study of the trading company concept to assist in increasing its exports.

III. OTHER EXPORT INCENTIVES PROVIDED BY VARIOUS COUNTRIES

Considerable information on this subject has been developed about rules and practices of other countries by U.S. business groups, the Ex-Im Bank, the U.S. Department of Commerce and other interested groups. Rather than duplicate those efforts, we attached to this statement as Appendix C a summary prepared by the Special Committee for U.S. Exports. This summary was submitted as part of the testimony of David C. Garfield, Vice Chairman, Ingersoll Rand Company, before the House Ways and Means Committee on March 14, 1978.

A review of Appendix C will quickly show that generally other nations are far more cognizant of the importance of exports to their economies than is the United States. While certain features in specific countries may be a result of the way their tax, legal and financial systems operate and therefore could be ignored, an objective observer cannot ignore the great disparity between what other nations offer to their exporters and what is offered to United States exporters.

Tax Incentives

We let the summary stand on its own merit and only comment on a few important comparisons. As is illustrated by the discussion of tax laws of other countries in Appendix D U.S. tax law works against U.S. exporters in comparison with tax laws of major trading competitors. This appendix is from a statement our firm submitted to the House Ways and Means Committee on April 3, 1978; the tax facts contained therein have changed only slightly since 1978.

A number of other countries either do not tax at all or tax only partially foreign source income. While some of these rules were primarily intended to prevent double taxation of income, they now provide a definite competitive advantage in international trade. Exports from these countries are often organized so that all or a large percent of the income derived from exports is treated as foreign source income (or isolated in foreign subsidiaries) and thereby either escapes taxation or is taxed at a significantly lower rate.

For example, France totally exempts foreign source income from taxable income. Furthermore, foreign source income is defined very broadly to include any income derived from a permanent establishment abroad, regardless of the location or nature of its activities. Belgium taxes foreign source income at one-fourth the rate applied to domestic source income, while The Netherlands very seldom taxes income derived from a foreign branch.

Almost all other countries do not tax currently the income of foreign subsidiaries of domestic parents. This is generally true in the United States, although through the complex provisions of Subpart F of the Internal Revenue Code, the income from U.S. exports earned by foreign subsidiaries is taxed currently in the United States in many situations. Furthermore, when a foreign subsidiary of a U.S. company repatriates its profits to the U.S. in the form of dividends, the dividends are fully taxed to the U.S. parent subject to the allowance of a foreign tax credit with certain significant limitations. In some countries, however, dividends paid by foreign subsidiaries to domestic parents are totally tax exempt, while other countries provide deductions against dividend income received.

In the Special Committee's summary, it indicates that some foreign countries do not zealously apply intercompany pricing rules to the benefit of exporters. While most countries have provisions similar to our Section 482, which requires the allocation of income among related parties on an arms length basis, some countries do not apply these standards strictly to exporters. Included in such handling are several major European exporting nations and Japan.

Border tax adjustments in many foreign countries clearly benefit export activities. Most European countries (all European Common Market countries) have adopted a value-added tax under which exporters obtain rebates of tax on exports, while importers must pay the value added tax on imports. This system clearly works as a special and effective export tax incentive and places imports at a disadvantage in domestic markets, unless the countries of origin of those imports also have a value-added tax rebated on products leaving their borders.

Non-Tax Export Incentives

As the Special Committee illustrates in Appendix C many countries have specific non-tax export incentives. Some have agencies similar to the United States Ex-Im Bank to help finance exports. Exports are financed through direct loans, guarantees, or insurance or credit refinancing, depending on the type and size of the transaction involved. Long-term export sales are usually supported by direct loans. Our Ex-Im Bank rules extend long-term credit only to foreign buyers of U.S. goods and services, while other countries extend direct loans to their own suppliers as well as to the buyers of exported goods.

IV. THE U.S. DISC RULES

In 1971, the U.S. Congress enacted the first significant group of tax provisions designed to stimulate exports. These are the so-called DISC rules providing favorable tax treatment for income of "Domestic International Sales Corporations." The rules are highly complex and the benefits provided were substantially reduced by changes made in the Tax Reform Act of 1976. On an overall basis, however, the effectiveness of the DISC provisions has been questionable for small and medium-sized companies including those not already engaged in export activities.

Based on the report prepared by the Treasury Department on DISC activities covering the year 1977, while DISC exports represented roughly 64 percent of total manufactured exports for 1977, 81 DISC entities accounted for nearly one-half of all tax deferred income. Large companies have utilized them and believe they have provided a significant export incentive to their activities. As the Treasury statistics evidence, however, DISC has been of limited use for small and medium-sized companies.

Several factors have limited the effectiveness of DISC in assisting and stimulating exports by smaller companies. The sheer complexity of the rules is perhaps the most significant. The statute itself, with subsequent amendments, and the voluminous regulations issued to interpret the statute have created monumental problems of interpretation. A few years ago we prepared a checklist of tests to be met, elections to be made and other technical questions which the DISC regulations required or brought into play. That list was thirty pages long. No small business can handle such complexity. Further, 14 percent of all of the DISCs examined by Internal Revenue Service audit personnel through 1976 were disqualified because of failures to meet technical requirements. Large companies have the resources to deal with these complexities, but they are a continuing source of discouragement to small and medium-sized companies.

DISC is a tax deferral system rather than a reduced tax or exemption approach. Income earned by DISCs can be deferred only if invested in certain types of export related assets. Some companies which considered commencing export activities as a result of the DISC legislation were unable to predict their future ability to invest DISC deferred income in qualified assets to justify incurring the start-up costs associated with entering export markets. Generally the DISC approach has provided too limited an incentive to encourage smaller companies to enter into export activities.

V. SPECIAL EXPORT PROBLEMS U.S. SMALL BUSINESSES FACE

Most of our small and medium-sized clients have not entered the export market to any significant degree. There are several reasons for this.

Market risks and uncertainties

A small business cannot possibly know market conditions around the world. Each country has its unique marketing problems, and most countries are quite different from the United States. Differences in tastes, customs and habits all require special knowledge and sometimes changes in products, to meet specific demands.

A manufacturer of greeting cards, for example, decided to produce cards in French, but the venture was less than successful. The company discovered that cards designed for the Quebec market were not at all appropriate for France.

Even though a product enjoys wide acceptance, its manufacturer often must alter it to meet the specific needs of each country. An electrical equipment maker, for example, followed U.S. requirements and produced each item to handle the maximum possible load of any user--even though many customers may not need such heavy devices. European safety regulations, however, allow lighter (and less expensive) equipment where actual loads are lower than maximum. The U.S. company thus failed in its efforts to compete with European manufacturers.

In both these cases, proper market advice could have helped the companies avoid their costly mistakes. Very few smaller companies can afford to do the market analysis and study necessary to determine if there is a meaningful market in other countries for their products, much less be certain of avoiding costly mistakes of this type.

Customs duties, import regulations

A small business simply cannot afford the time and paperwork needed to comply with the bewildering array of complex export procedures.

Currency problems

To be competitive, exporters often must quote prices in foreign currencies. But many small businesses are not able to afford the risk caused by wide currency fluctuations.

Collection problems

When a foreign customer is slow in paying, a small business may have problems following up on the account.

American entrepreneurs can surmount all of these problems, but the typical small business cannot do it alone--it takes too much time and too high an investment. Even when profit margins are good, the limited export volume that a small company can expect does not justify the effort. A well-organized trading company with contacts throughout the world could help small and medium-sized businesses prevent the mistakes that discourage them from export markets.

VI. SPECIFIC COMMENTS ON S.1663

The trading company concepts embodied in S.1663 are sound and should assist significantly in making export markets available to many U.S. companies that do not now participate in export activities to any degree. As stated earlier, trading companies should be of particular value to small and medium-sized companies that are not able for various reasons to penetrate foreign markets on their own. Accordingly, we are pleased to support the objectives of this legislative proposal.

By providing financial assistance to cover startup costs, and by permitting existing companies and banks to participate in their formation, the proposal should encourage the creation of trading companies in a relatively short time. The long-range restrictions on ownership (20%) should help prevent abuses of the trading company concept.

Section 102 (c)(2) of S.1663 establishes rules for licensing an export trading company where more than 20% of its stock is owned by any person. It provides that licensing will be permitted if "the person or persons whose ownership of stock or interest exceeds the limitation submits a divestiture plan under which he will divest himself of his stock or interest in excess of the limitation over a 10-year period beginning with the year in which the license is issued with-(i) the first sale or transfer of stock or interest occurring not later than the fifth year of such period."

We question the desirability of requiring such a plan at the time an export trading company is licensed. Until a company has been in operation for several years, it will be difficult for its owners to work out a reasonable plan for divestiture to meet the ownership limitations. We believe the objectives of the legislation would be met if the proposed bill were amended to provide that the divestiture plan must be submitted no later than the beginning of the fourth year of operation of the export trading company. This would be one year in advance of the year in which divestiture must commence, and would seem to satisfy the objectives of the plan but provide a more workable rule.

Following are some technical comments about the proposed rules contained in Title II of S.1663, providing tax treatment of export trading companies and their shareholders.

1. Proposed Internal Revenue Code Sec. 1398A would grant complete tax exemption to a licensed export trading company electing to file under its provisions. On page 16, line 10 of the draft legislation, the reference to Section 1398E should probably be to Section 1398C.

2. Proposed Code Section 1398B(b)(1) provides a flow-through to shareholders of a licensed export trading company's net investment credit. Subsections (b)(2) and (3) provide rules for calculating the "net investment credit" that would flow through to shareholders where there may be recapture of prior investment credits in accordance with IRC Section 47. The rules governing the allowance of the credit and recapture on early disposition of assets subject to the credit are very complex and the interrelationship of Subsections (b)(2) and (3) are difficult to follow. What seems to be intended is that the allowance of the investment credit as well as recapture should be based on ownership of the property by the licensed export trading company itself, rather than investments made directly by any of its shareholders. Perhaps this point can be handled by explanatory comments in the Committee report when the Bill is considered.

3. New Code Section 6039C requires a very detailed tax return for an electing licensed export trading company. The information required includes names and addresses of shareholders for each day of the year, numbers of shares owned at all times during the year and detailed information on amounts of money and other property distributed to each shareholder. The Internal Revenue Service should have access to this information to review reporting by the trading company and the shareholders, but we doubt the need to have all of this detailed information included in a tax return form itself required by the statute. Presumably, failure to file all of the information could jeopardize licensed status. We believe the objective of this provision would be accomplished by requiring that an electing export trading company maintain this information in a permanent form for review by the Internal Revenue Service when requested. Further, the company should file information returns (possibly on Form 1099) disclosing amounts to be taxed to shareholders each year based on distributions made.

4. New Code Section 1398C(b) provides a 10-year net operating loss carryover for electing licensed export trading companies. Since these companies will have a tax-exempt status, we are not clear as to the objective of the net operating loss carryover provision. If the intent is that losses accumulated while in licensed status may be carried over to offset profits if licensed status is lost, then we think that point should be made clear either in the statue itself or in Committee report language.

As noted earlier in our discussion of existing DISC rules, our trading partners in GATT have alleged that those rules violate the GATT agreement. The U.S. has made countercharges that certain tax incentive provisions adopted by other countries also violate the GATT agreement. Other countries may make similar charges, with respect to the tax exemption granted to export trading companies under S.1663. Furthermore, the tax incentives included in this bill should be reviewed in light of the multilateral trade agreements recently consummated by our country and a number of others.

In our view, the trading company concept represents a unique combination of incentives (or removal of disincentives) in the export area. Whether it is the right combination of economic and other factors to maximize U.S. exports only the future will tell. Clearly, however, the limitation of tax on export profits to distributed profits (a single tax system) combined with the flow through of tax credits, the partial financing of start-up losses and the removal of unnecessary antitrust constraints on joint export activity will motivate many knowledgeable and innovating persons to become involved in establishing and operating trading companies. The trading company concept, if enacted, should do much to help American business become more competitive in world markets.

Japanese trading companies in 1978 handled between 50% and 55% of Japanese exports. In order to eliminate the 1978 deficit of $16 billion, it would have been necessary to increase U.S. exports 11% from the 1978 level of $144 billion. In light of the Japanese experience with trading companies, such a target for U.S. trading companies would seem to be within the realm of reason.

APPENDIX A

DISTRIBUTION OF THE WORLD'S 100 LARGEST INDUSTRIAL COMPANIES

(Ranked by Sales)

Country	Number of Companies			
	1965	1970	1973	1978
United States	68	63	50	48
West Germany	12	10	12	14
Japan	2	8	11	9
France	3	3	9	10
United Kingdom	9	7	6	6
Italy	2	3	3	3
The Netherlands	1	2	3	3
Other	3	4	6	7
Total Companies	100	100	100	100

Source: *Fortune*, various issues.

APPENDIX B

DISTRIBUTION OF THE NONPETROLEUM COMPANIES THAT ARE AMONG THE WORLD'S 100 LARGEST INDUSTRIAL CORPORATIONS

(Ranked by Sales)

Country	Number of Companies			
	1965	1970	1973	1978
United States	57	49	36	32
West Germany	12	10	12	14
Japan	2	8	11	8
France	3	2	7	8
United Kingdom	8	6	5	5
Italy	2	2	2	2
The Netherlands	1	2	3	3
Other	2	3	5	5
Total Companies	87	82	81	77

Source: *Fortune*, various issues.

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TAX INCENTIVES FOR EXPORTS

	AUSTRIA	PORTUGAL	AUSTRALIA	NEW ZEALAND	JAPAN	CANADA
Taxation of foreign branch income	Fully taxed at usual rate (progressive rates from 30% to 55%). Deduction for foreign taxes paid. Foreign tax credit upon application.	Exemption of 2/3 of income (effective tax rate of 17.6%).	Exempt except if has not been taxed abroad (tax rates from 47.5% to 50%).	Fully taxed at usual rate (tax rates are from 20% to 45%). Foreign tax credit.	Taxable at usual rate (effective tax rate of 52%). Favorable foreign tax credit system.	Fully taxable at usual rate (46%). Foreign tax credit.
Taxation of foreign subsidiaries	None. No subpart F income equivalent.	None. No subpart F income equivalent.	None. No subpart F income equivalent.	None. No subpart F income equivalent.	None. No subpart F income equivalent.	Yes, but under conditions less stringent than under subpart F income.
Deductibility of foreign branch losses	Fully deductible.	Fully deductible.	Fully deductible.	Fully deductible.	Fully deductible.	Fully deductible.
Taxation of foreign source dividends	Exempt if at least 25% control.	Exempt if at least 25% control. One-third taxable in other cases.	Exempt in practice.	Exempt.	Fully taxed at usual rate. Direct and deemed paid foreign tax credit.	Exempt when foreign subsidiary is controlled (50%). Partial exemption from 1976. Foreign tax credit.
Special deferrals of taxable domestic income	Investment reserves.	None.		None.	Income may be deferred for: --overseas market development --overseas investment losses --foreign exchange losses	None.
Specific export tax incentives	10% write-off with respect to acquisition of shares in certain foreign entities. Custom free zones.	None.	Deductions and rebates for export market development expenses.	Deduction of 150% of the cost of export related expenditures. Deduction of an amount related to increased export sales.	--Reserves for overseas market development--Deduction of overseas investments. --Reserves for foreign exchange losses. --Special deductions for certain overseas transactions.	None.
Intercompany pricing rules	-				Favorable treatment for exporting companies.	
Border tax adjustments (VAT)	VAT (rate 16%) zero rate on exports.	None.	None.	None.	None.	None.
Tax incentives indirectly benefiting exports	Accelerated depreciation or tax-exempt investment reserve (1)	Reduced tax rate or exemption from taxation for introduction of new products or processes. Accelerated depreciation.	None.		None.	Tax reduction for manufacturing income. Accelerated depreciation. (1) Investment tax credit.

(1) Most of the tax incentives are granted in connection with industrial and regional development.

TAX INCENTIVES FOR EXPORTS

	BELGIUM	FRANCE	GERMANY	ITALY	LUXEMBOURG	NETHERLANDS
Taxation of foreign branch income	1/8 the usual rate (48%)	Exempt (1) Corporate tax rate is 50%	Normal tax rate (51%) plus foreign tax credit or, in certain cases, imposition of a flat 51% tax rate.	Taxed at usual rate (35%) Foreign tax credit.	Exemption on 50% of income (progressive tax rate from 39% to 49%). Foreign losses deductible.	Taxed at usual rate. Favorable foreign tax credit system.
Taxation of foreign subsidiaries	None. No subpart F income equivalent.	None except if election is made. No subpart F income equivalent.	Yes, but under conditions less stringent than the U.S. subpart F provision.	None. No subpart F income equivalent	None. No subpart F income equivalent.	None. No subpart F income equivalent.
Deductibility of foreign branch losses	Fully deductible even though foreign income is exempt under tax treaty.	Not deductible. (2)	Fully deductible even though foreign income is exempt under tax treaty. (3)	Fully deductible.		Fully deductible.
Taxation of foreign source dividends	Permanent participation (held for more than one year) 95% exclusion plus 5% tax credit. Non permanent participation 15% tax credit.	95% exclusion if French company owns 10% or more of the stock.	Fully taxed at usual rate. Foreign tax credit and deemed paid foreign tax credit under certain circumstances.	Fully taxed at usual rate. Foreign tax credit.	50% exclusion if at least 25% owned. Total exemption for holding companies. Foreign taxes deductible	Exempt in majority of cases.
Special deferrals of taxable domestic income	None.	Income may be deferred for: - Income of certain foreign businesses - Acts of investment in certain business in LDC's - Export credit extended to foreign buyer.	Income may be deferred for: - Income of foreign branches whose income is tax exempt - Income of foreign subsidiaries - Gain realized upon the exchange of property for stock of a foreign corporation.		None.	None.
Specific export tax incentives	None	- Fund exports programs - Election to compute income on a worldwide basis - All special defer rules - Exclusion from the "inflation levy".	None		None.	Tax credit for withholding tax on interest and royalties paid by residents in certain non-treaty LDCs.
Intercompany pricing rules	Will provide accounts on allocation in certain cases. Not specially generous to exporters.	No general rule, but enforced against exporters.	Usually enforced although relaxation may be granted in special circumstances.			Usually enforced but special agreement used. May be negotiated with the tax authorities.
Border Tax adjustments (VAT)	VAT (18% rate) up to 25% for luxury items. Zero rate on exports.	VAT (17% rate) up to 33% for luxury items. Zero rate on exports.	VAT (11% rate). Zero rate on exports.	VAT (12% up to 36% for luxury items). Zero rate on exports.	VAT (rate 10%). Zero rate on exports.	VAT (18% rate). Zero rate on exports.
Tax incentives on directly benefiting exports	- Accelerated depreciation - Exemption from real estate tax - Reduction in income tax rate on certain reinvested profits (4)	- Accelerated depreciation - Exemption from tax of business tax - Reduction of registration taxes (4)	- Accelerated depreciation - Reduction of corporate tax rate and VAT rate (4)	Tax exemption or reduction for foreign trade or government owned companies (4)	Investment credit from 7% to 5% of cost of certain capital assets	Accelerated depreciation (4) Investment tax credit from 5% to 15% of cost of certain capital assets

(1) Foreign branch income is taxable at usual rate if the French company elects to be taxed on a worldwide or consolidated basis.
(2) Losses of foreign branches are deductible when the American company elects to be taxed on a worldwide or consolidated basis.
(3) When the income has not been taxed at usual, the amount deducted for foreign losses must be put back in the income (for a number of years).
(4) Most of the tax incentives are granted in connection with industrial and regional development.

Chart I
Page 3

TAX INCENTIVES FOR EXPORTS

	U.K.	IRELAND	DENMARK	NORWAY	SWEDEN	UNITED STATES
Taxation of foreign branch income	Taxable at usual rate (52%). Foreign tax credit.	Taxable at usual rate. (Average rate 50%). Deduction for foreign taxes paid.	Taxed at half the usual rate (1/2 of 37%). Foreign tax credit.	Exemption on 50% of income (rate is 26.5%).	Taxed at usual rate (effective income tax rate is 54%). Foreign tax credit.	Fully taxable at usual rate (48%). Foreign tax credit.
Taxation of foreign subsidiaries	None. No subpart F income equivalent.	None. No subpart F income equivalent.	None. No subpart F income equivalent.	None. No subpart F income equivalent.	None. No subpart F income equivalent.	Yes, under subpart F provisions.
Deductibility of foreign branch losses	Fully deductible. Deductible against foreign source business income only when carried over to following years.	Fully deductible.	Fully deductible.		Fully deductible.	Fully deductible.
Taxation of foreign source dividends	Fully taxed at usual rate. Direct and deemed paid foreign tax credit.	Fully taxed at usual rate.	Fully taxed at usual rate. Deemed paid foreign tax credit.	Half-exempt if at least 85% control.	Fully taxed at usual rate. Foreign tax credit.	Fully taxed at usual rate. Direct and deemed paid foreign tax credit.
Special deferrals of taxable domestic income	None.		None.	Tax free reserves deductible.		About 25% of taxable income may be deferred under the DISC provisions.
Specific export tax incentives	Deduction of business entertainment expenses connected with export activities.	Exemption from corporate taxes on profits attributable to exports of goods produced in Ireland.		Tax free reserves deductible.	Additional deduction for interest charged on export credit.	None, aside from DISC.
Intercompany pricing rules	Not actively used.				Not actively used.	Strictly enforced, including against export industry. Important cases against exporters pending.
Border tax adjustments (VAT)	VAT (8% rate up to 35% for luxury items). Zero rate on exports.	VAT (19.5% up to 34.5% for luxury items). Zero rate on exports.	VAT (18% rate). Zero rate on exports.	VAT (20% rate). Zero rate on exports.	None.	None at Federal level.
Tax incentives indirectly benefiting exports	Favorable rates of depreciation. (1)	Accelerated depreciation. (1)	Tax-free investment reserves constituted by 20% of annual profits. Dissolved after 10 years. (1)	Accelerated depreciation. Tax-free reserves deductible. (1)	Accelerated depreciation. (1)	Accelerated depreciation, investment tax credit (10%).

(1) Most of the tax incentives are granted in connection with industrial and regional development.

Chart II
Page 1

NONTAX INCENTIVES FOR EXPORTS

	AUSTRIA	PORTUGAL	AUSTRALIA	NEW ZEALAND	JAPAN	CANADA
Nontax incentives indirectly benefiting exports	Investment allowances (1)		None.			Cash grants. (1)
Financing assistance	Guarantees for medium-term credits. Rate of interest is 7%.				Direct loans for medium-term sales. Long-term credits at preferential rates (from 7.5% to 8.75%). Financing of contract value from 48% to 84%. Mixed credits.	
Insurance assistance					Are insured: --production risks --commercial risks --political risks --currency fluctuations --loss of foreign investment. Risks are covered from 60% to 80%.	

(1) Most of the nontax incentives are granted in connection with industrial and regional development.

NONTAX INCENTIVES FOR EXPORTS

	BELGIUM	FRANCE	GERMANY	ITALY	LUXEMBOURG	NETHERLANDS
Nontax incentives indirectly benefiting exports	--Interest subsidies[1] --Investment subsidies (1)	--Grants --Investment subsidies (1)	Grants (1)	--Capital grants --Long and medium term loans by specialized government institutions (1)	--Grants --Loans --Guarantees (1)	--Investment subsidies --Interest subsidies (1)
Financing assistance	Discount at low rates. Interest rebates on export credit. Subsidized medium term export financing. Average rate borne by exporters is 8%. Financing of up to 80% of contract value.	Discount at low rates. Long-term loans at 7.5% rate, to both suppliers or buyers. Financing of up to 100% of contract value. Mixed credits.	Discount at low rates. Guarantees. Long-term credits to both suppliers or buyers. Preferential rates of 10%. Financing of up to 80% of contract value. Mixed credits.	Discount at low rates. Interest subsidies. Long-term loans at 8.95% rate to both suppliers and buyers. Financing of up to 100% of contract value.		Discount at low rates. Guarantees. Subsidized medium and long-term export credits. Average interest rate borne by exporters is 8.5%. Financing of up to 80% of contract value.
Insurance assistance	Are insured: --commercial risks --political risks --currency fluctuations Risks covered from 80% to 100%.	Are insured: --production risks --commercial risks --political risks --currency fluctuations --market development --exhibition expenses --inflation risks Risks are covered from 80% to 100%.	Are insured: --production risks --commercial risks --political risks --currency fluctuations --inflation risks Risks are covered from 80% to 100%.	Are insured: --commercial risks --political risks --currency fluctuations --inflation risks Risks are 90% covered.		Are insured: --commercial risks --political risks --currency fluctuations Insurance usually covers from 75% to 100% of the risks.

(1) Most of the nontax incentives are granted in connection with industrial and regional development. In Belgium, interest subsidies are granted for the purpose of investment throughout the country and not only in depressed areas.

NONTAX INCENTIVES FOR EXPORTS

	U.K.	IRELAND	DENMARK	NORWAY	SWEDEN	UNITED STATES
Nontax incentives indirectly benefiting exports	--Grants --Investment subsidies --Interest subsidies (1) --Employment subsidies (2)	--Investment allowances --Training grants --Loan guarantees (1)	--Loans --Cash grants (1)		--Investment allowances --Loan guarantees (1)	None, except limited agricultural subsidies.
Financing assistance	Guarantees. Interest rate subsidies. Portfolio refinancing. Support granted on a supplier and buyer basis. Interest rate borne by borrowers: 7.8%. Financing of up to 100% of contract value. Mixed credits.	Guarantees. Medium-term loans at preferential rates (8%). Financing of up to 80% of contract value.	Guarantees. Financing of up to 80% of contract value. Interest rate is 8.5% after first year.		Medium and long-term financing at 3% or 3% above discount rate. Financing of up to 100% of contract value.	Discount at medium rates. Guarantees. Long-term export credit financing at interest rates from 8.25% to 8.5%. No mixed credits. Financing of 30% to 85% of contract value.
Insurance assistance	Are insured: --commercial risks --political risks --production risks --inflation risks --currency fluctuations --performance bonds Risks are covered up to 100%.	Are insured: --production risks --commercial risks --political risks --currency fluctuations Risks are covered up to 100%.	Are insured: --commercial risks --political risks --currency fluctuations Risks are covered from 65% to 90%.		Are insured: --commercial risks --political risks --currency fluctuations --inflation risks Risks are covered up to 90%.	Are insured: --commercial risks --exhibition expenses --political risks Risks are covered up to 95%.

(1) Most of the nontax incentives are granted in connection with industrial and regional development.
(2) Granted in order to encourage employers to retain employees.

Chart III

TAX INCENTIVES FOR EXPORTS*

	Belgium	France	Germany	Italy	Luxembourg	Netherlands	U.K.	Ireland	Denmark	Norway	Sweden	Switzerland	Austria	Portugal	Australia	New Zealand	Japan	Canada	U.S.
Partial or total exemption on foreign branch income	X	X	X		X				X	X		X		X	X				
Foreign subsidiaries not subject to tax	X	X		X	X	X	X	X	X	X	X	X	X	X	X	X	X		
Foreign branch losses deductible	X		X	X	NA	X	X	X	X	NA	X		NA	NA	X	NA	X	X	X
Partial or total exemption on foreign source dividends	X	X			X	X			X			X	X	X	X	X		X	
Special deferrals of domestic income		X	X	NA				NA		X	NA				NA		X		X
Export tax incentives		X				X	X	X	NA	X	X		X		X	X	X		DISC only
Non-enforcement of intercompany pricing rules	X	X		NA	NA	X	X	NA	NA	NA	X	NA	NA	NA	NA	NA	X		
Border tax adjustments	X	X	X	X	X	X	X	X	X	X			X						

* X indicates country has incentives.
NA indicates that information not available.

Chart IV

NONTAX INCENTIVES FOR EXPORTS*

	Belgium	France	Germany	Italy	Luxembourg	Netherlands	U.K.	Ireland	Denmark	Norway	Sweden	Switzerland	Austria	Portugal	Australia	New Zealand	Japan	Canada	U.S.
Nontax incentives indirectly benefiting exports	X	X	X	X	X	X	X	X	X	NA	X		X	NA		NA	NA	X	
Financing Assistance														NA	NA	NA		NA	
- Rate of interest	8%	7.5%	10%	8.85%	NA	9.5%	7.5%	8%	8.5%	NA	(1)	NA	7%				7.5-8.7%		8.25-9.5%
- Portion of contract value financed	80%	100%	80%	85%	NA	80%	100%	80%	80%	NA	100%	NA	NA				48-64%		30-55% (to buyers)
- Mixed credits		X	X														X		
Insurance Assistance					NA					NA		NA	NA	NA	NA	NA		NA	
- Commercial risks	X	X	X	X		X	X	X	X		X						X		X
- Political risks	X	X	X	X		X	X	X	X		X						X		X
- Production risks		X	X				X	X									X		
- Currency fluctuations	X	X	X	X		X	X	X			X						X		
- Performance bonds							X												
- Market development		X																	
- Exhibition expenses		X																	X
- Inflation risks		X	X	X			X				X								

* X indicates country has incentives.
NA indicates that information not available.
(1) 2% or 3% above discount rate.

APPENDIX D

TAXATION OF FOREIGN BUSINESS OPERATIONS BY BELGIUM

Foreign Branch Operations

In principle, a company resident in Belgium that conducts business through a branch in another country is subject to current Belgian tax on a portion of the foreign branch profits. Conversely, losses sustained by the branch are currently deductible against the income of the Belgian company.

The income of a branch located in a country with which Belgium has an income tax treaty is exempt from Belgian tax. If losses from a branch in a treaty country have been deducted in Belgium and subsequent profits of the branch are not taxed in the branch country because of loss carry-overs there, those profits are fully taxed in Belgium. If the branch is located in a country that has no treaty with Belgium, the Belgian income tax applicable to this income is reduced by three-fourths. Foreign income taxes paid are deductible. The branch income may qualify for this reduction only if the branch is actually a permanent foreign establishment that maintains separate accounting records.

Foreign Subsidiary Operations

If the Belgian company operates in another country through a subsidiary rather than a branch, profits are not currently taxable and losses are not currently deductible. Tax at the normal corporate rate is imposed when the subsidiary distributes dividends. However, 95% of foreign dividends received, net of foreign taxes, are excluded from taxable income provided the shares in the foreign corporation have been held for a full taxable year. The remaining 5% of foreign dividends received is considered to represent financial and administrative expenses included in the recipient corporation's deductions attributable to this dividend income.

A foreign tax credit of 5% can be applied against the recipient corporation's tax liability; any excess of the credit over the liability will be refunded. Dividends subject to the 95% exclusion must be grossed up for the amount of the 5% foreign tax credit.

The overall effect is that foreign dividends flow through the Belgian corporation to its shareholders without any further corporate tax.

If the shares of the foreign corporation have not been held for a full taxable year, the net dividend received is taxable. A credit of 15% of that amount is granted.

Foreign Tax Credit

Normally, a direct foreign tax credit is not allowed when profits from a branch operation are currently taxable in Belgium. Double taxation of such foreign income is avoided by the exclusion (or exemption) of the income

from taxable income by tax treaty or through a tax rate reduction of 75% in the absence of a treaty. As already described, a limited foreign tax credit applies when foreign dividends are received.

A fixed foreign tax credit also applies on foreign interest and royalty payments if such income was taxed in a foreign country. Such interest and royalties generally are subject to the Belgian corporate tax. Applicable foreign income taxes are deductible in determining the corporate taxable income. In addition, a 15% foreign tax credit applies to such interest or royalty income. The credit is applied against the current income tax liability of the Belgian corporation. Any excess credit is unusable. No expenses need be allocated against the foreign-source interest or royalty income.

TAXATION OF FOREIGN BUSINESS OPERATIONS BY FRANCE

Foreign Branch Operations

In France, the principle of territoriality applies in that only income generated from activities in France is taxable. A company resident in France that operates through a branch in another country generally is not subject on a current basis to French tax on the foreign branch profits. Likewise, losses sustained by the branch are not currently deductible against the other income of the French company.

Expenses of starting foreign operations represent an exception to the general rule relating to the nontaxability of foreign profits. A deductible reserve for these expenses is permitted; however, this reserve must be added back to taxable income in equal installments during the sixth to tenth years following the year of deduction. Start-up costs related to sales and information or study offices located in foreign countries generally qualify for this treatment. The total allowable reserve varies according to the foreign country involved. For European Economic Community countries, the total allowable annual reserve is equal to the losses incurred during each of the first five years, but the amount generally is limited to the capital invested during that period. For all other foreign countries, except those considered to be tax havens, the reserve is equal to the capital invested during the first five years, irrespective of the losses incurred.

A similar tax deduction is available in France for industrial operations in prescribed underdeveloped countries if prior approval is obtained from the Ministry of Economy and Finance. The amount of the deductible reserve must be negotiated with the tax authorities but cannot exceed one-half of the funds invested in the first five years.

The French law also provides that a taxpayer may enter into an agreement with the Minister of Finance to permit the current inclusion of the results of foreign branch operations in taxable income. The Minister's consent is difficult to obtain, and this privilege, called "benefice mondial," has been

granted to only about 20 entities in France. For these few companies, the tax paid to the foreign country is creditable against the French income tax but only to the extent of 50% of the income.

Foreign Subsidiary Operations

Generally, if the French company operates in another country through a foreign subsidiary, profits are not currently taxable and losses are not currently deductible. Dividends received from a 10%-or-more-owned subsidiary are not taxable in France. However, expenses equal to 5% of any dividend received are deemed to be attributable to the tax-exempt income and are included in taxable income. If the parent incurs and can prove expenses of less than 5% of the distribution, then the inclusion in taxable income is limited to this lesser amount. Dividend withholding taxes paid to the other country are not deductible.

An exception to the noninclusion of subsidiary profits in current taxable income permits the consolidation of all foreign subsidiaries and branches in a single tax return. To be included, any subsidiary must be at least 50% owned. The use of this procedure requires permission of the Minister of Finance. In practice, this permission is almost never given. A credit is allowed for foreign income taxes paid up to 50% of the foreign income.

The deduction for losses and subsequent return to taxable income (as described in the section dealing with branches) is also applicable if the foreign subsidiary is at least 50% owned. Under those circumstances, current subsidiary losses can be offset against other taxable French income. French companies operating outside of France that grant medium-term loans (such as the sale of merchandise on extended terms) are allowed to establish a reserve, which is deductible for tax purposes, amounting to 10% of the amount receivable from the loans.

Royalties or the proceeds from the sale of patent rights received by a French company are taxable to French entities at a reduced rate of 15%. This rate applies to royalties resulting from agreements between affiliated entities when the licensee is a foreign company.

Foreign Tax Credit

The law in France does not provide specifically for a direct or deemed foreign tax credit since most of the foreign income involved is not taxable. As previously discussed, there are provisions that allow for the consolidation of all foreign subsidiaries and branches or the inclusion of all branches in one tax return. In such circumstances, a credit is allowed against the French tax but may not exceed 50% of the foreign income included in the return. The limitation is computed on a per-country basis. For unused credits, there is a five-year carry-over period; if the taxes are not claimed as a credit during that period, they become automatically deductible.

A foreign tax credit is allowed for certain withholding taxes applicable to taxable income if the credit is provided for in a treaty. As an investment incentive, some treaties provide for a credit higher than the tax withheld. There is no provision for a carry-over or carry-back of an unused credit. If it cannot be utilized, it becomes immediately deductible.

French law does not require allocating indirect expenses against foreign-source income for purposes of a foreign tax credit limitation although direct expenses are allocable against such income.

TAXATION OF FOREIGN BUSINESS OPERATIONS BY GERMANY

Foreign Branch Operations

A company resident in Germany that conducts business operations through a branch in another country is subject to German corporate income tax on the foreign branch profits on a current basis. Conversely, for corporate income tax purposes, losses sustained by the branch are currently deductible against its other income.

Generally, where Germany has entered into double taxation treaties with other countries, the right to tax profits attributable to a permanent establishment rests with the country where such permanent establishment is located. Therefore, profits from a branch that qualifies as a permanent establishment are exempt from German tax. Conversely, losses incurred by a foreign branch located in a treaty country are not deductible for German income tax purposes.

Normally, the transfer of assets from a domestic business enterprise to a branch or subsidiary in a foreign country requires the disclosure and taxation of unrealized gain relating to such assets. Under the Foreign Investment Tax Law, an amount not in excess of such a gain may be transferred to a tax-free reserve for five years. At the end of this period, the reserve must be credited to taxable income in annual installments of at least one-fifth of the reserve.

The Foreign Investment Tax Law also allows a German resident company to apply for permission to currently deduct losses generated by a permanent establishment located in a country that has a double taxation treaty with Germany. Permission is granted if the losses are computed according to German tax and accounting standards. The loss deduction is available only for corporation income tax purposes and not for the municipal trade tax on income. To the extent losses have been claimed, subsequent years' profits from the branch (which would normally be exempt from tax by treaty) are subject to German tax to the extent the foreign branch is able to utilize the prior-year losses through a tax loss carry-forward in the local country. Similarly, any branch loss claimed must be included in German income in subsequent years if the foreign branch is incorporated, unless the branch loss carry-forward in the local country is lost through the incorporation.

Foreign Subsidiary Operations

If the German company operates in another country through a subsidiary, the profits are not currently taxable and losses are not deductible. Tax is normally imposed only when dividends are paid. If the operations of a foreign subsidiary are located in a "developing" country, as defined in the Developing Countries Tax Act, effectively no tax is levied on the dividends since the amount of foreign tax creditable against the income is assumed to be equal to the amount of tax attributable to the dividends.

One exception exists to the basic rule of taxing only remitted earnings. The income of foreign base companies controlled directly or indirectly (more than 50% control) by shareholders resident in Germany, and under certain circumstances by nonresident German citizens, is taxed currently to the shareholders without payment of dividends. A deemed foreign tax credit is allowed. Foreign base company income is taxed if:

1. The income is subject to an effective tax rate of less than 30% in the country of operation.
2. The passive income of the foreign company together with foreign base company sales and services income exceeds 10% of its total gross income. Foreign base company income below 10% of the foreign company's total gross income is taxed if the aggregate amount, otherwise exempt, that is allocable to a German shareholder exceeds DM 120.00.

These provisions, which are similar to the U.S. Subpart F provisions, were modeled after the U.S. provisions.

Under the German Foreign Investment Tax Law, a domestic corporation that directly owns at least 50% of the share capital of a foreign corporation (25% if the foreign corporation is located in a "developing" country) may establish a tax deductible reserve for that portion of the foreign subsidiary's losses applicable to investments made after December 31, 1968. However, the investments made after December 31, 1968, must have (1) increased the parent's ownership to 50% or more or (2) when added to previous investments, increased the ownership to at least 50% and (3) must be at least 5% of the subsidiary's capital. Unincorporated resident taxpayers may qualify for the same benefit.

There are certain other prerequisites for establishing the tax deductible reserve. The foreign subsidiary must have income from industrial or commercial activities (leasing or licensing income is nonqualifying). The subsidiary's loss must be computed under German tax accounting rules, and any foreign tax incentives claimed must be disregarded. Certain documentation must also be provided to the German tax authorities to prove the loss, and the foreign subsidiary must authorize the local tax administration to provide information to the German tax authorities upon request.

The tax-free reserve must be recaptured as taxable income to the extent subsequent profits are generated by the subsidiary. It must also be recaptured

to the extent a write-down of the investment is claimed by the parent corporation or to the extent the reserve is allocable to shares sold by the domestic corporation. The parent may claim a write-down after a consistent pattern of serious losses occurs. The reserve must be recaptured in full at the end of five years after the year in which such reserve was established.

In addition to the above reserves resulting from current losses of a foreign subsidiary, other reserves may be established for qualifying investments made in developing countries (that are covered under the Developing Countries Tax Act) after December 31, 1973, and before January 1, 1979. An extension of this date is generally expected. A transfer of 40% to 100% of the cost of an investment to the tax-free developing country reserve is permitted for six years. At the end of six years, the reserve must be credited to taxable profits in annual installments of at least one-sixth of the reserve. For investments in labor-intensive enterprises, the annual installments must equal at least one-twelfth of the reserve. This reserve may not generate or increase a tax loss of a resident. It appears that under certain circumstances a deduction may be allowed relating to the same investment under both the Foreign Investment Tax Law and the Developing Countries Tax Act.

Foreign Tax Credit

German law provides for an extensive system of granting relief from double taxation through a foreign tax credit where income is subject to tax both in Germany and another country. The requirements for claiming the credit are similar to the U.S. rules in that the claimant must be a German resident taxpayer and the foreign-source income must also be subject to German tax. The foreign income taxes claimed as a credit qualify only if they are national taxes as opposed to state or local taxes. All double taxation agreements concluded by Germany specify which foreign income taxes qualify for the foreign tax credit and when foreign-source income may be taxed by the source country as well as Germany.

Those taxes not qualifying for the foreign tax credit may be claimed as a deduction if allocable to income taxable in Germany.

A limitation on the allowable foreign tax credit must be computed on a per-country basis, similar to the U.S. method. The credit may not exceed the German tax allocable to the item of foreign-source income. Also, qualifying foreign income taxes are creditable only to the extent they apply to taxable foreign-source income from the same tax year.

The foreign-source income includable in the German company's taxable income is determined after deduction of those expenses incurred directly in earning that income. Indirect administrative expenses normally need not be allocated against that income.

Upon application, a foreign tax credit is allowed for the taxes deemed to have been paid by a foreign corporation. The credit is allowed only if the resident corporate shareholders own 25% or more of the foreign corporation's capital shares and the profits received from the foreign corporation

have been earned through the active conduct of a trade or business. For dividends received from a qualifying subsidiary with management and legal situs in a developing country, a hypothetical tax at the German rate is granted as a tax credit, irrespective of actual taxes paid by the foreign subsidiary.

If a first-tier subsidiary, which is at least 25% owned by a German corporation, in turn owns at least 25% of the voting stock of a second-tier foreign corporation, which also pays dividends, upon application, the dividend is treated as if received directly from the second-tier subsidiary. This can occur only if the German corporation's indirect ownership in the second-tier subsidiary through the first-tier subsidiary is at least 25%. The profits received from the second-tier subsidiary must be earned through the active conduct of a trade or business. The mechanics of computing the deemed credit for first- and second-tier subsidiaries are generally similar to the U.S. method. The German tax law requires the taxpayer to adjust the foreign subsidiary's profits to the German accounting standards. The adjustments are similar to those required by U.S. law.

The treatment of dividends received from a first-tier subsidiary, of course, depends on the treaty provisions applicable to its country of incorporation. If the second-tier subsidiary is domiciled in a treaty country, either the dividend to the first-tier subsidiary is not taxable or, if no such exemption is provided for in the treaty, the tax credit system described above applies. In addition, German tax treaties with developing countries mostly have tax-sparing clauses for dividends, interest and/or royalty payments to Germany. If the developing country grants a tax holiday or reduces withholding taxes, the foreign tax credit allowed to the German corporate recipient will be based upon a higher tax rate than the one actually paid.

TAXATION OF FOREIGN BUSINESS OPERATIONS BY ITALY

Foreign Branch Operations

Business income in Italy is generally subject to two income taxes: a corporate tax at a rate of 25% and a local income tax at a rate of 15%. As the local tax is a deductible item for the corporate tax, the effective overall income tax rate is 36.25%. A company resident in Italy that conducts business operations through a branch in another country is subject to the corporate income tax on foreign branch profits on a current basis. The local income tax does not apply if the branch has separate management and accounting. Conversely, losses sustained by the branch are currently deductible against the other income of the company for corporate tax purposes. A foreign tax credit can be claimed against the corporate tax for income taxes paid abroad by the branch.

Foreign Subsidiary Operations

If the Italian company operates in another country through a subsidiary, undistributed profits are not currently taxable. Distributed profits are subject only to corporate income tax, and then only 40% of such distributions are taxable. Losses sustained by the foreign subsidiary are, in effect, allowed as deductions for purposes of both the corporate and local income taxes. This results from a provision in the law that allows a company to reduce the carrying value of investment not quoted on an exchange by the proportionate reduction in net book value of the subsidiary as reflected by its latest approved financial statements. If the subsidiary's stock is quoted on an exchange, a deduction is allowed to the Italian company to the extent necessary to reduce the investment to market price, based on the average price during the last quarter of the year.

Foreign Tax Credit

The foreign tax credit is a new feature of the Italian tax law that became effective January 1, 1974. Italian corporations that are subject to the Italian corporate tax on foreign-source income, i.e., dividends, branch profits, royalties, etc., may claim a credit against Italian corporate tax for foreign income taxes actually paid abroad.

The credit is allowed only to the extent that the foreign country imposing the tax reciprocally allows a foreign tax credit. It is limited to the lower of (1) the actual taxes paid, (2) two-thirds of the corporate tax when the foreign country also allows a credit on income of the same nature or (3) 25% of the corporate tax when the foreign country does not allow a reciprocal credit. For foreign branch operations, the credit can be claimed for foreign income taxes imposed on branch profits. For a foreign subsidiary operation, the credit can be claimed for withholding taxes on dividends paid but not for the underlying foreign tax paid by the subsidiary itself.

TAXATION OF FOREIGN BUSINESS OPERATIONS BY JAPAN

Foreign Branch Operations

A Japanese company that conducts business operations through a branch in another country is subject to Japanese tax on the foreign branch profits on a current basis. A foreign tax credit for taxes paid in the other country is allowed; the mechanics will be described below. Conversely, losses sustained by the branch are currently deductible against the other income of the Japanese company.

Foreign Subsidiary Operations

If the Japanese company operates in another country through a subsidiary rather than a branch, profits are not currently taxable at the present time and losses are not currently deductible. Tax at the normal corporate rate is

imposed when dividends are distributed from the subsidiary with a deemed foreign tax credit generally being available.

As of April 1, 1978, Japan will tax currently income of certain subsidiaries whether distributed as a dividend or not (a modified form of Subpart F income). Proposals (not yet in legislative form) indicate the following rules may be involved:

1. Current earnings (after March 31, 1978) of an overseas subsidiary in tax-haven countries will be taxed currently with the parent company's taxable income.
2. A subsidiary in a tax-haven country is defined as a company owned over 50% directly or indirectly by the Japanese parent company or its related parties.
3. An overseas subsidiary not carrying on substantial business activity in the tax-haven country would be taxed unless Japan has a tax treaty with the country.
4. Tax-haven countries would be countries (including treaty countries) that have the following conditions:
   a. No corporation taxation,
   b. An effective tax rate of 25% or less on corporate income or
   c. No taxation on offshore source income.

Subsidiary losses create tax benefits recognized only upon liquidation or bankruptcy of the subsidiary or when there has been a "significant deterioration" of the value of the subsidiary. A "significant deterioration" occurs when the value of the original investment has decreased by 50% and there is little prospect of recovery in the future. If these events occur, the parent company may, for tax purposes, write down the value of its original investment to the current value.

The parent company has the option of deducting a reserve for foreign investments. A reserve of 30% may be claimed in the initial year for investments in underdeveloped countries. A reserve of 40% to 100% is available in any country for companies organized to develop natural resources. After five years, the reserve is restored to income in five annual installments.

Foreign Tax Credit

The Japanese law provides for an extensive system of granting relief through a foreign tax credit where income is subject to taxation in Japan and another country. The requirements for claiming the credit are similar to the U.S. rules in that (1) the claimant must be a Japanese resident taxpayer and (2) the foreign-source income must also be subject to Japanese and foreign tax. In addition, a Japanese resident company that owns at least 25% of the voting stock of a foreign subsidiary may claim a credit for taxes deemed to have been paid by the foreign subsidiary when a dividend is received from that subsidiary. This credit is similar to the U.S. deemed credit under Section 902.

A limitation on the allowable foreign tax credits must be computed on an overall basis. Originally, Japanese tax law provided for a per-country limitation; then the concept of the overall limitation was introduced and the taxpayer was permitted to elect either method. In 1963, the per-country limitation was deleted from the law and only the overall limitation remains.

For purposes of computing the overall limitation, any loss incurred by a foreign branch need not reduce other foreign-source income. This provision is referred to as the "modified" overall limitation.

In practice, the Japanese authorities do not normally allocate indirect expenses to foreign income.

The deemed foreign tax credit is allowed for taxes paid by a foreign subsidiary if the Japanese parent owns at least 25% of the issued and outstanding stock for an uninterrupted period of at least six months before the dividend is received. This credit is available upon receipt of a dividend from a "qualified" foreign subsidiary. To qualify, a foreign subsidiary must carry on an active business and may not be a tax-haven-type corporation organized for the purpose of reducing income tax in Japan.

The mechanics for computing the deemed foreign tax credit are similar to those of the U.S. credit. The ratio of the dividend received to the foreign income (net of foreign taxes) is multiplied by the foreign tax to determine the tax deemed paid. The amount of foreign tax deemed paid is included in the Japanese parent's income and is included in foreign-source income when computing the overall limitation. The deemed credit is allowed only for taxes paid by directly owned subsidiaries; taxes paid by second- or third-tier subsidiaries do not qualify.

The Japanese tax law does not require the taxpayer to substantially adjust a foreign subsidiary's earnings and profits to the Japanese standards when computing the deemed credit. The profits to be used for computing the foreign tax credit are either the profits as shown by the foreign financial statements or taxable income as reflected on the tax return, whichever is greater. There are certain minor adjustments that should be made regardless of whether financial statement income or taxable income is utilized. For example, if there is any income that is not subject to foreign income tax, it must be included in foreign-source income for purposes of the deemed credit calculation.

Unused foreign tax credits may be carried forward to the five taxable years following the year in which the foreign income taxes are paid or accrued. Also, the current-year credit may be increased to the extent the foreign income limitation exceeded available credits during the five previous years. Thus, either the excess foreign tax credit or the unused limitation can be carried forward five years. Refunds of prior years' income taxes paid are not granted; instead, the procedure is simply to increase the foreign tax credit in the current year by recomputing the Japanese taxes paid on foreign-source income including that of prior years.

TAXATION OF FOREIGN BUSINESS OPERATIONS BY THE NETHERLANDS

Foreign Branch Operations

A company resident in The Netherlands that conducts business operations through a branch in another country is subject to The Netherlands tax on the foreign branch profits on a current basis. However, a foreign tax credit for taxes paid in the other country is allowed; the credit can effectively make the branch profits tax exempt (the mechanics are described below). Conversely, losses sustained by the branch are currently deductible against the other income of the company. However, to the extent branch losses reduce current taxable income from Dutch sources, the losses will be recaptured against future branch profits of the next six years that might otherwise not be taxed because of the credit. If foreign branch income exceeds total net income of a Netherlands corporation, the excess may be carried forward as excludable foreign income in the six following years.

Foreign Subsidiary Operations

If The Netherlands company operates in another country through a subsidiary, the profits or losses of the subsidiary are normally not taxable or deductible. Any dividends received by the parent corporation are exempt from tax, provided the parent operates as an integrated business (and not a pure holding company), owns at least 5% of the share capital of the foreign subsidiary and the subsidiary is subject to some kind of foreign income tax. If the subsidiary's income is not subject to foreign tax, dividends it pays are not exempt from tax.

Foreign Tax Credit

The Netherlands has entered into numerous income tax treaties in order to avoid double taxation of income. Normally, foreign tax credits are granted in The Netherlands in accordance with the provisions of these treaties. If no treaty exists, The Netherlands law includes unilateral provisions for the avoidance of double taxation.

In theory, a Netherlands corporation is subject to Dutch corporate taxation on its worldwide income. However, if, in accordance with a tax treaty, an item of income is excluded from Dutch taxation, a tax credit is granted in order to comply with the provisions of that treaty. Generally speaking, the Dutch tax credits are limited to the Dutch tax due on the foreign income. Under most Dutch treaties, the foreign tax credit is determined by multiplying the total Dutch tax due on worldwide income by a fraction, the numerator of which is the foreign-source income and the denominator of which is worldwide income.

In cases where no tax treaty has been negotiated with a particular country, a Netherlands corporation may claim a foreign tax credit only on certain specific types of foreign income, including profits from a foreign branch or

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partnership, income from real estate located outside The Netherlands and income from loans secured by mortgages on real estate located outside The Netherlands. The foreign tax credit would be computed as described above. In determining the allowable foreign tax credit, an overall limitation is utilized permitting a taxpayer to group all foreign-source income, including losses.

In addition, a foreign tax credit is granted (whether a treaty exists or not) to a resident corporation against tax due on dividends, interest and royalties received from a debtor in a "development country," if the dividends, interest and/or royalties are subject to income tax in the development country. This tax credit is limited to the lower of the tax levied in the development country (for dividends limited to 25%) or The Netherlands corporate income tax due on the income. There are presently about 100 qualifying development countries.

Foreign taxes paid on any other type of foreign income are not allowed as foreign tax credits in the absence of treaties. Where foreign income is included in taxable income and no tax credit is allowed, any foreign taxes paid on the income can be claimed as a deduction.

All direct and indirect expenses of earning foreign-source income must be allocated against that income in computing the applicable foreign tax credit limitation unless an applicable tax treaty holds otherwise. There are no specific statutory guidelines on the mechanics of allocating indirect expenses.

The Netherlands law does not provide for the deemed foreign tax credit similar to the Section 902 credit in the United States since the dividends involved are not taxed.

TAXATION OF FOREIGN BUSINESS OPERATIONS BY THE UNITED KINGDOM

Foreign Branch Operations

A company resident in the United Kingdom that conducts business operations through a branch in another country is subject to U.K. tax on the foreign branch profits on a current basis. A foreign tax credit for taxes paid in the other country is allowed; the mechanics are described below. Conversely, losses sustained by the branch are currently deductible against the other income of the U.K. company.

Foreign Subsidiary Operations

Assuming the U.K. company operates in another country through a subsidiary, which is a nonresident U.K. company rather than a branch, profits are not currently taxable and losses are not currently deductible. Tax at the normal corporate rate is imposed when dividends are distributed from the subsidiary. Generally, a foreign tax credit is available (see details below).

The exchange control rules of the Bank of England require annual repatriation of two-thirds of the combined profits of overseas subsidiaries. The U.K. parent company may select foreign subsidiaries with high foreign tax credits from which to pay dividends, if it wishes.

Foreign Tax Credit

The U.K. law provides for an extensive system of granting "double taxation relief" through a foreign tax credit where income is subject to taxation in the United Kingdom and another country. The requirements for claiming the credit are: (1) the claimant must be a U.K. resident taxpayer and (2) the foreign income must also be subject to U.K. tax.

In addition, a U.K. resident company directly or indirectly controlling not less than 10% of the voting power of a foreign subsidiary may also claim credit for the "underlying" corporate income tax paid by the foreign subsidiary when a dividend is paid to the parent. This credit is broadly similar to the United States deemed credit under Section 902.

If a foreign tax credit is not allowable or not claimed, a deduction for those taxes (withheld or underlying) may be claimed. The limitation on the allowable foreign tax credit claimed must be computed on each separate "source" of foreign income and the credit is limited to the greater of the foreign tax or the U.K. tax payable on that particular source of income. The income from each separate subsidiary or branch is considered a separate source of income. Because of this rule, there is no overall limitation in the U.K. law. Furthermore, unused foreign taxes may not be carried back or forward to another year. However, U.K. companies with varied overseas interests commonly incorporate an overseas holding company, which receives all foreign dividends from the subsidiaries and thereafter pays a single dividend to the U.K. parent company. Thus, there is only one source of income for U.K. tax purposes and, effectively, the averaging of foreign taxes (as the U.S. overall limitation allows) is possible in the United Kingdom.

The foreign-source income includable in a U.K. company's taxable income is determined after the deduction of those expenses incurred directly in earning that income. The allocation of indirect expenses against that income is not normally required in the United Kingdom.

As mentioned above, a foreign tax credit is allowed for the "underlying tax" incurred by a foreign subsidiary, provided the U.K. parent company owns not less than 10% of the voting power of the subsidiary. There is no restriction on the number of tiers of subsidiaries for which the "underlying" tax credits may be obtained, provided the 10% ownership exists at each level of the chain of ownership. Unlike the United States, the ownership requirement is examined directly at each tier level and the law is not concerned with the effective percentage of ownership. For example, if U.K. resident company A owns 10% of foreign company B which in turn owns 10% of foreign company C, company A can receive a credit for its proportionate share of the

underlying taxes paid by companies B and C, provided dividends are paid through the chain of ownership.

The mechanics for computing the underlying tax credit are generally similar to the U.S. method of computing the deemed credit for a developed country corporation. The taxes in the "underlying tax" credit are normally computed on an accrual basis adjusted to the amount actually paid. The U.K. tax law does not require the taxpayer to adjust the foreign subsidiary's earnings and profits to the U.K. standards. Instead, the profits to be used for computing the foreign tax credit are distributable profits as determined from the foreign company's financial statements.

Foreign tax credit benefits may be restricted by payments of Advance Corporation Tax (ACT). ACT is collected as a percentage of dividends paid. It is creditable in arriving at the annual corporation tax liability subject to certain limits. Foreign tax credits must be taken into account before crediting ACT. The impact of the rules involved varies according to the rates of overseas taxes, the ratio of overseas to U.K.-source income and the level of dividends paid. Where the U.K. business has significant foreign-source income subject to high foreign taxation, part or all of the foreign tax credits will be lost.

Mr. KAPNICK. Finally, in concluding, I must say, Mr. Chairman, that as a member of your constituency and as a person deeply committed to improving the world of small and medium-sized business, I congratulate you on introducing this bill and adding to the debate on the need for expanding exports for our country.

Senator STEVENSON. I thank you, sir. We Illinoisans just recognize what is good for Illinois is good for the country.

Mr. KAPNICK. It's good for New Hampshire too. [Laughter.]

Senator STEVENSON. That is an exceptionally helpful statement, and I will do all I can to see that it gets a wide audience. I know it has taken a great deal of effort from you and your colleagues and others in your firm. I note just looking at it hurriedly that it contains, in addition to the statements, valuable, perhaps unique source material, including the chart on comparative tax incentives for exports, which would make interesting reading for people in Washington. I want to come back to that in a minute.

Mr. Kapnick, Arthur Andersen is a worldwide firm, is it not?

Mr. KAPNICK. Yes, sir. We operate in nearly 40 countries.

Senator STEVENSON. So you and your colleagues are familiar with accounting procedures, tax laws, industrial policies of many, many countries.

Mr. KAPNICK. That's right.

TAX CONCESSIONS

Senator STEVENSON. You have been in a unique position, I submit, to give us an informed opinion on the value of these bills. Now, as has been mentioned, S. 1663 includes some so-called tax concessions for trading companies. There is strong recognition here that when it gets started, it will need some assistance. For that purpose, as well as their continuation, there are some tax concessions. Those provisions of the code or amendments to the code have

drawn a complaint that they would violate the GATT codes against export subsidy. Have you considered that complaint? If so, are there ways, either by this device or by others, of achieving the same objective, but without violating the GATT codes?

Mr. KAPNICK. Mr. Chairman, I am sure you recollect that I am a member of the Presidential Advisory Commission for the Multinational Trade Negotiations. Therefore, I am quite familiar with some of the results of the Trade Act which you have already addressed. I would like to analyze that in two ways, if I could, for you.

First of all, I understand that there is some concern over those issues, but if we analyze what you are proposing, it's a matter that is before the Congress already in some of the debate on whether or not there should be an integration of the tax code between shareholders and corporations. As I see it, one of the things you are proposing is an integration for just a small part. As it affects the GATT discussions, it seems to me that's the place this area should be resolved, we think it's good for the United States. The most significant part of the GATT negotiations for our country was to provide a mechanism by which you could resolve differences between countries.

If you recollect, there are many, many countries overseas that have already integrated their tax systems, and it seems to me that we, as a nation, have a right to do this for a small segment of our economy. The place to negotiate that out is the international scene, where we have set up procedures whereby these can be resolved.

We have somewhat the same difficulty with the DISC issue. The most important thing is, do what is best for our country and negotiate our positions out on an international scene.

Senator STEVENSON. DISC is grandfathered, is it not, in the code? I think so.

It's a question of whether this is an export subsidy, I guess. Existing subsidies, including DISC, would be grandfathered.

Mr. KAPNICK. I think it's a means of our taxing our companies, as we see it, and if we take the position that it is an export subsidy, if you study other countries tax incentives, there are many that also should be considered in the same light. It seems to me that we have to protect our own nation and think in terms of how are we going to improve our sell side of the equation and then negotiate on a pretty hard basis on an international level to eliminate those that are export subsidies elsewhere, if they put ours in the same category.

Senator STEVENSON. Do the trading companies of foreign countries enjoy tax concessions similar to those proposed in S. 1663?

Mr. HOEFS. The principal one you would be referring to is Japan. Japanese trading companies don't enjoy features that are similar to those proposed in this bill. They do have some provisions to assist in the form of certain allowances that are described in our statement. However, those allowances are available to all Japanese companies. They are not limited to the trading companies. Presumably, they are of value in assisting the Japanese trading companies. As I remember the particular provisions, one, for example, provides some recognition for foreign exchange losses on export activity in a way which provides an acceleration of the deduction.

Right now the second one escapes me. Bill Penick points out the second one relates to bad debt treatment on export activities.

These are not limited to Japanese trading companies but are available for all Japanese companies whether they use a trading company or not.

Senator STEVENSON. The Treasury yesterday was not so enthusiastic about this proposal as the Commerce Department, but indicated that its attitude might change if enactment of S. 1663 with its changes in the Internal Revenue Code was accompanied by a repeal of DISC. How would that hit you?

Mr. KAPNICK. If you are going to move along that line, it might be desirable to reconsider the limitations on the ownership of trading companies, where you get down to the 20 percent at the end of 10 years. I happen to believe we have two export problems in the United States. We don't have one. We have very large multinational companies where DISC provides a very real incentive for them to develop their exports. By reinvesting in export activities, you have permitted them to use the DISC savings to further develop export markets, which to me is a very desirable approach.

In considering the trading companies, though, I think we have to recognize that by and large America is made up of small- and medium-sized businesses. It is very difficult for them to compete in export activities. So I would say that the Treasury Department, with all due regard for their approach, has not really focused in on the true needs of the small businessman. The small businessman is the one that we have to help—if you want more exports, you have to find more things to export. When you philosophize a bit, you get down to the small- and medium-sized businesses having excellent export potential.

So I would say that that may be Treasury's approach, and if that is the way the Congress decides, I would encourage you then to look at the ownership rules and have one policy as opposed to two. At this point, though, I believe you should leave the DISC in place and try to encourage through these tax incentives exports for small- and medium-sized businesses.

Senator STEVENSON. We may have to reexamine the tax provisions in light of these complaints about GATT. There are some indications that it would be possible to accomplish the same objectives without running these larger risks. Maybe we could discuss this a bit further later. It's a very complex question.

Mr. KAPNICK. We would be most happy to provide any assistance we can in evaluating that question and looking at alternatives.

Senator STEVENSON. I am grateful for that. As you probably know, you can't offer assistance without running a considerable risk of me taking advantage of it. But——

TAX ISSUE SECONDARY

Mr. KAPNICK. I would make one comment, if I could, in that regard. I think the tax issue is a secondary issue. The overriding issue is to get trading companies on the books, so that we can increase the exports. As to how you get the tax incentive structured, we will work with you. I would hope you would see that as the secondary issue, rather than the prime issue.

Senator STEVENSON. The DISC provisions would be valuable to trading companies, would they not?

Mr. HOEFS. No. Your provisions are incompatible with the DISC provisions. The company would fit into one category or the other.

Senator STEVENSON. If the tax provisions are not essential, if we kept loans and guarantees, because of the startup problems and then took out the development provisions, because of whatever objections there are, would DISC go far enough to accomplish that purpose for the trading companies? That is a provision that does not conflict with GATT.

Mr. HOEFS. I suppose it depends on whether you would be restricted to the present DISC provisions or have some ability to expand on them in some way.

LIMITATIONS AND COMPLEXITY OF DISC

The greater incentives offered, the greater the possibility that meaningful use will be made. The key thing—really two things—wrong with DISC is from the small- and medium-sized business point of view. One is their limitations.

Basically DISC provides 50 percent or less of the tax benefits that your bill offers. Obviously 50 cents on the dollar is not as valuable as a $1.

Second is the complexity. I am not sure which is the worse. DISC gets so horribly complex.

As we point out in our written statement, we prepared a 30-page list for our people to use in determining whether a particular company has problems qualifying as a DISC or not.

Obviously, a small- or medium-sized company can't begin to deal with that complexity.

Senator STEVENSON. My staff gave me a note. They concur fully with what you said.

Mr. PENICK. The DISC's serve a real function for larger companies. We do need this kind of incentive. S. 1663 provides an extra incentive—clearly more incentive than DISC—but we need that for small- and medium-sized businesses.

Senator STEVENSON. I am groping at the moment for some way to minimize the GATT problems. Maybe we will have to do more work on that.

Mr. KAPNICK. We will look at that and get back to the staff.

Senator STEVENSON. Good.

Mr. KAPNICK. I wonder if the GATT issues aren't getting overplayed. I would like to see what is involved—we have not taken a look at that.

Mr. PENICK. No; beyond generally looking at it and discussing it. That is as far as we have gone.

Senator STEVENSON. That would be much appreciated. As you probably detected earlier, there is some interest in the Finance Committe which could share the jurisdiction in this matter and an opportunity to move ahead, if we can overcome the GATT obstacle.

I would sense that that may be the major obstacle at the moment. Well, I think we will probably have some additional questions. If so, I think I will follow up in writing with those.

Thank you again.

Our next witnesses will comprise a panel. Richard Baker of the Alliance for Progress in North Carolina. Michael Doyle of Alston, Miller & Gaines, Atlanta? Marshall Frankel, president of J. D. Marshall International and Guy Tozzoli, director of the World Trade Department, Port Authorities of New York and New Jersey.

STATEMENTS OF A PANEL CONSISTING OF RICHARD BAKER, ALLIANCE FOR PROGRESS, NORTH CAROLINA; MICHAEL DOYLE, ESQ., ALSTON, MILLER, & GAINES, ATLANTA, GA.; MARSHALL FRANKEL, CHAIRMAN OF THE BOARD, MARSHALL INTERNATIONAL, TRADING CO., INC., SKOKIE, ILL.; AND GUY F. TOZZOLI, DIRECTOR, WORLD TRADE DEPARTMENT, PORT AUTHORITIES OF NEW YORK AND NEW JERSEY

Senator STEVENSON. Mr. Baker.

If any of you would like to summarize your full statements, I would be more than happy to enter them. The full statements will appear in the record.

Mr. Baker.

Mr. BAKER. I will be glad to summarize in just a couple of moments. I am Richard Baker. I represent Alliance for Progress in northeastern North Carolina which is a development corporation and we are currently charged with responsibility of starting up an international training company that will assess foreign market potential for agricultural products and put together a large group of producers in North Carolina and the Southeast.

This would involve also arranging for the necessary processing of the products. We would probably end up using joint ventures in foreign capital, specially as it relates to the processing plants and other entities of this corporation.

We would like very much to applaud your efforts in getting the Federal Government to assit foreign trade in a very positive way.

Since we are in the middle of the startup of this venture, we have run into situations that perhaps would be very applicable to your Senate bill S. 1663.

Of course, this would include the component of your bill that we are very interested in. That is the startup.

The financing of the company. And that is the startup as well as the ongoing operation of the company which would include the possible bank guarantees for inventory of receivables and we are real happy to see these components in the bill.

We also are happy to see that possibly the bill might provide remedies for any antitrust problems.

NO ANTITRUST PROBLEMS

Senator STEVENSON. Hopefully it will provide for no antitrust problems, but will offer remedies.

Mr. BAKER. That's right. And it speaks to the startup and operating capital. I would like to suggest some ways that this good bill might be enhanced.

We encourage foreign ownership in a joint venture. We feel that would help in this case.

Senator STEVENSON. Others made the same point. I think it's well taken. We will take that suggestion under advisement.

Mr. BAKER. Another way would be the elimination of the 20-percent ownership clause. We would hope there would be consideration for partnerships and also for family owned activity.

We see a possible need for guarantees and commercial bank loans for the inventory and accounts receivable in the operations of the company a few years hence, especially since large amounts of capital will be necessary for contracting with farmers. Providing this cash for large inventories coming in would be a problem.

We see this consideration as a real help in the future. When I talk to businessmen and consultants working with me on the project, we find that licensing by the Department of Commerce seems to scare a lot of businessmen. Using a term other than licensing would probably help.

With that, we thank you so much for the opportunity to share this with you. Again, we applaud your effort.

Senator STEVENSON. I thank you, sir, for the help. If there is no objection, we will finish up with the panel and come back to all of you with questions.

Mr. DOYLE. I will attempt to focus my remarks. I would appreciate my comments being made part of the record.

Senator STEVENSON. All the full statements will be entered in the record.

Mr. DOYLE. I am Michael A. Doyle, a partner with the Atlanta law firm of Alston, Miller & Gaines. My practice has been specialized principally in the area of antitrust law.

I have been particularly involved and interested in the recent past in the representation of agricultural producers in the Southeast.

I have recently served as counsel to a group of about 15 poultry producers who have formed a Webb-Pomerene Export Association for the export of broilers and eggs. I applaud this subcommittee's efforts to encourage export associations.

ANTITRUST EXEMPTIONS NEEDED

If joint export activity is to expand, I am convinced that a more certain antitrust exemption must be provided.

I know from my own experience and my own practice that lack of a certain antitrust exemption has kept a number of smaller businesses out of joint export associations and thus out of the export market.

The Department of Justice position that no antitrust exemption is required gives no comfort. As you pointed out in the testimony of Mr. Ewing, the Department of Justice position does not bind private attorneys general—plaintiffs treble damage, class action counsel; it does not bind the Federal Trade Commission.

It does not bind a court. In sum, the difference between the Department of Justice position and the legislation that is currently being pursued by this committee is this: I can say to my clients that it is my opinion that if you are sued for treble damages, that after a number of years, after untold expense, I think I can win that lawsuit before a jury of six citizens.

The Department of Justice agrees with me. Enactment of legislation that you have before your subcommittee allows this statement to be made to all small businessmen, in advance:

"Declare your purpose. Obtain certification. And you will not be sued so long as you retain that certification." The comfort of that kind of legislation can do what no opinion of the Department of Justice and no opinion of private counsel can do.

It will make the difference between participation and no participation in my experience and my opinion. I am delighted to support the concept of the legislation before this committee and would be happy to answer any questions.

[The full statement follows:]

Remarks By

MICHAEL A. DOYLE, ESQ.

ALSTON, MILLER & GAINES

My name is Michael A. Doyle. I am a member of the Atlanta and Washington law firm of Alston, Miller & Gaines and have been a practicing attorney for 18 years. My principal area of expertise is antitrust. Within that area, I have advised numerous clients, including a number of trade associations and agricultural cooperatives, concerning their compliance with the antitrust laws. I have also been called upon to represent certain of these clients when their activities have been challenged under the antitrust laws.

Not infrequently, the antitrust challenges faced by my clients have stemmed from attempts by vigorous antitrust enforcers to expand the scope of the antitrust laws. While I applaud vigorous antitrust enforcement, the expanding nature of this enforcement makes it difficult to advise clients as to whether their conduct is lawful. More importantly, the breadth of the antitrust laws, particularly Section 1 of the Sherman Act, makes it very hard for a businessman to assess the risks of a particular course of conduct and plan his affairs accordingly. This uncertainty is, of course, a direct impediment to many forms of business activity -- activity which nonetheless may be desirable from a standpoint of economic efficiency and growth, as well as procompetitive. In any area of economic activity, such uncertainty is expensive.

The Webb-Pomerene Act is a model of the vague, general statutes one typically finds in the antitrust field. While providing a general exemption from the antitrust laws for certain activities conducted by qualified export associations, the Webb-Pomerene Act is far from clear in its scope and offers the businessman little day-to-day certainty in its application. Business Letter Review procedures, which are available through the Antitrust Division of the Justice Department, provide no firm assurances that a future challenge will not be forthcoming.

Let me give you a flavor of the "comfort" provided in a Business Review Letter by quoting a paragraph from a recent Business Review Letter issued to a Webb-Pomerene association:

> In light of the foregoing, the proposed organization would seem to qualify as a Webb-Pomerene association pursuant to 15 U.S.C. §§61-65, the formation of which is exempt from the antitrust laws so long as certain statutory conditions are met. Since these conditions appear to have been satisfied in this instance, the Department of Justice has no present intention to institute antitrust proceedings with respect to the formation of (the export association). However, as with all Webb-Pomerene associations, the statutory exemption is contingent upon conformity of the Association's behavior with the provisions of the statute, applicable regulations of the Federal Trade Commission, and judicial interpretation of both. (Emphasis supplied.)

By my count, there are six qualifiers in the quoted paragraph alone. I do not believe that cautious businessmen are likely to embrace enthusiastically cooperative export activity in

light of an antitrust exemption as tenuous as this. I believe that the lack of Webb-Pomerene export activity in the past is partly accounted for by this uncertainty.[1] No conservatively advised businessman can discount the grave antitrust risk which is very real under current law. That risk is this -- a step ventured into the area of Webb-Pomerene uncertainty today may result in exposure to ruinous antitrust treble damages exposure that is visible only through 20-20 hindsight. It is no wonder that prudent businessmen forego this opportunity to add fractionally to their sales, through a venture that might, innocently and without forewarning, risk their entire business. Published statements to the effect that the Justice Department is "itching to sue" a Webb-Pomerene association further diminish the value of the present exemption.[2]

I believe that S.864, which amends the Webb-Pomerene Act, S.1499, which replaces the Webb-Pomerene Act, and S.1663, which provides for a new concept -- the Export Trading Company -- while preserving Webb-Pomerene, each adds a substantial degree of certainty to the application of the antitrust laws in this area. Accordingly, I urge this Subcommittee to adopt some form of clarification or supplementation of the existing Webb-Pomerene Act. I do not, however, think that any of these three bills goes far enough in providing the business community with the degree of certainty to which it is entitled. I do not

think that any of these three bills goes far enough in providing the assurances necessary to spur an increase in the number of export organizations sufficient to reduce the balance of payments difficulties this country is presently experiencing.

The primary benefit provided in each bill being considered is the institution of administrative "certification" or "licensing" procedures, which provide export organizations with an exemption from the present uncertainty of after the fact, ad hoc application of the antitrust laws.[3/] As I understand these procedures, each entity which hopes to operate under the revised Webb-Pomerene or Export Trading Company umbrella must submit certain information to a monitoring federal agency, either the Commerce Department (S.864 and S.1663) or the Federal Trade Commission (S.1499), and then await administrative action which will either sanction or not sanction the entity as being exempt. The criteria for exemption and the particulars of the information which must be supplied to the relevant agency vary from bill to bill, but in essence they appear to be much the same and, in my view, are generally fair in their scope.

The great benefit of each of these bills is that once an association or trading company has been "cleared" or "licensed" it is exempt from the antitrust laws until one of two exceptions to the general exemption comes into play. These

exceptions are (i) material changes in "domestic and international circumstances" and (ii) material changes in the association's or company's membership, trading activity or mode of operations.[4/] In my mind, this statutory framework provides the businessman with substantially greater assurances that he will not face antitrust exposure prior to a determination that his activity has been unlawful. As I said before, however, I believe that the American businessman is entitled to further assurances that his conduct is lawful. This is particularly so where there is every incentive to encourage the businessman to adopt a particular course of conduct for the general welfare of the country.

The two exceptions to the general antitrust exemption afforded in each bill are rather amorphous. Such an approach is often required in drafting statutes that must deal with a myriad of contingencies that its drafters can never contemplate. Accordingly, I do not fault the lack of specificity found in the "exceptions" provisions of these bills. I do, however, believe that the pending legislation is at fault for not specifying with sufficient clarity the consequences of application of these exceptions to the general exemption.

Let me offer the following hypothetical based upon S.864 as an illustration. Suppose that association XYZ applies for and receives clearance to operate as a Webb-Pomerene

association under the amended Act and commences to export a particular commodity pursuant to that clearance. Some time thereafter the Department of Commerce determines that the association's exempt status should be terminated, either because domestic and international conditions have changed or because the association has begun to conduct itself in a manner that the Department believes is not in accordance with the applicable statute. Hearings and perhaps appeals follow, but the association's exemption is ultimately terminated. What then? Clearly, if the association continues to operate after a final administrative or judicial determination that it is without the protection of Webb-Pomerene, the association should be subject to the antitrust laws. But what if the association ceases its activities or comes into compliance with Webb-Pomerene? Is the association subject to the antitrust laws for activities conducted during the period it thought it was exempt, but as matters ultimately were resolved, it was not? Each of the three bills before this Subcommittee is less than totally clear on this point.

To me, the answer should be that the association is exempt for all activities which took place prior to the final administrative or judicial determination that the association was not exempt. This is for two reasons. First, S.864 and S.1499 provide for an annual administrative review of the

exemption for each association.[5] This reporting requirement could be easily added to S.1663. Through this device it should be feasible to monitor the activities of each exempt export organization on a reasonably current basis. Under these circumstances, it seems only proper that if the organization is not informed that conditions have changed or that it has fallen from administrative grace, it should be permitted to presume that it is still exempt and its activities lawful. Second, I seriously doubt that businessmen will utilize an exemption that is tenuous enough to be abrogated by an ex post facto determination. In short, if we are to encourage exports through the technique of Webb-Pomerene associations or Export Trading Companies, we should supply businessmen with the greatest degree of security possible, consistent with maintaining a competitive domestic economy. Prohibiting prosecution for activities conducted subsequent to clearance and prior to rescission of that clearance provides this security and does little to impede legitimate enforcement of the antitrust laws.

Because each of the bills proposed does not treat this situation with sufficient clarity, I propose that the following language be added to whatever bill is ultimately reported out of this Subcommittee in a favorable manner:

> Provided, however, that no organization which has obtained clearance under Section ___ of this Act shall be subject to any criminal or civil liability under

> the antitrust laws for activities conducted subsequent to certification under Section ___ of this Act and prior to a final administrative or judicial termination of certification under Section ___ of this Act.

Without an amendment such as this, a vigorous antitrust enforcer or a private treble damages plaintiff can institute a Section 1 suit against the erstwhile exempt association for all activities conducted during the period the association believed it was exempt. Although it seems that certain language in these bills, particularly in S.1663,[6/] mitigates against this, I do not believe that any of the proposed bills necessarily precludes this possibility; and at a minimum, I would expect this to be a litigated point. In the wc ld of antitrust treble damage suits, a litigating point too of en results in virtual extortion. Brought as class actions on behalf of the universe of all domestic customers by attorneys whose sole incentive is their contingent fee, the extortionate threat that follows uncertainty in this never-never land is as sure as night follows day. This uncertainty alone can vitiate this entire, commendable legislative effort.

In addition, the law at present is that once a regulated entity is found to have violated the applicable regulatory framework, any conduct not condoned by the regulator is subject to the antitrust laws in the absence of a specific statute to the contrary.[7/] Because of this, without an

amendment similar to the one I have suggested, the benefits of the "clearance" mechanism will be vitiated in large measure.

I do have one caveat to the amendment I have suggested: In the event the export organization (i) is not exempt due to either of the two exceptions and (ii) knowingly failed to report or knowingly reported materially misleading information, the exempt organization should be subject to the antitrust laws for the period of time in which it was willfully out of compliance with the applicable reporting requirements. Obviously, any determination that the reporting requirements were not fulfilled should be in the hands of the relevant regulatory agency, and I would preclude application of the antitrust laws until after such a determination has been made.

None of this is to say that I believe the proposed bills completely fail to address the issue of certainty. The certification/licensing procedure is, as I have said, a very positive provision by itself. Moreover, Senator Roth's proposal that recovery in a civil suit be limited to actual damages removes two-thirds of the risk perceived by any businessman.[8/] If my suggested revision is not accepted, I strongly urge adoption of this proposal by Senator Roth.

There are a number of other points contained in S.864, S.1499 and S.1663 that also merit discussion. In the important area of enforcement, I believe that S.864 and S.1663 are

correct in transferring administrative jurisdiction over Webb-Pomerene associations and Export Trading Companies to the Department of Commerce. The clear focus of the pending legislation is to promote exports, and it strikes me that this purpose will be better served by Department of Commerce oversight than by Federal Trade Commission oversight. As an institutional enforcer of the antitrust laws, the FTC has an inherent interest in construing exemptions to the antitrust laws as narrowly as possible. While this position has merit in its general application, I believe that such an institutional bias is inappropriate in the export field where practices which might arguably be viewed as restraints of trade can also, and should, be viewed as part of a reasonable competitive effort to expand markets for our goods and services.

With regard to judicial enforcement, it strikes me that the solutions reached by each bill are in general appropriate. All three bills preclude a private right of action, at least until after the relevant administrative agency has determined that the association is not exempt.[9/] Private complainants are protected through their right to petition the Department of Commerce or the FTC and bring their grievances to the attention of those agencies.[10/] I believe that this is adequate to protect private interests. I repeat my strong belief that any new legislation should make clear that no

exempt export organization is subject to the antitrust laws because of any activities conducted prior to a final determination that the exemption does not apply or that reporting requirements have not been followed. Thereafter, the export organization would be on notice that its conduct is subject to the antitrust laws.

S.1663's favorable tax treatment of Export Trading Companies appears to be consistent with our national goal of improving our foreign trade deficit.[11/] Since our balance of payments difficulties are a national problem, it seems appropriate that those who participate in alleviating this problem receive some type of inducement. A favored tax status, which is born indirectly by all Americans, is justified under these circumstances. The same, of course, is also true of S.1663's authorization of the Small Business Administration, the Economic Development Administration and the Export-Import Bank to extend loans to Export Trading Companies.[12/] These financial incentives will go a small way toward overcoming the advantages many of our foreign competitors receive from their governments. The more attractive, and less risky, these associations are, the more they will be used as an export vehicle. Should this Subcommittee recommend amendment or replacement of Webb-Pomerene, I suggest that these provisions of S.1663 be incorporated into that legislation as well.

S.864's confidentiality provisions are meritorious for much the same reason.[13/] Disclosure of sensitive business information to one's competitors -- either directly or indirectly by operation of a Freedom of Information Act request or a subpoena addressed to a government agency that has access to that information -- is perceived by businessmen as a very real threat to their competitive well being. Because of the extensive reporting requirements of the pending bills, a confidentiality arrangement of the type contained in S.864 is essential, since it reduces the perceived risk that information produced to the government will ultimately find its way into the hands of competitors.

Each of the bills under consideration wisely expands the scope of the antitrust exemption to exports of "services" as well as goods.[14/] This corrects a distinct shortcoming in the existing Act. I am troubled, however, by the fact that S.864 and S.1499 restrict the exporting of "technology" by Webb-Pomerene associations.[15/] American technology, particularly in fields such as agriculture, is a valuable resource readily saleable on the world market, and it seems inappropriate not to permit its export when we are experiencing severe international trade imbalances. Moreover, there are very real "line drawing problems" between "goods and services" and "technology," particularly where specific technological

know-how is inherently "incidental" to the goods and services being sold.[16]

My criticism of the existing Webb-Pomerene Act is not all encompassing. The very breadth of the existing Act has permitted the judicial and administrative creation of several very beneficial principles which the proposed bills, especially S.864 and S.1499, call into question. First is the issue of whether a Webb-Pomerene association or Export Trading Company may refuse to handle the products of nonmembers. Under the present Act, a Webb-Pomerene association can refuse to handle any products other than those of its members.[17] Each of the three proposed bills, although tracking language in the existing Act,[18] potentially abrogates this rule by providing that the exemption is lost if there is "a substantial restraint of the export trade of any domestic competitor."[19] I believe that the language of the bill as proposed by this Subcommittee should be amended to make clear that a Webb-Pomerene association or an Export Trading Company is free to refuse to handle the products of domestic competitors and that such a refusal shall not be deemed to be a restraint on the export trade of those domestic competitors. Otherwise, there would be little impetus to form an exempt organization, since non-members could coerce the organization into exporting their goods and services.

Second, the Webb-Pomerene Act has also been interpreted as permitting a qualified association to require its members to use the association as their exclusive foreign outlet.[20] While this interpretation of the existing Webb-Pomerene Act does not seem to be called directly into question by any provision in the proposed bills, I believe that there should be express language preserving this interpretation of the existing Act in any new statute, since without it there is little internal incentive for the export organization's members to support it. Attending this ability of present Webb-Pomerene associations to restrict the export activities of their members are the powers of the association to fix export prices, assign quotas to its members, reasonably restrict withdrawal from the association, and restrict the activities of its foreign distributors.[21] These powers should not be abolished by the Act's amendment and should be included in S.1663.

The existing Act has been criticised because it permits competitors to come into closer contact with each other and to discuss matters which, if in the domestic context, could clearly lead to violations of the antitrust laws. It is feared by some that discussion of these activities in the area of exports may have anticompetitive domestic "spillover" effects.[22] There are two answers to this criticism. First,

I am unaware of any evidence indicating that such spillover effects have in fact occurred. Second, to the extent that cooperative export activity may lead to anticompetitive domestic consequences, the antitrust laws are available to deal with those situations when they actually occur. The appropriate target of the investigation would, of course, be the non-exempt domestic entity rather than the exempt export organization.

As I stated at the outset, I have had extensive experience counselling trade associations and agricultural cooperatives. The membership of these trade associations and agricultural cooperatives is generally comprised of small to middle sized businesses. On several occasions, members of these associations and cooperatives and at times the associations and cooperatives themselves have considered forming Webb-Pomerene export associations. The uncertainty surrounding application of the antitrust laws to Webb-Pomerene associations has impeded their formation.

Based on these experiences, it is clear to me that the bills pending before this Subcommittee are the type of legislation needed to induce the formation of export organizations, particularly organizations of producers of agricultural commodities. Agriculture is, of course, one of the relatively few remaining areas in which this country maintains a clear advan-

tage over its competitors in the world marketplace. This advantage is often compromised, however, by restrictive import policies and the existence of powerful cartels under the direct auspices of foreign governments. In order to realize our competitive advantage, economic theory holds that either these barriers to trade must be removed or, as a second best solution, countervailing arrangements must be constructed. Since the former solution is unworkable, at least in the foreseeable future, focus on the latter is imperative. Webb-Pomerene organizations and Export Trading Companies of the types contemplated by these bills are one answer. Moreover, these associations should benefit the people who need to be able to engage in this type of activity the most -- the small to middle sized producers of undifferentiated products who cannot on their own undertake export activities because of economies of scale and the necessity for particular types of business expertise and contacts that they are not likely to have.

In short, I wholeheartedly support enactment of legislation of the type pending before this Subcommittee. Each of the three bills alleviate many of the antitrust risks inherent in any cooperative activity with minimal impact on domestic competition. As I have said, however, even greater risk reduction can be added without hampering domestic antitrust enforcement. This additional certainty is needed if cooperative export activity is to reach its full potential.

Endnotes

1/ See Report to the President and the Attorney General of the National Commission for the Review of Antitrust Laws and Procedures, ATRR No. 897 at 87 (January 18, 1979), hereinafter "NACRALP Report."

2/ See statements attributed to Douglas Rosenthal, Chief of the Department of Justice, Antitrust Division's Foreign Commerce Section in ATRR No. 892 at 16 (December 7, 1978).

3/ S.864 at Sec. 5 (all citations to S.864 are to be existing Act, as amended by S.864), S.1499 at Sec. 6 and S.1663 at Sec. 102.

4/ S.864 at Sec. 5(c), S.1499 at Sec. 6(c) and S.1663 at Sec. 102(f).

5/ S.864 at Sec. 7 and S.1499 at Sec. 10.

6/ S.1663 at Sec. 103(d).

7/ Mt. Hood Stages, Inc. v. Greyhound Corp., 555 F.2d 687, 688-695 (9th Cir. 1977), vacated on other grds 437 U.S. 322.

8/ S.1499 at Sec. 5(d)(2).

9/ S.864 at Sec. 2(b), S.1499 at Sec. 5 and S.1663 at Sec. 103.

10/ S.864 at Sec. 2(b)(2), S.1499 at Sec. 5(b) and S.1663 at Sec. 103(b).

11/ S.1663 at Title II.

12/ S.1663 at Sec. 105(a) and (b).

13/ S.864 at Sec. 10.

14/ S.864 at Sec. 1(1), S.1499 at Sec. 3(1) and S.1663 at Sec. 101(1).

15/ S.864 at Sec. 2(a)(6) and S.1499 at Sec. 3(1)(B).

16/ S.1499 at Sec. 3(1)(B).

17/ United States v. Minnesota Mining at Manufacturing Co., 92 F.Supp. 947, 965 (D. Mass. 1950).

18/ 15 U.S.C. §62.

19/ S.894 at Sec. 2(a)(2), S.1499 at Sec. 4(3) and S.1663 at Sec. 106(a)(1).

20/ Minnesota Mining, 92 F.Supp. at 965.

21/ Id.

22/ NACRALP Report at 87.

Senator STEVENSON. Thank you.

Mr. Frankel?

Mr. FRANKEL. Thank you, Mr. Chairman, for the opportunity to express my views and those of my company before this subcommittee.

As chairman of the board of Marshall International Trading Co., the holding company for two operating subsidiaries, J. D. Marshall International, Inc., and Marshall Electronics, Inc., I have devoted my business career to bringing American manufacturers into world markets. Therefore, I view the three bills under discussion today, each of which is intended to foster growth of export trade associations, with particular interest.

J. D. Marshall International, Inc., is one of the largest, if not the largest, export management company in the United States and we have been characterized as a smaller scale American version of one of the world's giant trading companies such as the Japanese Mitsubishi Corp. or Mitsui Bussan.

The fact is that there are no American trading companies, including our own, that can begin to compare in size and world impact with the giants I have just mentioned. It may, however, be helpful to this committee to understand how an American export management company—EMC—operates under existing market and legal restraints.

Twenty-seven years ago, along with my partner Joel D. Honigberg, I founded J. D. Marshall International with the idea that we could find markets around the world for many American manufactured products that were not at that time being exported. Today, Mr. Honigberg and I, as president and chairman, respectively, have seen the company grow to encompass over 200 employees at our Skokie, Ill., world headquarters and in our 19 sales offices around the world.

We offer a complete export program to the manufacturers and effectively become their export division. We are a sales-oriented organization, however; our services include marketing, promotion and market analysis, as well as the ability with our in-house traffic and documentation department to handle inland and overseas freight as well as all foreign documentation requirements.

Most importantly, we are able to relieve the manufacturer of all financial risk by paying him for the goods as they leave his plant. J. D. Marshall International is an example of how an American EMC operates.

Now let us look at the proposed legislation for export trade associations and see how they would improve the climate to encourage the growth for more American exports.

S. 864 and S. 1499 are similar in that they seek to encourage growth of export trade associations by modifying Webb-Pomerene and assuring potential exporters that they will not be prosecuted under antitrust laws. However, beyond providing for establishment of an office in the Department of Commerce, they do little to provide real impetus for the formation of such associations.

S. 1663 offers more constructive specific ideas and incentives, although I see several areas where the bill unnecessarily restricts the intended growth.

ASSOCIATIONS ELIGIBLE FOR LOANS

I like the provision contained in the bill for making the associations eligible for loans from the Export-Import Bank, although I wonder if this will require a change in the Bank's charter. I also believe that the provision for distribution of profits as ordinary income rather than dividends is a genuine incentive for exports.

One of the problem areas I see in the bill is the restriction against foreign ownership and capital. This restriction would remove any incentive for a foreign trading company to distribute American products through their existing systems. Since the goal is to increase the export of American products it seems unwise, in my judgment, to ignore the ability of the great trading companies of the world to lend their distribution systems and expertise to selling American products.

Senator STEVENSON. I am sorry to interrupt. I will have to vote. We will have to recess for a few minutes and then resume.

[Recess.]

AFTER RECESS

Mr. RUSSELL. As sometimes happens, Senator Stevenson is detained on the Senate floor. He asked me to reconvene the hearing and ask you to go through the remainder of your statements and to begin the questioning. He will try to get back as quickly as he can.

I believe, Mr. Frankel, you were in midsentence when the hearing recessed. Please finish your statement, then we will go on with the other statement.

Mr. FRANKEL. I might repeat the last sentence or two. One of the problems I see in the bill is the restriction against foreign ownership and capital. This restriction would remove any incentive for a foreign trading company to distribute American products through their existing systems.

Since the goal is to increase the export of American products, it seems unwise in my judgment, to ignore the ability of great trading companies of the world to lend their distribution systems and expertise to selling American products.

In yesterday's testimony, Hon. C. Fred Bergsten, further points out that this denial of domestic tax benefits to foreign persons would violate the nondiscrimination provision in our double taxation conventions with other countries.

The positive impact on our trade deficit is not altered by having a foreign controlled company exporting American products.

Another problem I have with this bill is with the limitation of ownership by any one person to a maximum of 20 percent. This would seem to me a real deterrent to the formation of such a company. It would dictate a working partnership of at least five persons and I can assure you from my own experience, that there are enough problems associated with a partnership of two. Five or more partners would exaggerate those problems dramatically.

I understand that manufacturers can own export trade associations. The existing apparatus and expertise of some of the export divisions of our major American manufacturers would be extremely adaptable to the export trade association concept. The association could use the existing distributor network of the manufactur-

er to offer in addition capital products of other American manufacturers in related industries.

The point of my criticisms and comments is only to say that in forming legislation to foster creation of export trading associations, we should not lose sight of the bottom line goal of increasing the access of American products to world markets. I am concerned, as noted, that the legislation as presently formed is unnecessarily restrictive in some areas.

As I mentioned in the beginning of this testimony, I have been involved for nearly 30 years in the export business and, more often than not, that has meant giving American manufacturers their first taste of world markets. It is my experience that the major attraction to interest an American manufacturer to export their products is for them to increase their profits. The most useful legislation, since we have been in business, has been the legislation which established the Domestic and International Sales Corporation—DISC—in 1971.

I am a member of the Task Force on International Trade of the White House Conference on Small Business. We are studying and helping to form various proposals for legislation favorable to increased exports by small- to medium-sized American manufacturers. These proposals and ideas will be considered ultimately in January 1980 when the conference takes place in Washington, D.C. One of the options presently being considered calls for the development of American export trading companies, which should eventually lend support to the bills being considered today.

DISC RULES MUST BE ALTERED

I firmly believe that for the proposed export trading associations to be successful, the DISC rules must be altered so the export trade associations can be DISC's in their own right.

Additionally, the formation of export trade associations and their incorporation as a DISC would expand U.S. exports substantially by some key changes in current DISC laws. These changes would include special increased deductions to be given to DISC corporations on premiums paid to either the Export-Import Bank or the Foreign Credit Insurance Association—FCIA—on export insurance premiums.

For example, if a premium of 1½ percent is paid to these governmental or quasi-governmental entities in order to promote exports, twice that amount should be allowed as a deduction prior to the payment of any DISC taxes. This would aid in both the promotion of Eximbank and FCIA amongst DISC corporations as well as be a monetary incentive for the DISC itself.

DEEMED DISTRIBUTION

Additionally, the 50-percent "deemed distribution" which is taxed to the parent corporation of the DISC should be changed. There should be a graduated tax for "deemed distribution" dependent upon the gross volume of the DISC. On a gross volume of $500,000 or less, there should be no "deemed distribution."

At the present time, DISC's are allowed an exemption of $100,000. Therefore, we suggest that this exemption be increased to

$500,000. Between $500,000 gross volume and $50 million gross volume, there should be a graduated scale of "deemed distribution;" with a gross volume of $50 million or more, there should be a 50-percent "deemed distribution," as outlined in the DISC legislation of 1971.

Furthermore, all new DISC's should be exempt for a period of 3 years from all "deemed distribution."

I believe that the incremental provision of DISC, which passed along with the Tax Reform Act of 1976, should be repealed. This eliminated 40 percent of the DISC benefits in 1977 and by the year 1980 there will be more and more elimination of benefits due to this incremental provision.

It is my strongly held belief that we should be increasing, not decreasing, benefits and incentives for promotion of American exports. This is the only way that we will increase our share of international trade and decrease our negative trade balance. I would draw your attention to Report 78-251E of the Congressional Research Service of the Library of Congress, "Incentives and Disincentives for U.S. Exporters" by George D. Holliday. This report clearly indicates the excess of disincentives and the dearth of incentives.

It has been a pleasure and a privilege to address my comments before this subcommittee. I applaud the entire committee and particularly the leadership of Senator Stevenson as chairman, for their outstanding work of recent years and their understanding and support of the American exporter, large and small.

Thank you.

Mr. RUSSELL. Mr. Frankel, it might be useful if we put that CRS study in the record at this point, don't you think so?

Mr. FRANKEL. Yes.

Mr. RUSSELL. Fine. It will be inserted in the record.

[Complete statement of Mr. Frankel and the paper referred to above follow:]

STATEMENT BY MARSHALL FRANKEL, CHAIRMAN OF THE BOARD OF MARSHALL INTERNATIONAL TRADING COMPANY, SKOKIE, ILL.

Thank you, Mr. Chairman, for the opportunity to express my views and those of my company before this Subcommittee. As Chairman of the Board of Marshall International Trading Company, the holding company for two operating subsidiaries, J. D. Marshall International, Inc. and Marshall Electronics, Inc., I have devoted my business career to bringing American manufacturers into world markets. Therefore, I view the three bills under discussion today, each of which is intended to foster growth of export trade associations, with particular interest.

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division. We are a sales oriented organization, however, our services include marketing, promotion and market analysis as well as the ability with our in-house traffic and documentation department to handle inland and overseas freight as well as all foreign documentation requirements. Most importantly, we are able to relieve the manufacturer of all financial risk by paying him for the goods as they leave his plant. J. D. Marshall Internatioal, is an example of how an American EMC operates. Now let us look at the proposed legislation for export trade associations and see how they would improve the climate to encourage the growth for more American exports.

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S. 1663 offers more constructive specific ideas and incentives, although I see several areas where the bill unnecessarily restricts the intended growth.

I like the provision contained in the bill for making the associations eligible for loans from the Export-Import Bank although I wonder if this will require a change in the Bank's Charter. I also believe that the provision for distribution of profits as ordinary income rather than dividends is a genuine incentive for exports.

One of the problem areas I see in the Bill is the restriction against foreign ownership and capital. This restriction would remove any incentive for a foreign trading company to distribute American products through their existing systems. Since the goal is to increase the export of American products it seems unwise, in my judgment, to ignore the ability of the great trading companies of the world to lend their distribution systems and expertise to selling American products. Insert (1) The positive impact on our trade deficit is not altered by having a foreign controlled company exporting American products.

Another problem I have with this Bill is with the limitation of ownership by any one person to a maximum of 20 percent. This would seem to me a real deterrent to the formation of such a company. It would dictate a working partnership of at least five persons and I can assure you from my own experience that there are enough problems associated with a partnership of two. Five or more partners would exaggerate those problems dramatically.

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The point of my criticisms and comments is only to say that in forming legislation to foster creation of export trading associations we should not lose sight of the bottom line goal of increasing the access of American products to world markets. I am concerned, as noted, that the legislation as presently formed is unnecessarily restrictive in important areas.

As I mentioned in the beginning of this testimony I have been involved for nearly thirty years in the export business and, more often than not, that has meant giving American manufacturers their first taste of world markets. It is my experience that the major attraction to interest an American manufacturer to export their products is for them to increase their profits. The most useful legislation, since we have been in business, has been the legislation which established the Domestic and International Sales Corporation (DISC) in 1971.

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I firmly believe that for the proposed export trading associations to be successful the DISC rules must be altered so that the export trade associations can be DISCs in their own right. Additionally, the formation of export trade associations and their incorporation as a DISC would expand U.S. exports substantially by some key changes in the current DISC laws.

These changes would include special increased deductions to be given to DISC corporations on premiums paid to either the Export-Import Bank or the Foreign

Credit Insurance Association (FCIA) on export insurance premiums. For example, if a premium of 1½ percent is paid to these quasi-government or governmental entities in order to promote exports, twice that amount should be allowed as a deduction prior to the payment of any DISC taxes. This would aid in both the promotion of EX-IM and FCIA amongst DISC corporations as well as be a monetary incentive for the DISC itself.

Additionally, the 50 percent "deemed distribution" which is taxed to the parent corporation of the DISC should be changed. There should be a graduated tax for "deemed distribution" dependent upon the gross volume of the DISC. On a gross volume of $500,000 or less, there should be no "deemed distribution". At the present time, DISC's are allowed an exemption of $100,000. Therefore, we suggest that this exemption be increased to $500,000. Between $500,000 gross volume and $50,000,000 gross volume, there should be a graduated scale of "deemed distribution". With a gross volume of $50,000,000 or more, there should be a 50 percent "deemed distribution", as outlined in the DISC legislation of 1971.

Furthermore, all new DISCs should be exempt for a period of three years from all "deemed distribution".

I believe that the incremental provision of DISC, which passed along with the Tax Reform Act of 1976, should be repealed. This eliminated 40 precent of the DISC benefits in 1977 and by the year 1980 there will be more and more elimination of benefits due to this incremental provision.

It is my strongly held belief that we should be increasing, not decreasing, benefits and incentives for promotion of American exports. This is the only way that we will increase our share of international trade and decrease our negative trade balance. I would draw your attention to Report 78-251 E of the Congressional Research Service of the Library of Congress, "Incentives and disincentives for U.S. Exporters" by George D. Holliday. This report clearly indicates the excess of disincentives and the dearth of incentives.

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Report No. 78-251 E

INCENTIVES AND DISINCENTIVES FOR U.S. EXPORTERS

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CRS
CONGRESSIONAL RESEARCH SERVICE
LIBRARY OF CONGRESS

December 18, 1978

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SUMMARY

This report provides a survey of incentives and disincentives for U.S. exporters. U.S. Government programs wich have the effect of promoting or restricting exports are the focus of the report. Special attention is given to the Carter Administration's program, announced in September 1978, to improve U.S. Government export promotion activites.

INCENTIVES AND DISINCENTIVES FOR U.S. EXPORTERS

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INCENTIVES AND DISINCENTIVES FOR U.S. EXPORTERS

I. Introduction

In 1977, the U.S. trade balance was in deficit by $26.6 billion, compared with a deficit of $5.9 billion in 1976. The deficit is expected to be slightly higher this year before declining in 1979. The large deficits are a result of rapidly increasing imports accompanied by a poor export performance. The value of U.S. imports increased by 22 percent in 1977 (volume increased by 13 percent), while exports increased by only 5 percent (1 percent in volume).

All major categories of U.S. exports have experienced relatively slow growth. Agricultural exports, which grew rapidly in the early 1970s and now account for over 20 percent of the U.S. total, increased by only 5 percent in value in 1977. This slowdown was primarily due to improved harvests abroad and a general decline in prices paid for U.S. grains.

Non-agricultural exports rose by 5 percent in 1977, mostly because of higher prices. (Volume actually declined by 1 percent.) Typical of the trend in non-agricultural exports is the export performance of capital goods (such as machinery, aircraft and other transport equipment), which account for about one-third of all U.S. exports. In 1976 and 1977, capital goods exports experienced no real growth. A drop in the foreign sales of civilian aircraft was a primary cause for this poor performance. Other major categories of U.S. exports - industrial

supplies, consumer goods and automotive products - increased slowly in 1977.

The increase in the overall U.S. trade deficit reflected a deterioration in the bilateral trade balance with all major world areas. While 1977 exports to OPEC countries grew substantially, they did not keep pace with imports from those countries. In trade with the largest U.S. trade partners - Canada, Japan and Western Europe - imports also grew faster than exports. Most observers attribute the poor performance of U.S. exports primarily to the slow economic growth and depressed demand in the economies of major U.S. trade partners. During 1977, U.S. industrial production expanded more than twice as rapidly as the average increase in other major Western industrial countries. As the differential between growth in the United States and the rest of the world narrows, the U.S. trade balance is expected to improve.

Despite the expected improvement in the U.S. export performance, there is concern about the ability of U.S. businesses to expand exports rapidly enough to pay for the country's long-term import needs. Considerable attention has been focused on the various incentives and disincentives for U.S. exporters. Some observers maintain that the general domestic and international economic environment in which U.S. business operates is not conducive to an expansion of exports. Moreover, critics of U.S. Government policy in this area frequently

maintain that U.S. export promotion programs are ineffective and that many laws and regulations have the effect of disincentives to export. These views are not shared by some economists, businessmen and policymakers. The latter emphasize the temporary nature of poor U.S. export performance. They frequently maintain that the flexible exchange rate regime under which the United States and its major trade partners operate will provide an automatic adjustment to the country's balance of trade problems.

The following is an overview of the various incentives and disincentives for U.S. exporters. Conditions in the general economic environment and those policies of foreign governments which affect the ability of U.S. businesses to export are discussed in Section II. The focus of this paper is on U.S. Government laws, administrative regulations and policies which have a significant effect on U.S. exports. Sections III and IV provide descriptions of these elements of U.S. export policy and an analysis of their effects on U.S. exports. Section V provides a discussion of the Carter Administration's program, announced in September 1978, to improve the Government's export promotion efforts and to remove some of the Government-imposed barriers to exporters.

II. General Economic Environment for U.S. Exporters

In 1976, the United States exported approximately 6.6 percent of its gross national product. This compares with over 20 percent for West Germany, the United Kingdom and Canada and about 45 percent for the Netherlands. The primary reasons for the relatively small U.S. export/GNP ratio are evident. The United States is a large country, well-endowed with natural resources and a large, prosperous population which provides the largest single market for goods and services in the world. It also occupies a somewhat insular position with respect to the world economy. It is geographically remote from the major potential markets in Europe and Asia, and transportation costs for its exports are relatively high. Thus, geography alone has traditionally served as a major disincentive for U.S. exporters.

Traditionally, U.S. producers have profited by concentrating on meeting the needs of domestic consumers. For most businesses, success has been assured by designing products which satisfy the tastes of U.S. consumers and orienting corporate strategies to meet the special requirements of the domestic market. There has been little inducement to study the needs of foreign consumers or techniques for penetrating foreign markets. The risks, uncertainties and costs of selling in foreign markets have far outweighed the benefits of exporting. Many U.S. businessman has no training, experience or inclination to export.

Small- and medium-sized U.S. firms have special problems in exporting. Travel expenses, foreign market surveys, changes in product designs and packaging, provision of after-sales servicing and other start-up costs can be substantial. To penetrate a foreign market, a firm may have to forego profits in the short run. Many small firms are unable to absorb the start-up costs of exporting. This is one of the major reasons why only a small percentage of U.S. firms export: the Commerce Department has estimated that about half of U.S. exports of manufactured goods are made by only 100 companies and that 80 percent are made by only 250 companies. Large corporations dominate U.S. export trade.

Foreign government restrictions on trade - tariffs and non-tariff measures - are major barriers to expansion of U.S. exports. All countries, including the United States, have such restrictions. Another set of foreign government policies which affect U.S. exports is the formation of regional economic groupings or common markets. Of particular concern to the United States is the formation and expansion of the European Common Market. By lowering internal tariff barriers while retaining external tariffs, the Common Market has tended to displace U.S. exports. (Western Europe has been and continues to be a major market for U.S. exports.) In the interest of political and economic stability in Europe, the U.S. Government has consistently supported the concept of a common market in Europe, even though this development has probably contributed significantly to a loss of U.S. export markets.

Despite the geographical disincentives and the historical anti-export bias of U.S. producers, the United States has some notable competitive advantages on world markets. In particular, in two broad categories of goods - agricultural products and technology-intensive goods - U.S. exporters have gained dominant positions. In both categories U.S. exporters have made large positive contributions to the country's balance of trade. The success of U.S. exporters in these sectors is due to a number of factors, including the innovativeness of U.S. industry, the high level of productivity of U.S. workers (in both manufacturing industries and agriculture) and fertile farmland.

The volume of U.S. agricultural exports is highly variable, depending on crop conditions in other parts of the world. Although the growth rate has slowed in recent years, most forecasts suggest continued strong foreign demand for U.S. farm products in the future. However, a number of observers have expressed concern about the long-run competitiveness of some U.S. high-technology exports. Since the postwar reconstruction of West European and Japanese industries, those countries have gradually emerged as alternative sources of industrial innovation. Moreover, U.S. companies, through direct foreign investment, licensing agreements and other mechanisms, have begun to transfer their technologies abroad at a more rapid rate. Industries in other industrial countries and the advanced developing countries have succeeded in assimilating technologies developed

in the United States and competing with U.S. exporters in third markets. While, in the past, this pattern was limited largely to industries with mature technologies, some observers maintain that U.S. high-technology industries are facing similar competitive pressures.[1/]

U.S. producers in both the agricultural and manufacturing sectors should benefit in the near future from the substantial depreciation of the dollar against the currencies of some of the major U.S. trade partners during 1977-1978.[2/] Dollar depreciation has the effect of reducing the foreign currency price of U.S. exports and raising the dollar price of U.S. imports, thus improving the price competitiveness of exporters or import competitors. Empirical studies suggest that any improvement in the price competitiveness of U.S. exports is likely to lag behind the depreciation by about 1 1/2 years.[3/] (Thus, the recent improvement in the U.S. trade balance may be due in part to the effects of

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1/ See, for example, Jack Baranson, "International Transfers of Industrial Technology by U.S. Firms and Their Implications for the U.S. Economy," prepared for the U.S. Department of Labor, Bureau of International Labor Affairs, December 1976. Also, George D. Holliday, "Trends in U.S. Technological Progress and International Trade Competitiveness," Congressional Research Service, August 27, 1976.

2/ See Arlene Wilson, "Depreciation of the U.S. Dollar," Congressional Research Service Issue Brief 78033.

3/ Anthony M. Solomon, Testimony, in U.S. Congress, House, Committee on Banking, Housing, and Urban Affairs, Subcommittee on International Finance, Export Policy, Hearing, 95th Congress, 2d session, Part I, February 6, 1978 p.6.

the depreciation of the dollar.) However, such an improvement in the price competitiveness of U.S. exports is dependent on the domestic rate of inflation. A U.S. inflation rate in excess of those of its major trade partners would tend to offset the price advantage engendered by depreciation of the dollar.

III. U.S. Government Incentives for Exporters.

The major U.S. Government programs designed specifically to promote exports are tax incentives, export credits and marketing information services. The principal tax incentive is the Domestic International Sales Corporation (DISC), which is designed to make exporting more profitable by in effect, lowering corporate income taxes. The Export-Import Bank and the Department of Agriculture's Commodity Credit Corporation promote exports through their export financing activities. The Departments of Commerce, State, and Agriculture provide a variety of informational and marketing services designed to expand exports. A number of other programs, many of which are designed to accomplish other goals, may have the effect of stimulating exports. Finally, U.S. participation in the multilateral trade negotiations and the Government's exchange rate policy have major implications for U.S. exports.

Domestic International Sales Corporation (DISC)

The principal tax device designed to promote exports is the Domestic International Sales Corporation. Created by the Revenue Act of 1971 (P.L. 92-1978), DISC is a largely paper organization designed to purchase export goods from a domestic American parent corporation, and then to export them to a foreign purchaser. For example, a company might establish a wholly owned DISC. Goods destined for export would be sold by the company to its own DISC, and the DISC would in turn sell the goods to purchasers in a foreign country.

Prior to the Tax Reform Act of 1976, taxable income from the export sale was divided between the parent and the DISC in one of two ways. Depending on which was larger, 50 percent of the profits or 4 percent of the gross receipts was allocated to the DISC. In most instances, the 50 percent rule was followed. The 50 percent of taxable income attributed to the parent company was subjected to the statutory corporate tax rate of 48 percent. However, only half of the income attributed to the DISC was taxed at the statutory corporate rate. The rest would not be taxed until it was returned to the parent corporation. Because the tax need never be returned to the parent, the delay (deferral) in paying the tax was generally regarded as a permanent subsidy. In summary terms, a DISC resulted in reducing the tax rate applied to export income from 48 to 36 percent. In other words, only three quarters (3/4) of export income earned by a DISC was subject to the normal corporate rate.

The benefits of a DISC, however, are to be gradually reduced as a result of the Tax Reform Act of 1976. From the start, the DISC mechanism was criticized because it reduced taxes on both the income from new exports and the income from exports that would have been made in any case. The 1976 law attacks that problem by applying the DISC subsidy only to that portion of export income that exceeds a particular historical base.

The initial export base was to be the average gross receipts from exports for the four-year period 1972 through 1975. After 1979, the base period would move forward year by year. In other words, in 1979 the base period would be 1974 through 1977. To qualify for DISC benefits, export income must exceed 67 percent of the average base period income. The new provisions apply to export income for all tax years beginning after December 31, 1975.

The Tax Reform Act of 1976 contained a number of other features that further restricted the use of the DISCs. After October 2, 1975, only 50 percent of export income from military sales can qualify for DISC treatment. The ability of a parent corporation to make a tax free disposition of DISC securities has also been curtailed.

The DISC program has been used extensively by U.S. business. In DISC year 1976, there were 4,822 DISCs. DISC benefits accrued to over two-thirds of total U.S. exports during that year. DISC

is the most costly of Government export incentives, resulting in revenue losses of over $1 billion in recent years. Estimated revenue losses for 1978-1980 are provided in Table 1.

Table 1: Estimated Revenue Loss from DISC, Fiscal Year 1978-1980

Fiscal Year	(millions of dollars) Revenue Loss
1978	1,135
1979	1,335
1980	1,525

Source: U.S. Senate. Committee on the Budget. Tax Expenditures: Relationships to Spending Programs and Background Material on Individual Provisions. 95th Congress, 2d session. Washington, U.S. Govt. Print. Off., 1978, p. 214.

Export-Import Bank

The Export-Import Bank of the United States (Eximbank) is the primary agency providing official credit assistance to U.S. exporters. The Export-Import Bank Act of 1945, as amended, directs the Bank to aid in financing and to facilitate U.S. exports and imports and stipulates that Eximbank financing must be competitive with financing offered by other governments.

In its efforts to carry out this function, Eximbank has developed a variety of services to U.S. exporters and financial institutions. The most important of these are direct loans, financial guarantees, exporter credit insurance and discount loans.

Direct loans are dollar credits extended by Eximbank directly to foreign borrowers for purchases of U.S. goods and services. The borrowers must use the loans to pay U.S. exporters and must repay them in dollars. The direct lending program is designed to supplement private sources of financing by providing credits in some cases when private lenders are unwilling to assume the risks or by extending credit on terms longer than private lenders can provide. Generally, Eximbank requires a downpayment from the buyer, provides part of the financing from its own funds, and requires private financing for the balance.

Financial guarantees are assurances to private financial institutions that finance U.S. exports that their loans will be repaid. The guarantees are backed by the full faith and credit of the United States. Such guarantees are designed to encourage private lenders to extend export credits and, in some cases, to lower interest cost to the borrower.

Credit insurance is provided to exporters of U.S. goods and services to protect them against the political and commercial risks inherent in foreign trade transactions. The insurance is provided by Eximbank in cooperation with the Foreign Credit Insurance Association, a group of approximately 50 U.S. insurance companies. The private insurers cover the normal commercial risks, such as insolvency of the foreign buyers, and Eximbank covers political risks, such as war or expropriation.

Discount loans are advance commitments to discount export debt obligations which U.S. commercial banks acquire. The Eximbank commitment assures the private lender that additional funds will be available should they be needed during the full maturity of the obligation. Thus, Eximbank provides an incentive to private banks to participate in the financing of U.S. exports.

In recent years, Eximbank has participated in an average of about 10 percent of all U.S. exports. It has concentrated its support

on exports of manufactured goods (approximately 18 percent of all U.S. exports in this category) and capital goods (approximately 21 percent). Transportation and construction equipment and electric power plants (especially nuclear power plants) have accounted for a major portion of Eximbank financing. Agricultural exports have accounted for only a small percentage of Eximbank activities. Eximbank's management maintains that the Bank's concentration on large-scale, capital-intensive projects is justified because private banks are frequently unable to provide the large, long-term credits necessary to facilitate such sales. Generally, Eximbank benefits U.S. exporters by providing financing at better terms than private financial institutions. (For example, its credits are extended at lower interest rates and with longer repayment terms.)

In fiscal year 1977, over 140 countries participated in Eximbank programs. Among the major beneficiaries were developing countries, such as Algeria, Brazil, Taiwan, Mexico, Korea, and industrial countries, such as Canada, France, Japan, and the United Kingdom.

During fiscal year 1977, Eximbank authorizations (including loans, insurance, and guarantees) totaled $5.6 billion. Eximbank programs supported $8.5 billion in U.S. exports. The level of Eximbank activities in 1977 represented a decline from the previous

few years, partially the result of more restrictive lending criteria. The peak year of Eximbank activity was in fiscal year 1974, when total authorizations of $9.1 billion supported $12.8 billion of U.S. exports. Estimated authorizations for 1978-1980 are summarized in Table 2.

Table 2: Estimated Credit Activity for Official Export Financing Programs, Fiscal Years 1978-1980 (in millions of dollars)

Program	Credit activity 1978	1979	1980
Export-Import Bank 1/	7,865	9,500	10,100
Short-term agricultural credits 2/	1,700	1,500	1,250
Food for Peace 3/	1,160	1,157	1,256

(Credit activity reflects the sum of all loans obligated during a fiscal year under direct loan programs, or the value of all commercial loans or export shipments guaranteed or insured by Eximbank programs.)

1/ Expected authorizations, all Eximbank estimates.

2/ Expected credits. Commodity Credit Corporation estimates.

3/ Food for Peace, titles I and II (loans and direct grants), excluding ocean transportation costs.

Commodity Credit Corporation estimates.

Source: U.S. Congress, Senate. Committee on the Budget. Tax Expenditures: Relationships to Spending Programs and Background Material on Individual Provisions. 95th Congress, 2d session. Washington, U.S. Govt. Print. Off., 1978, p. 214.

Commodity Credit Corporation Export Credit Sales

The Commodity Credit Corporation (CCC) Export Credit Sales Program, established in 1956 under the authority of the Commodity Credit Corporation Charter Act, is designed to help U.S. agricultural exporters expand sales in foreign markets. The CCC provides financing for exports of specified, privately owned agricultural commodities on a deferred payments basis, usually for periods of 6 months to 3 years. (A bill passed late in the 95th Congress authorizes the CCC to provide, under certain conditions, intermediate-term (3-10 year) credits for agricultural exports).

CCC financing stimulates U.S. agricultural exports by making credits available at somewhat better terms than exporters could obtain elsewhere. Interest rates for CCC credits vary, but are usually slightly below equivalent market rates. Maturities for CCC credits are often longer than agricultural export credits offered by private banks.

Exports financed under the Export Credit Sales Program in fiscal year 1977 totaled $755.3 million. The peak year was fiscal year 1973, when $1,029 million of exports were financed. The budget for fiscal year 1978 was $1.7 billion (See table 2).

P.L. 480 (Food for Peace) Exports

The Food for Peace Act (P.L. 83-480), originally enacted in 1954, is designed to promote U.S. agricultural exports and provide

assistance to less developed countries. The concessional sales program under title I of the Act provides long-term, low-interest rate loans to developing countries which meet certain poverty level criteria. (Interest rates have averaged 3 percent and repayment periods have been as long as 40 years.) Title II provides for grants through humanitarian relief activities.

Initially, agricultural products exported under this program were surplus products in Commodity Credit Corporation stocks. However, since 1966, the Government has purchased some of the products to be exported on the open market. The annual value of exports under the P.L. 480 program has varied from $0.9 billion in FY 1974 to $1.6 billion in FY 1965.[1/] Estimates for fiscal years 1978-80 are provided in Table 2.

1/ For additional details on programs to promote U.S. agricultural exports, see, Congressional Research Service, "Potential for U.S. Agricultural Trade Expansion," in U.S. Congress, Senate, Committee on Agriculture, Nutrition, and Forestry, Subcommittee on Foreign Agricultural Policy, Export Promotion, Hearings, 95th Congress, 2d session, Washingtion, U.S. Govt. Print. Off., 1978, pp. 208-233.

Export Promotion Programs

The Department of Commerce's export promotion programs are concentrated in the Industry and Trade Administration. The following are brief descriptions of the export services provided by the Industry and Trade Administration:[1/]

Export Stimulation Programs

Media Campaigns are conducted through the facilities of the Ad Council, utilizing the American business press representing some 2,300 publications, to promote the image of exporting as beneficial to participating firms as well as the Nation

"E" and "E Star" Awards are granted to firms that have achieved outstanding export success as a means of demonstrating to others, by example, the benefits of exporting

Domestic Publications describe services available in the Department and elsewhere to assist firms in exporting

Multiplier Activities enlist the support and cooperation of appropriate private sector groups and firms, such as banks, trade associations and so forth, in joint efforts to stimulate interest in exporting and to counsel new exporters

Export Counseling and Information Programs

General Business Counseling Services provide orientation-type information to companies interested in exporting and in need of advice on how to proceed

Seminars on how and where to export are sponsored or co-hosted with private market organizations to stimulate interest in and knowledge about exporting

Country Specialist Counseling provides detailed advice and guidance on how best to develop and take advantage of commercial opportunities in individual countries

International Marketing Information provides extensive and in-depth published information and reports on marketing techniques, prospects, practices and conditions in almost every country in the world

Foreign Market Research provides detailed information on export potential for specific U.S. products in key foreign markets, much of it conducted on-the-spot by market research firms under contract

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1/ These program descriptions are provided in Department of Commerce, Industry and Trade Administration, "Export Promotion Strategy and Programs," reprinted in U.S. Congress, Senate, Committee on Banking, Housing, and Urban Affairs, Subcommittee on International Finance, Export Policy; hearing, 95th Congress, 2nd session, Part 6, April 5, 1978, pp. 391-393.

Customer Identification and Contact Programs

Export Contact Lists provide requesting U.S. firms and official users with specialized lists of foreign buyers and representatives in select countries for select product categories

The Trade Opportunities Program provides subscribing U.S. firms with specific trade leads abroad through a computer-based notification system

The Major Projects and Overseas Product Sales activities apprise U.S. firms of specific "big ticket" opportunities abroad--namely large scale engineering, design, and construction projects, and major product and equipment sales opportunities--and directly assist them to compete successfully for contracts and orders

The Agent/Distributor Service provides requesting U.S. firms with the names of specific potential foreign representatives

The New Products Information Service publishes and disseminates abroad information on U.S. firms having newly developed or manufactured products available for export

The Exporter/Agent Information System (a proposed new program which is presently under study) identifies individual U.S. suppliers of specific products, and provides information about the firm and its product on microfilm cassettes for use at commercial libraries at Foreign Service Posts abroad

The Foreign Buyers Program encourages groups and individual foreign buyers to come to the U.S. to purchase goods and services, assists in making contacts between potential buyers and U.S. suppliers, and supports foreign buyer attendance at domestic trade shows

Overseas Sales Promotion Programs

Trade Centers and International Marketing Centers provide U.S. firms with continuing opportunities to demonstrate their products in 14 major markets abroad to a select audience of targeted foreign buyers and representatives

Trade and Industrial Exhibits provide U.S. firms with scheduled opportunities to demonstrate their products under Commerce-sponsorship in major or specialized international trade fairs or "solo" exhibitions abroad

Catalog Shows and Video Catalog Exhibitions provide U.S. firms with scheduled opportunities and facilities to display their product catalogs and sales literature and to depict the operations of their company and product in developed and emergent markets abroad

The Overseas Information Services provide visiting U.S. firms at U.S. Trade Centers, International Marketing Centers, Embassies and Consulates abroad, with on-the-spot counseling and assistance in contacting foreign buyers and representatives

In-Store Promotions provide U.S. suppliers of consumer goods with scheduled opportunities to expose their products to the overseas public through Commerce-sponsored events held in select foreign retail stores

Specialized and Industry Organized-Government Approved (IOGA) Trade Missions provide groups of U.S. firms with scheduled opportunities to travel abroad under Commerce sponsorship to meet directly with potential foreign buyers and representatives

Technical Trade Missions provide foreign buyers and representatives with scheduled opportunities to learn about the latest product/industrial technologies in the U.S. available from U.S. suppliers

In carrying out these programs, the Industry and Trade Administration is assisted by Foreign Service economic and commercial officers under the jurisdiction of the Department of State. Foreign Service officers assigned to U.S. embassies and consulates abroad report on economic developments and market conditions in their countries of assignment. This information is reported to the Commerce Department, which disseminates it to the U.S. business community. Foreign Service officers abroad also directly assist U.S. businessmen in contacting potential buyers of their products. The combined State and Commerce Department budget for export promotion has totaled over $50 million in recent years.

The Department of Agriculture's Foreign Agricultural Service (FAS) is responsible for promotion of agricultural exports. FAS provides the following kinds of services for U.S. agricultural exporters.[1/]

1/ Program descriptions are provided in U.S. Congress, House, Committee on Appropriations, Subcommittee on Agriculture and Related Agencies, Agriculture and Related Agencies Appropriations for 1978; hearings, 95th Congress, 1st session, Washington, U.S. Govt. Print. Off., 1977, 170.

It maintains a worldwide agricultural intelligence and reporting service to provide U.S. farmers and traders with information on world agricultural production and trade that they can use to adjust to changes in world demand for U.S. agricultural products. This is done through a continuous program of reporting by agricultural attaches and officers located in 67 posts throughout the world covering some 108 countries. Reporting includes information and/or data on foreign government policies, analysis of supply and demand conditions, commercial trade relationships and market opportunities.

The Foreign Agricultural Service analyzes agricultural information essential to the assessment of foreign supply and demand conditions in order to provide estimates of the current situation and to forecast the export potential for specific U.S. agricultural commodities. Published economic data about commodities are combined with attache reports and subjected to analysis through advanced econometric techniques to generate these estimates.

In addition, the Service is currently responsible for determining the utility and cost effectiveness of using satellite, meteorological and climatological data to predict global production of major crops. These operations, being conducted by the LACIE program, will yield estimates of wheat production for the U.S., Canada and other regions outside North America which will be used to evaluate the experiment. The program has already begun to design and test an advanced prototype for an operational crop forecast system within USDA. The program is conducted in cooperation with the National Aeronautics and Space Administration (NASA) and the National Oceanographic and Atmospheric Administration (NOAA).

The Service develops foreign markets for U.S. farm products through effective market promotion activities. It provides tradesmen, both foreign and domestic, with services that are necessary to build and maintain markets for U.S. products overseas.

Under authority of the Trade Act of 1974, the Service directs and coordinates Department participation in the formulation of trade programs and Agreements in order to stabilize and expand the world trade of U.S. agricultural products. It effectively negotiates to reduce restrictive tariff and trade practices which are recognized as barriers to the import of U.S. agricultural commodities.

The fiscal year 1978 budget for FAS was $43 million, about $2 million higher than the previous year.

Trade Negotiations

The trade barriers imposed by foreign governments also serve as disincentives to U.S. exporters. A key goal of U.S. foreign trade policy in the postwar period has been the elimination or reduction of many of the barriers which restrict world trade through bilateral and multilateral trade negotiations. In 1973, the United States and over 100 other countries signed the Tokyo Declaration which initiated the seventh round of trade negotiations under the auspices of the General Agreement on Tariffs and Trade (GATT). The Tokyo Round of the multilateral trade negotiations is expected to be completed in late 1978 or early 1979.

Negotiators at the previous six rounds of trade negotiations concentrated on reduction of tariffs and elimination of quantitative restrictions on trade in manufactured products. Most economists believe that the success of these negotiations has contributed significantly to the rapid expansion of world trade. U.S. exporters, like those in other countries, have been primary beneficiaries. However, the previous rounds of negotiations made relatively little progress in liberalizing trade in agricultural goods and eliminating many of the nontariff measures (NTMs) which distort international trade. (NTMs include measures, other than tariffs, which restrict imports as well as measures which artificially

increase the level of trade. Among the former are import quotas, restrictive product standards, and government procurement procedures. The latter include government export subsidies). All countries, including the United States, have made extensive use of NTMs. If successful, the conclusion of the present round of trade negotiations could provide a major stimulus to U.S. exporters.

Exchange Rate Policy

Since 1973, the U.S. Government has supported the more flexible exchange rate system of "managed floating". Generally, the Government has allowed the exchange rate of the dollar to be determined by the interaction of supply and demand forces. Thus, until November 1978, the Carter Administration's stated policy was to intervene only to counter disorderly markets (i.e., the U.S. Government would buy dollars on international monetary exchanges when dollar depreciation was considered to be caused by speculative or psychological forces, and not by underlying economic conditions). Despite criticism by a number of foreign government officials, the Administration allowed the dollar to depreciate substantially against some major foreign currencies.

This policy changed somewhat in November 1978. After the dollar had again begun to depreciate rapidly, the Government intervened more

actively to support it. The discount rate was raised, and reserve requirements on large time deposits were increased. The resulting higher interest rates were expected to attract capital inflows, thus relieving pressure on the dollar. The Administration also announced that it would increase its gold sales and would intervene more forcibly in foreign exchange markets by exchanging more of its foreign exchange reserves for dollars.

The Government's exchange rate policy should be seen as an integral part of its export efforts. The general policy of allowing the dollar to depreciate may result in an improvement of the price competitiveness of U.S. goods and thus an expansion of exports. (There is evidence that this improvement is already taking place). However, the degree to which this happens will depend on a number of factors, including the rate of domestic inflation relative to the rates of other countries, the degree to which foreign buyers respond to price changes and expand their purchases of U.S. exports, and the extent of foreign barriers to U.S. exports.

Other Government Programs and Policies

The following are brief summaries of other Government programs and policies which may have (or may have had in the past) the effect of stimulating U.S. exports.

Taxation of U.S. citizens abroad. Part of the foreign earned income of U.S. citizens residing abroad may be excluded from income for tax purposes. Some observers maintain that the stationing of employees abroad by U.S. businesses is important to their export activities. The tax exclusion, it is suggested, allows more Americans to live abroad and thus stimulates U.S. exports.[1/]

Western Hemisphere Trade Corporation. For some years, the Western Hemisphere Trade Corporation (WHTC) has constituted a limited subsidy to U.S. exports to the Western Hemisphere. To qualify as a WHTC, a firm must do all of its business outside the United States but within the Western Hemisphere. In addition, 90 percent of the WHTC's income must be from the active conduct of a trade or business (as opposed to receiving dividend payments) and at least 95 percent of the preceding three years' (or the life of the corporation if shorter) income must be from outside the United States.

For firms that qualify as a WHTC, there is a subtantial reduction in taxes. The overall effect of a WHTC is to reduce the corporate income tax rate from 48 to 34 percent - a drop of 14 full percentage points. Despite the evident advantages, the WHTC mechanism has been little used. In 1972, the taxes foregone to permit the WHTC deduction amounted to some 40 million dollars.

1/ U.S. Department of Treasury. Office of Tax Analysis. The American Presence Abroad and U.S. Exports, by John Mutti. OTA Paper 33, October 1978.

However, the future of the WHTC is extremely limited. The Tax Reform Act of 1976 provided for a four-year phaseout of the WHTC benefit. For tax years following 1979, the WHTC will be repealed.

China Trade Act Corporation. Until 1978, a China Trade Act Corporation (CTAC) could obtain a special deduction that could completely eliminate any U.S. income tax liability. To qualify as a CTAC there were both a source-of-income test and an ownership test. For a CTAC, income must have come from sources within Taiwan and Hong Kong (the original purpose of the 1922 law was to promote business in China, but after the Communist takeover CTACs were restricted to Taiwan and Hong Kong). The deduction was further limited by the proportion of par value stock that was owned by U.S. citizens or residents of Hong Kong, Taiwan or the United States. If 100 percent of the stock met the ownership test, all U.S. corporate tax liability would be eliminated.

In addition, dividends paid to shareholders who were residents of Hong Kong or Taiwan were not subject to U.S. tax. In other words, a group of American citizens that owned a CTAC and lived in Hong Kong or Taiwan would not have to pay any U.S. corporate or individual income taxes on CTAC income.

Much like WHTC, the CTAC appealed to both raw material producers and wholesalers. Because of the radical changes that took place on mainland China, the CTAC provision was little used. Since

enactment of the provision in 1922, nearly 300 firms had been incorporated under the Act. By 1968, however, the majority of these firms were no longer in existence, and only four were actively conducting a business in Hong Kong or Taiwan. Under the Tax Reform Act of 1976, deductions under the CTA were phased down and then eliminated for taxable years beginning after December 31, 1977.

Commodity Credit Corporation Export Subsidies and P.L. 480 Barter Programs.[1/] Two Commodity Credit Corporation programs, the export subsidies and barter programs, were formerly used to stimulate agricultural exports, but are now inactive. Under the export subsidies program, the CCC provided direct subsidy payments to exports of specified farm commodities. The subsidies were intended to compensate exporters for the differential between the world market price and the higher U.S. price, making it economically feasible to export U.S. products. From 1964 to 1973, almost 30 percent of U.S. agricultural exports received such subsidies. The payments were suspended because they were considered no longer necessary to promote exports.

Under the barter program, between 1964 and 1974, the CCC exchanged surplus agricultural commodities in its stocks for foreign strategic materials or goods and services needed by U.S. Government agencies (primarily the Defense Department and the Agency for

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1/ Congressional Research Service, "Potential for U.S. Agricultural Trade Expansion," op. cit., p. 228.

International Development). The bartered commodities, which accounted for 5 percent of total U.S. agricultural exports in 1964-1974, were intended for foreign customers who did not have sufficient currency to pay for them but had materials needed for U.S. strategic stockpile.

Deferral of Income of Controlled Foreign Corporations. The foreign subsidiary of a U.S. corporation is not taxed on the subsidiary's income until the income is remitted or repatriated to the U.S. parent company. The deferral of U.S. tax liability continues as long as the income is reinvested in the subsidiary or other foreign subsidiaries. A tax credit is allowed for the amount of foreign taxes paid on repatriated income. To some extent, the special treatment of foreign subsidiary income may stimulate U.S. exports. For example, the establishment or expansion of a foreign subsidiary may require exports of capital goods or other inputs from the parent company to the subsidiary.

Overseas Private Investment Corporation. The Overseas Private Investment Corporation (OPIC) is a U.S. Government agency chartered to encourage U.S. private investments which support economic development in developing countries. It provides a number of services and incentives to U.S. companies investing abroad, including insurance of private investments against political risks. Like tax deferral, OPIC's encouragement of U.S. foreign investment may stimulate, to some extent, exports to foreign subsidiaries.

Foreign Military Sales Program. The U.S. Government provides credits and loan guarantees through the Department of Defense to friendly countries for the purchase of U.S. military goods and services. While this program is used primarily as a tool of U.S. foreign policy, it provides significant support for defense-related exports.

Foreign Trade Zones. A Foreign Trade Zone (or free-trade zone) is a warehouse or manufacturing area approved by the Department of Commerce's Foreign Trade Zones Board to receive imported goods without formal Customs entry and without payment of duties. The use of a zone benefits a U.S. exporter primarily because duties are not applied on imported materials or components used in manufacture or assembly in the zone if the finished product is exported.

Duty Drawbacks. A U.S. exporter is entitled to a duty drawback or refund of previously deposited customs duties assessed on imported products that are incorporated within an exported finished product.

Exemption from Federal Excess Taxes. Sales for export are exempt from Federal retailer's excise taxes.

Webb-Pomerene Associations. The Webb-Pomerene Act exempts export trade associations from the ban on certain activities which would otherwise violate antitrust laws. It provides a legal basis for U.S. companies to pool their efforts to expand exports. However, it has had little effect on U.S. exports.

Foreign Aid. U.S. bilateral assistance programs increase the foreign demand for U.S. exports by the use of so-called "tied aid", which restricts the use of aid funds to the purchase of U.S. products. In addition, they sometimes create a demand for U.S. products which remains after foreign aid is discontinued. One study of the impact of U.S. bilateral aid programs on U.S. exports estimated that each dollar of AID development assistance results in a 50- to 90-cent increase in U.S. exports.[1/]

State Export Promotion Activities. Many States provide financial and non-financial export incentives to attract industry. Several of them exempt from State taxation all receipts from sales outside the State, regardless of whether sales occur at home or abroad. Included among other financial incentives are various exemptions from State and local taxes for specified time periods.

In addition to financial incentives, most States conduct seminars, workshops and export education programs to familiarize mainly small and medium sized businesses with the procedures (documentation, licensing, etc.) and advantages of exporting. In this regard, each year the Federal Government grants $50,000 to each State to assist in expanding export development programs.

1/ Congressional Research Service, The Impact of the United States Bilateral Aid Program on U.S. Exports and Other Economic Variables, by Raymond Ahearn and Warren E. Farb, Multilith 77-53, March 2, 1977.

IV. Government-Imposed Disincentives for Exporters

U.S exporters frequently complain that various Government laws, regulations and policies have the effect of restricting exports. Some of their complaints relate to programs designed specifically to influence foreign trade; others relate to Government measures which generally increase production costs for business and thus adversely affect the competitiveness of U.S. exports on foreign markets. The following is a list of the major regulatory programs and policies that are asserted (especially by U.S. exporters) to have a negative effect on U.S. exports. The list is intended only to reflect the views of those observers who see elements of an anti-export bias in Government policies. Generally, the impact of these Government measures cannot be determined with precision.

Export Controls

In the post-World War II period, U.S. export control legislation has contained three rationales for imposing Government restrictions on U.S. exports: (1) to preserve national security; (2) to prevent shortages and export demand-induced inflation in the domestic economy; and (3) to promote U.S. foreign policy. Export controls have been used most frequently for national security purposes, primarily to restrict U.S. exports to the Soviet Union and other communist countries. Under the Export Administration Act of 1969 (EAA), the Department of Commerce controls exports of goods or

technologies that would make a significant contribution to the military power of a potential adversary and would also be detrimental to U.S. national security. Most frequently, denials of export licenses on national security grounds have been issued on applications to sell high-technology products to communist countries.

Even when licenses are ultimately approved, the national security export control program often involves delay in acting on applications. Although the vast majority of applications are handled routinely and quickly, some applications involving major export sales take longer because of extensive interagency review. Businessmen often complain that such delays can result in the loss of contracts.

Foreign policy export controls are also administered by the Commerce Department after interagency discussions, primarily with the State Department. Prominent examples of foreign policy controls are the following: general embargoes on trade with Cambodia, Cuba, North Korea and Vietnam; the economic boycott of Rhodesia, declared in compliance with a United Nations Resolution; human rights restrictions, such as prohibitions on exports of military or police equipment to South Africa; ad-hoc restrictions, such as denial of a license to export certain goods to Libya because of its alleged support for international terrorism; and the routine referral to the National Security Council of applications to export oil and gas equipment to the Soviet Union.

The EAA also authorizes the Department of Commerce to restrict exports in order to protect the domestic economy from excessive drain of scarce materials and to reduce the inflationary impact of foreign purchases. Short supply controls are currently imposed on exports of petroleum and petroleum products and were in the past imposed on other materials, such as ferrous scrap, soybeans and an array of other agricultural products.

Restrictions on U.S. Trade with Communist Countries

In addition to export controls, there are special restrictions on trade with communist countries which have indirectly limited the volume of U.S. exports to those markets. The most important of these are restrictions on the extension of most-favored-nation tariff treatment and U.S. Government export credits to those countries. An amendment to the Trade Act of 1974 conditions the extension of MFN treatment and Government credits to communist countries on compliance with certain freedom-of-emigration provisions. The Export-Import Bank Amendments of 1974 places a $300 million ceiling on Eximbank credits to the Soviet Union and a $40 million subceiling on credits for exports of energy-related goods or services to the Soviet Union.

Regulation of the Sale of Military Equipment

There are various limitations on the export of military equipment. The Arms Export Control Act requires that direct military sales be licensed by the Department of State's Office of Munitions

Control. The Renegotiation Board recently amended its regulations to subject foreign military sales contracts to renegotiation (i.e., recapture of "excessive" profits made by a U.S. manufacturer on arms export sales). Contracts for sales brokered by the Department of Defense under the Arms Export Control Act are subject to most of the Armed Services procurement regulations. Finally, on May 19, 1977, the President announced a policy of conventional arms transfer restraints, implemented by various controls on military hardware exports. Among the controls is a prohibition on the United States, being the first supplier to introduce into a region new weapons systems which would create a new or higher combat capability.

Antitrust Laws

Under U.S. antitrust law, actions occurring in foreign countries which have substantial and foreseeable effects on domestic commerce are subject to U.S. antitrust jurisdiction. Many businessmen complain that the antitrust laws inhibit their overseas activities. The major problem is apparently the uncertainty of application of antitrust laws. Businessmen, reluctant to risk antitrust violations, may sometimes limit their involvement in international business activities, thus losing possible export opportunities.

Businessmen maintain that a major area of uncertainty is the establishment by U.S. firms of consortia to bid on foreign projects. The Webb-Pomerene Act provides an antitrust exemption for domestic

firms combined in an association for the export of "goods, wares, and merchandise" under certain specified conditions. However, the law does not include a similar exemption for the export of services—a potential area of significant export growth.

National Environmental Policy Act (NEPA) Environmental Impact Statements

U.S. exporters have faced uncertainty over whether the National Environmental Policy Act (NEPA) requires environmental impact statements for U.S. export licenses, Eximbank financing, Overseas Private Investment Corporation insurance and other Government foreign trade programs. (The Agency for International Development has already begun to take into consideration the environmental impact of U.S. foreign assistance projects.) There has been concern in the business community that environmental constraints may have a negative effect on exports by introducing delay and uncertainty into international commercial transactions.

Nuclear Export Restrictions

The Nuclear Non-Proliferation Act and other Government policies have a number of restrictions affecting U.S. nuclear and nuclear-related exports. Industry spokesmen claim that these policies, combined with complex procedural requirements for exporting nuclear materials and equipment have made the United States less competitive in international markets.

Anti-Boycott Statutes and Regulations

Anti-boycott amendments to the Export Administration Act and the Internal Revenue Code contain overlapping and allegedly inconsistent prohibitions, exceptions, reporting requirements and sanctions. Antitrust law imposes still a third set of legal constraints. Businessmen maintain that the complexity of the regulations creates confusion and uncertainty which complicate the international activities of exporters and inhibit potential exporters from entering the export field.

Foreign Corrupt Practices Act

Some businessmen assert that uncertainty about the meaning of certain provisions of the Foreign Corrupt Practices Act and about Department of Justice and Securities and Exchange Commission enforcement policies will inhibit many international business transactions. They assert that these uncertainties create large risks which may force them to forego certain business opportunities.

Human Rights Restrictions

A number of laws have been passed in recent years which restrict U.S. economic and military assistance to countries which have poor records in the observance of basic human rights. To the extent that foreign aid and military assistance generate additional exports (see above), the human rights provisions may limit U.S. exports. When making decisions on loans, guarantees or insurance, the Overseas Private Investment Corporation and the Export-Import Bank are also required

by law to consider the human rights records of recipient countries. Eximbank has denied loans to some countries with poor human rights records. Exports of crime control equipment to most destinations require validated licenses from the Commerce Department.

Health and Safety Export Restrictions

Federal regulations restrict the export of some consumer goods that have been banned for domestic use for health or safety reasons. An example is the Consumer Product Safety Commission's (CPSC) 1978 action prohibiting the export of TRIS-treated garments. Amendments to the Consumer Product Safety Act passed by the 95th Congress require anyone intending to export a product which does not comply with a U.S. product safety rule to file a statement with the CPSC at least 30 days prior to the export. CPSC is required to notify the appropriate public health officer in the importing country.

Cargo Preference Laws

Cargo preference laws, such as the Cargo Preference Act and Public Resolution 17, require the use of U.S.-flag vessels for transportation of U.S. Government-financed commodities (including P.L. 480 agricultural commodities and Eximbank-financed exports). Such laws may result in higher exporter costs--and hence lower competitiveness--since foreign-flag vessel freight rates are typically less than those of U.S.-flag vessels.

Laws, Regulations and Policies with Indirect Effects on the Cost Competitiveness of U.S. Exports

There are many Federal laws and regulations which do not directly affect exports, but which mandate substantial capital and other expenses by U.S. companies. When passed on through price increases, the result may be diminished competitiveness of U.S. exports. Prominent examples include: the Clean Air Act; the Federal Water Pollution Control Act; the Occupational Safety and Health Act; the Toxic Substances Act; the Consumer Product Safety Act; minimum wage laws; and the Employment Retirement Income Security Act (ERISA).

V. Carter Administration's Program on Export Promotion--Brief Description and Evaluation

On September 26, 1978, President Carter announced a comprehensive program to stimulate U.S. exports.[1/] The Administration's program focused on three areas of export policy:

(1) increased direct assistance to U.S. exporters;

(2) reduction of domestic U.S. barriers to exports; and

(3) reduction of foreign barriers to U.S. exports.

Elements of the first two areas are discussed in this section. The third measure--U.S. participation in trade negotiations--is not a new proposal, but a continuation of past policy (see above, p. 23). No further discussion of the trade negotiations is included here. However, it is important to note that a successful conclusion of the current round of Multilateral Trade Negotiations could provide a major stimulus to U.S. exports. Similarly, the Carter Administration's policy of allowing the dollar to depreciate in 1977-1978 (which was not announced as part of the export program) could have an important stimulative effect on U.S. exports. Taken together, these two policies could be much more significant, from the standpoint of export expansion, than any of the other programs announced by President Carter.

1/ President Carter's statement is reprinted in U.S. Congress, Senate, Committee on Commerce, Science and Transportation, National Export Program, Hearing, 95th Congress, 2d session, September 28, 1978, Washington, U.S. Govt. Print. Off., 1978, pp. 73-76.

Direct Assistance to U.S. Exporters

The President's proposals to increase direct assistance to exporters places major emphasis on increased export credit assistance--both Eximbank and CCC short-term agricultural credits. Eximbank direct loans are to be increased from $700 million in FY 1977 to $3.6 billion in FY 1979. Short-term agricultural credits are to be increased from $755 million in FY 1977 to $1.7 billion in FY 1978. (Authorizations for both of these increases had been requested before the President announced his export program.) In both cases, FY 1977 credit activity had been at low levels (compared to the early 1970s) for a number of reasons, including more restrictive lending criteria and reduced demand for U.S. agricultural products. The expansion for FY 1978-1979 marks a resumption of the upward trend for official credit assistance of the early 1970s.

Proponents of more Government assistance to U.S. exporters often identify official export credits as one of the most valuable Government programs. Official credits, it is maintained, are necessary to compensate for gaps in the private financial market. For example, it is claimed that many long-term, risky export transactions would not be financed by private institutions. Moreover, proponents maintain that U.S. export credit programs must be improved to meet the competition from aggressive official lending programs in other countries. According to advocates of this point of view, official

export credits make possible many U.S. exports which could not take place without them.

Opponents of official export credit programs often maintain that such assistance provides an implicit subsidy to the export sector which is not needed and which has the effect of distorting private investment decisions. In particular, they argue that under the current exchange rate system, any expansion of exports resulting from official credit assistance will be offset by shifts in exchange rates. For example, an increase in U.S. exports tends to drive up the value of the dollar, making U.S. exports more expensive and imports less expensive. Thus, appreciation of the dollar tends to counteract the effort to expand exports. (It should be noted that this is an argument against all Government efforts to stimulate exports under a flexible exchange rate system.)

Various efforts to measure the "additionality" of Eximbank programs (i.e., the amount of additional exports generated by the programs) have come to radically different conclusions. A Treasury Department study estimated that all Eximbank programs generated about $4 billion in U.S. export sales in FY 1976, $3.4 billion of which was attributed to Eximbank's direct loan program.[1/] However, a study

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1/ U.S. Department of Treasury, "Additionality" in the Activities of the Export-Import Bank of the United States, by Dean A. DeRosa and William W. Nye, in U.S. Congress, House, Committee on Banking, Finance, and Urban Affairs, Subcommittee on International Trade, Investment and Monetary Policy, To Amend and Extend the Export-Import Bank Act of 1945, Hearings, 95th Congress, 2d session, March 13, 15, 16, and 17, 1978, Washington, U.S. Govt. Print. Off., 1978, pp. 54-71.

by the Congressional Research Service, using a different methodology, estimated that additional exports of only $670 million were generated by Eximbank's 1976 direct lending.[1/] The Carter Administration's decision to expand considerably official export credit assistance suggests that it accepted the more optimistic appraisals of the effectiveness of such programs. However, the Administration's program also includes a pledge to negotiate with major U.S. trade partners for stricter limits on official export credit assistance. The latter measure suggests a desire to limit the use of official export credits in the future.

Estimates of the benefits from tax incentives to U.S. exporters also vary. The 1976 Treasury Department DISC report estimated the net increase in exports attributable to DISC in 1974 at $4.9 billion,[2/] while a Congressional Research Service study of that year estimated a maximum net increase of only $1.4 billion.[3/] The most recent Treasury Department report estimates that DISC may have increased U.S. exports in 1976 by about $2.9 billion, and suggests that its estimate may

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1/ Gravelle, Jane, Impact of Eximbank on U.S. Exports, Congressional Research Service typed report, April 25, 1978.

2/ U.S. Department of the Treasury, The Operation and Effect of the Domestic International Sales Corporation Legislation: 1976 Annual Report, April 1978.

3/ Congressional Research Service, The Domestic International Sales Corporation and Its Effects on U.S. Foreign Trade and Unemployment, by Jane Gravelle, Kent Hughes and Warren E. Farb, Multilith 76-92 E, May 4, 1976.

overstate the effect of DISC.[1/] In contrast, a report commissioned by the Special Committee for U.S. Exports, an association of U.S. exporters, estimated that DISC generated $6.3 billion of additional exports in 1974.[2/] In the case of DISC, the Administration's export program appears to be based on the less optimistic appraisals. In his statement of September 26, 1978, President Carter maintained that DISC was an inefficient use of the taxpayers' money and recommended that it be either phased out or revised to a simpler, less costly form.

The President recommended retention of another tax incentive--tax relief for Americans employed abroad. Under his proposal, the total tax relief to U.S. citizens abroad would be approximately $250 million. Both of the tax measures in the President's program had been proposed before the export program was announced.

The President also announced a significant expansion of the export promotion programs of the Commerce, State, and Agriculture Departments. The Commerce and State budgets are to be increased by a total of $20 million, and certain agricultural export development programs are to be expanded. The proposed increases in the Commerce and State budgets focus squarely on what has been a major criticism

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1/ DISC 1976 Annual Report, op. cit., p. 10.

2/ Norman B. Ture, Inc., The Economic Effects of DISC, a study commissioned by the Special Committee for U.S. Exports, September 17, 1975.

of the program--that it helps large and experienced firms much more than small or medium-sized firms with little experience in exporting. The President emphasized that smaller firms were to be given high priority in spending the additional funds. Specifically, the President proposed three areas of assistance to exporters:

> a computerized information system to provide exporters with prompt access to international marketing opportunities abroad and to expose American products to foreign buyers;
>
> risk sharing programs to help associations and small companies meet initial export marketing costs; and
>
> targeted assistance to firms and industries with high export potential and intensified short-term export campaigns in promising markets.

In addition, the President announced that the Small Business Administration would channel up to $100 million of its current authorization for loan guarantees to small business exporters. The money would be used to assist small businesses in expanding production capacity and meeting cash flow problems involving overseas sales or initial marketing expenses.

The Government's export promotion program has long been criticized for its lack of attention to the needs of small, inexperienced businesses. Many critics maintain that the Government's programs are needed only by small businesses. Large exporters, they maintain, have sufficient resources to penetrate foreign markets and expand export sales without Government assistance. Yet, it is alleged, the latter have been the primary beneficiaries of Government assistance.

However, there is not unanimity among businessmen on this point. Some observers suggest that attempts to generate a major expansion of exports from small and medium-sized firms are futile. It is sometimes suggested that most of these firms are not suited for exporting directly, and that their role in international trade will continue to be confined primarily to subcontracting for the large corporations which have traditionally dominated U.S. exports.

Reduction of Domestic Barriers to Exports

Despite many complaints from businessmen about Government-imposed barriers to exports, it is unclear to what degree various Government programs have inhibited exports. There is no way to measure in precise quantitative terms either the reduction in exports which results from Federal regulations and policies or the improvement which might result from removing various barriers. Nevertheless, the Carter Administration's export expansion program is apparently based on the assumption that some improvement in U.S. export performance can result from an increased awareness on the part of Government administrators of the importance of exports. The President emphasized the need to administer Federal laws and policies "with greater sensitivity to the importance of exports." He announced that he was directing the head of all departments and agencies to take into account the possible adverse effects on exports of their administrative and regulatory activities.

The President also announced three specific approaches to solving the problem of Government-imposed disincentives to exporters:

> he directed the Departments of Commerce, State, Defense and Agriculture to take export consequences fully into account when considering the use of export controls for foreign policy purposes;
>
> he directed the Justice Department to give guidance to businessmen who were uncertain about the application of the Foreign Corrupt Practices Act or the antitrust laws; and
>
> he issued new guidelines on the applicability of the National Environmental Policy Act, which would require abbreviated environmental reviews only for exports of nuclear reactors, financing of exports which might create serious public health risks, and certain Federal actions which might have a significant adverse effect on the environment of foreign countries or on national resources of global importance.

The initial reaction to the Administration's program suggests that it will not please many observers. Some businessmen in the export community, while applauding the program as a first step, have noted that it does not address some important criticisms of U.S. Government policy. For example, frequent complaints about the allegedly poor management of the Commerce and State Department export promotion programs are not explicitly taken into account. Likewise, many of the Government programs identified by businessmen as barriers to exports are not addressed. Some observers suggest that much depends on how the program, particularly the President's directives on barriers to exports, will be administered.

The Administration's export promotion program also faces criticism from other perspectives. The Government programs identified

as barriers to exports are generally being carried out to pursue alternative social and economic goals. The success of the President's proposals will depend largely on how much weight export expansion is given vis-a-vis these alternative goals. Advocates of these Government programs will probably resist sacrificing them to the goal of increased exports. Many people believe that the alternative goals are more important than export expansion.

Moreover, some observers believe that there is no need for new Government incentives for exporters. They point to the recent improvement in the U.S. balance of trade as evidence that exchange rate fluctuations and expansion of the economies of major U.S. trade partners will provide sufficient U.S. export expansion.

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Mr. RUSSELL. Mr. Tozzoli?

Mr. TOZZOLI. I sent you a formal statement last week. With your permission, I would like to summarize.

Mr. RUSSELL. The chairman ordered all statements inserted in full in the record.

Please go ahead.

Mr. TOZZOLI. I am Guy Tozzoli, director of the World Trade Department and director of the World Trade Center in New York which was constructed and is being operated by the Port Authority of New York and New Jersey.

As many of you know, the port authority is a joint public and self-supporting agency of the States of New York and New Jersey. Its mission is to promote the port's commerce and trade and to plan, develop and operate transportation and terminal facilities authorized by the States within the bi-State port district.

The port authority operates a variety of facilities on both sides of the Hudson River, including marine terminals, a rail system, bus terminals, truck terminals, airports, bridges, and tunnels.

The port authority, of course, is also responsible for the World Trade Center, which is aimed at promoting the port's trade by providing modern centralized facilities for the many and complex administrative and marketing activities that are so essential to the growth of international business.

In addition to the development of physical facilities, the port authority promotes the commerce and trade of the port through a

three-part program of port promotion, trade development and port protection.

I hope that this brief introduction will help establish our credentials in this area and our deep interest in supporting new approaches to help increase the Nation's, and our port's, international business activities.

Today, you are holding a hearing on a topic of great importance to the international commercial development of the United States. If bill S. 1663 is passed, it could help develop some very powerful instruments for the expansion of U.S. exports.

In 1977, the port authority conducted a major study of the future needs of the region and recommended broad strategies to guide the port authority's policies during the next decade.

In its studies of industrial growth and job creation, it became clear that the port authority could greatly benefit the region by encouraging and assisting those manufacturers in the states of New York and New Jersey which are not now exporting but have the capability of being successful exporters.

A U.S. Department of Commerce study indicates that, for the United States as a whole, there are about 20,000 manufacturers which could export their products but are not doing so. On a pro rata basis—and this has been confirmed by a study we did—there should be 900 such firms in New Jersey and 1,500 in New York.

POSSIBLE $393 MILLION IN EXPORTS

If these 2,400 potential exporter firms were to export at the average U.S. rate for firms of their size, they could be exporting a total of $393 million of manufactured goods per year.

This would produce an estimated 22,000 new jobs and create considerable cargo movement through the Port of New York.

We feel that an excellent method to get firms involved in exporting is through the creation of a trading company along the lines of Japanese trading companies.

In the course of our study, we obtained the Hay Associates study which the U.S. Department of Commerce commissioned in 1976 to analyze why the export trading concept had not developed in the United States and what would need to be done to encourage the growth of such entities.

That report states that the export trading concept would be viable in the United States context if various conditions were met, including the possible necessity for a U.S. trading company to be a quasi-public institution.

On the other hand, the Hay report was skeptical about the concept in the United States because of lack of support by manufacturers, lack of management expertise, and need for government support.

We do not feel that these are fatal problems. For example, manufacturers must be interested when told that the trading company has offices in certain markets abroad and has developed a demand for his products.

Second, there are thousands of export managers and vice presidents of international divisions of U.S. firms who could make excellent managers of a trading company.

The only remaining potential problem is "need for government support," and that is the purpose of the bill and of these hearings.

Prior to the introduction of S. 1663, the port authority had come to the conclusion that Federal assistance should be made available to permit the port authority to conduct progams to encourage nonexporting manufacturers to export.

We now have a proposal to that effect pending with the Commerce Department. However, to support the growth of a trading company, there is a need for Federal grants or loans similar to those which could be made available pursuant to section 105 of your bill.

However, the uses to which such loans might be put would have to be revised.

At present, section 105(a) of the bill states: "Any such assistance shall be used only for expenses directly related to exports and export services * * *." But one of the major functions of a Japanese trading company is to provide financing to its client manufacturing firms.

This can be critical to a firm's capability to produce goods for export. There is little purpose in providing funds to increase exports if production cannot be increased.

Therefore, I urge that you consider amending the bill to permit such funds to be made available to client manufacturing firms to finance any activities needed to respond to export markets, provided that such firms are unable to obtain adequate funds from other available sources.

I should note that the staff of the port authority is continuing to investigate the possible formation of a port authority trading company, including a wholly owned subsidiary, a joint venture with one other organization, and a corporation with a number of shareholders, including banks, Edge Act subsidiaries of banks, bank-owned SBIC's, venture capitalists, and export management companies.

Although the U.S. Government could be criticized in certain circumstances if it loaned $25 million to a large manufacturing company to help it to create a trading company which benefitted primarily the parent company's own exports, section 102(c) on ownership requirements appears to be unduly restrictive.

For example, a public or quasi-public organization may wish to create a trading organization which would operate on a very low profit margin, with perhaps no other interested investors.

Although the 20 percent ownership maximum per investor means that there would need to be at least five investors, I believe that a minimum of three investors would provide sufficient protection from potential criticism and make the project far more feasible.

I suggest that section 102(c) be changed to read that no person may own more that 34 percent of the voting stock or interest in an export trading company, and that public and quasi-public organizations be exempted from this restriction.

FTC REGULATION ON REFUNDS

I would like to introduce one other point.

Japanese trading companies act as their own shipping brokers and can receive refunds from shipping companies in the United States, the FTC has a regulation which only permits independent brokers to receive such a refund.

This could be equivalent to 1.5 percent of the value of goods shipped and sometimes may be as much as half of the profit. Thus, EMC's in the United States may not receive such a refund.

The bill should be revised to permit trading companies to include the brokerage function and to be exempted from the FTC provision.

I will be writing more about this to you in a followup letter.

Thank you very much for allowing me to testify.

[Prepared statement of Mr. Tozzoli follows:]

Remarks of

Guy Tozzoli, Director of the World Trade Center in New York

Mr. Chairman, and distinguished members of this committee.

You are holding a hearing on a topic of great importance to the international commercial development of the United States, and I consider it a privilege to be able to participate in these deliberations. If bill S1663 is passed by the Congress, it could facilitate the development of some very powerful instruments for the expansion of U.S. exports.

In 1977, the Port Authority of New York and New Jersey created a Committee on the Future to examine the present state and probable future needs of the region which the Port Authority serves, and to recommend broad strategies to guide the Port Authority's policies during the next decade. The Committee sought to identify regional strengths, problems and needs and to assess possible points of intervention where the Port Authority's expertise and institutional structures specially qualify it to undertake regional leadership roles. Following an initial screening of regional problems, the Committee determined that it should most logically focus its attention in three areas -- economic development, transportation and energy. Study task forces were assembled in each of the areas from a cross-section of the Port Authority staff. These task forces conducted extensive surveys of concerned publics and held conferences with government officials and private interest groups to define the nature and magnitude of regional problems in each of the study areas.

One of the areas studied was that of industrial growth and job creation. It became clear that the Port Authority could greatly benefit the region by encouraging and assisting manufacturers, in the states of New York and New Jersey, which were not now exporting but which had products capable of being exported, to do so.

A U.S. Department of Commerce study indicates that, for the U.S. as a whole, there are about 18,000 manufacturers which could export their products but are not doing so. On a pro rata basis (the share of total U.S. exports now held by New York and New Jersey), there should be 900 such firms in New Jersey and 1500 in New York. A sample analysis undertaken by the Port Authority of 1000 manufacturing firms in New Jersey confirmed that these figures are very accurate. If these 2400 potential exporters firms were to export at the average U.S. rate for firms of their size, they could be exporting a total of $393 million of manufactured goods per year, which would produce an estimated 22,000 new jobs and create a cargo movement through the Port of New York.

One potential method to get firms involved in exporting was through the creation of a trading company which could develop markets for the products abroad, and purchase the goods from the manufacturer f.o.b. his factory, thereby relieving him of the problems of foreign marketing, the burdens and risks of export financing, and the complexity of export procedures. In many cases, this could require the manufacturer to expand production to meet the export demand and possibly to secure governmental assistance to finance his plant expansion or quality control or export packaging requirements. This would result in a relationship with the manufacturers which was similar to that which Japanese trading companies have with their client firms. Also to be effective, a system of foreign sales offices would have to be developed and staffed with a broad range of product specialists, similar to the more modest-sized Japanese trading companies.

In connection with our study, we obtained the Hay Associates study which the U.S. Department of Commerce commissioned in 1976 to analyze why

the export trading company concept had not developed in the U.S. and what would need to be done to encourage the growth of such entities. It is, we feel, in many respects an excellent study.

That report states that the export trading company concept would be viable in the U.S. context if the following conditions were met:

(a) It must have strong ties to manufacturers;

(b) It must have product specialist capabilities;

(c) It must have a strong foreign sales network under its control;

(d) It must have depth and continuity of management;

(e) It must be able to create substantial amounts of credit;

(f) It must have sufficient diversity of products and markets;

(g) It must be integrative in nature and capable of dealing in imports as well as exports;

(h) The incentive and capital must come from outside the manufacturing sector; and

(i) It may be necessary for a U.S. trading company to be a quasi-public institution.

On the other hand, the Hay report was skeptical about the feasibility of implementing the successful operation of the trading company concept in the U.S. for three reasons:

(a) lack of support by manufacturers

(b) lack of management expertise; and

(c) need for government support

We do not feel that all of these are fatal problems.

The first basis for skepticism was "lack of support by manufacturers." It is difficult to see this as a problem. There is no reason why a manufacturer who does not export and never heard of a Japanese trading company should get excited about the concept of an "Export Trading Company." We could reasonably expect manufacturers to become interested when told that the trading company has offices in certain markets abroad and has developed a demand for his products.

The second basis for skepticism is "lack of management expertise." Hay Associates does not substantiate this assertion. There are thousands of export managers and vice presidents of international divisions of U.S. firms who could make excellent managers of a trading company. Also, there are many owners or executives of export management companies who have the dynamism and expertise required for successful operation of a trading company. We do not see this as a real problem.

The only remaining potential problem was "need for government support," and that is the purpose of bill S1663 and of those hearings.

Prior to the introduction of S1663, the Port Authority had come to the conclusion that federal assistance should be made available to permit the Port Authority to carry out a detailed feasibility study and launch initial steps to encourage manufacturers not presently exporting their products to begin to export. We now have a proposal to that effect pending with the Commerce Department. However, to support the growth of a trading company there is a need for federal grants or loans similar to those which could be made available pursuant to Section 105 of S1663. However, the uses to which such loans might be put would have to be revised.

At present, Section 105 (a) of the bill states that: "Any such assistance shall be used only for expenses directly related to exports and export services..." But one of the major functions of a Japanese trading company is to provide financing to its client manufacturing firms and this can be critical to a firm's capability to provide the goods which the trading company wishes to export. There is little purpose in providing funds to a trading company to finance market research and development and increased staffing if production cannot be increased. Therefore, I urge that you consider amending the bill to permit such funds to be made available to client manufacturing firms to finance any activities needed to respond to the demands of production for export markets, provided that such firms are unable to obtain adequate funds from banks, from the Small Business Administration or from other available sources.

I should note that the staff of the Port Authority is continuing to investigate the possible formation of a Port Authority trading company, including a wholly-owned subsidiary, a joint venture with one other organization, and a corporation with a number of shareholders, including banks, Edge Act subsidiaries of banks, bank-owned SBIC's, venture capitalists, and export management companies.

In addition, inasmuch as the potential for bank participation in a trading company, either directly or via an Edge Act subsidiary, could be of critical importance, we are therefore delighted to see that S1663 would make this possible.

Finally, although the United States could be criticized in certain circumstances, if it loaned $25 million to a large manufacturing company to

help it to create a trading company which benefitted primarily the parent company's own exports, Section 102 (c) on Ownership Requirements appears to be unduly restrictive. For example, a public or quasi-public organization may wish to create a trading organization which would operate on a very low profit margin, as a result of which there may not be other interested investors. Also, the 20% ownership maximum per investor means that there would need to be at least 5 investors. I believe that a minimum of 3 investors would provide sufficient protection from potential criticism and make the project far more feasible. Thus, I suggest that Section 102 (c) be changed to read that no person may own more that 34% of the voting stock or interest in an export trading company, and that public and quasi-public organizations be exempted from this restriction.

Mr. Chairman, the Port Authority of New York and New Jersey feels that this is a very important bill. We will follow its progress through Congress with keen interest and hope to participate in its implementation. Thank you again, for giving me the opportunity to present these views.

Mr. RUSSELL. Thank you very much.

I wonder if I could presume on your gentlemen for a few moments. If you have planes to catch, please tell me so. Mr. Baker had a plane to catch. I have a few questions which could expedite consideration of these bills if answered now for the record.

First, I want to follow up with Mr. Doyle on the matter of the Webb-Pomerene associations. One of the continuing issues is whether there is a problem with the existing antitrust system.

The Justice Department and FTC consistently argue they received no evidence from business to substantiate the contention that antitrust serves as a barrier to exports, that any significant export activities are prohibited.

Can you provide evidence of export losses or examples of export activities which have been avoided due to antitrust concerns? If so, could you provide those for the record.

ANTITRUST LIABILITIES AND EXPOSURES

Mr. DOYLE. The principal loss has been the loss of export participation by businesses—efficiently operated and managed, producing a product that is desirable for sale domestically and abroad—the loss of participation by those companies in joint export activity, because of antitrust concern.

That is real. That is present. Companies who would otherwise participate in export activities have not joined in because of their concern and their counsel's concern that domestic antitrust liabilities and exposures are too great and the exemption afforded by the

Webb-Pomerene association is too tenuous and uncertain to make it worthwhile.

Mr. RUSSELL. You heard Mr. Ewing say the business review procedure was available. You heard the FTC representative indicate that they had something similar. Why isn't the business review procedure adequate if, as Justice and FTC claim, no one ever challenges their approval of an activity through this device?

Mr. DOYLE. The business review procedure offers shallow protection at best. Hollow protection, really.

In the first instance, I am familiar with a business review letter which the Department of Justice, Antitrust Division, only recently issued in this area which contained within it seven qualifiers.

I quoted from it specifically in my written testimony. Those qualifiers all deal with "reasonable" and "general" and is the typical and usual sort of approach in interpreting a statute as broadly written as the Sherman Act.

It does not address specific situations. It gives no guidance with respect to a specific problem or specific transaction, which the certification procedure would give.

Perhaps most compellingly, Senator Stevenson's observation that whatever the Department of Justice says has no binding effect on the private attorneys general who can wield the extortion and threat of treble damages alleged in class actions, which in this instance would relate to damages claimed to be attributable to the entire domestic sales of all the participating companies.

That threat would have to be borne throughout the lengthy course of antitrust litigation and the expensive and burdensome and diverting process of that litigation, before the Department's prediction about what a judge would charge and a jury would find could ever be vindicated.

It's that ex post facto validation which in essence makes the prediction of the Department of Justice so unhelpful in this area.

It is the prior certification and protection which the legislation before this subcommittee holds out as a promise which makes this legislation so vitally necessary.

Mr. RUSSELL. I want to be sure I understand this. I am sure this will be a subject of debate in this committee.

What you are suggesting is the reason the Justice Department has found no instance in which a private party challenged their business review findings is that no association has taken the chance of engaging in activities, even if covered by a business review letter, which might bring forth the kind of intimidating private action you cite.

Mr. DOYLE. That's correct, sir. It has always been my suspicion that the lack of, or relatively small number of Webb-Pomerene associations is accounted for by the fact that the Department of Justice and Federal Trade Commission have consistently had a hostile attitude toward the Webb-Pomerene exemption so, therefore, it offered no sure haven.

The reason there has been no challege is because companies who would have otherwise participated have not done so. So, therefore, the testimony that has been so consistent here today about the number of companies in this country who are not exporting I think is in large degree accounted for by the fact that they have not been

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able to do so jointly and they have not done so jointly because they are concerned about domestic antitrust constraints.

I have had that suspicion for a long time. I have recently seen in my practice in the formation of a Webb-Pomerene association, I have seen the evidence of that and a number of businesses who otherwise would have participated have not, simply because of domestic antitrust concerns.

Mr. RUSSELL. Mr. Frankel, Mr. Tozzoli, have you encountered instances in which activities that would have promoted exports have not been engaged in because of the antitrust statutes?

Mr. FRANKEL. It would not be the nature of our business to become involved with the antitrust statutes. There are, of course, recently enacted laws but these have nothing to do with Webb-Pomerene.

However, I do completely agree that the FTC and Justice Departments' attitudes would generally be considered as hostile to people who might otherwise consider forming Webb-Pomerene associations, and the clearcut elimination of that threat is certainly desirable.

Mr. TOZZOLI. I had no experience in this regard but we will now be conducting first-hand interviews with at least 1,000 or 1,500 companies and I will make it a point to try to find out from them what their experience is and I will communicate with you.

Mr. RUSSELL. It would be interesting to know whether there is a feeling that in the context of the trading company legislation, this type of antitrust provision is necessary, and if you have information on that, we would appreciate having it for the record.

20-PERCENT OWNERSHIP

Let me go back to the point that was made about the 20-percent ownership limitation. The committee will probably consider changes in that. Partnerships, small businesses might be exempted from that provision. It was intended to apply largely to the instance you cited, Mr. Tozzoli, large corporations exporting their own products. We want to really add to exports, not merely move them from one corporate form to another.

The point already indicated about foreign participation was well taken. That is something we will probably want to change.

And certainly the point about public agencies participating as shareholders or partners in such trading companies is one we will take into account.

So these points have all been most helpful. The report of the Hay Associates, by the way, was very helpful to us in working on this legislation. Yesterday Senator Stevenson mentioned it, and it was included in the record (see p. 413).

I wanted to ask you, Mr. Tozzoli, about the importance of startup cost assistance for exporters. You mentioned the large number of potential exporters and that you are going to survey them as to why they aren't doing more now.

One of the things we noted in the Hay Associates report is a need for the Government to take a hand in helping finance the startup costs. Having the banks participate is one element of that.

Public agencies that may be able to participate as shareholders might be another source of help.

We also involved the Small Business Administration, Eximbank and EDA. Do you consider helping to finance startup costs an essential part of the proposal or just a marginal feature?

Mr. TOZZOLI. No, sir. I consider it a very essential part.

LIAISON WITH SMALL BUSINESS FIRMS

Our studies in the work we have done in the last 3 years, indicate that that probably is the most difficult part to get going, and there is one other segment of U.S. industry that hasn't been mentioned today that could benefit very strongly. Those are those small businesses which are impacted by imports. Small businesses impacted by imports could very well benefit from the creation of trading corporations. We are going to try to identify in the New York-New Jersey area those small firms who have been hurt by imports and see if we can help them. That is why I brought up the financing end also. See if we can help them restructure themselves, so we can create more jobs and put them back in the stream of the economy.

Mr. RUSSELL. Good point. Senator Stevenson is fond of saying the companies that don't learn to compete in the international markets pretty soon find they can't compete in the domestic markets either, because of foreign competition. There isn't any such thing as a strictly domestic market anymore.

Mr. Frankel, we are maintaining liaison with the White House Small Business Conference and keep in touch with them as they prepare these proposals. We appreciate your references to that. I take it some of the tax proposals are also being considered in that forum.

Mr. FRANKEL. Yes, they are and I checked yesterday. The proposals should be complete, certainly published within the next 2 weeks.

If I might just interject one other item, I have in front of me a publication from the Federal Register on Friday, August 9, 1968, which was entitled, "Joint Export Associations." At that time there was a passage of what, Mr. Tozzoli, might be considered seed money. I believe there were 10 such recipients for the formation of what was called joint trade associations. It only lasted for a brief time during 1968, but in our recommendations for the conference for small business we make specific reference to these joint export associations.

Mr. RUSSELL. Thank you, Mr. Frankel. I wanted to call your attention to the problem we have in the area of expanding DISC or improving DISC. That is, we are told by the Treasury Department that in their opinion any expansion of DISC would violate the subsidies code.

In other words, they seem to be taking a position that what they grandfathered wasn't just a DISC, but DISC with its incremental feature and very cumbersome procedures and all the other rules and regulations, and any liberalization would be looked upon unfavorably.

I hope that won't be their final position on it or the final U.S. position, but at the moment it is a major concern.

Mr. FRANKEL. My comment on that, I spoke both to Mr. McDonald and Mr. Strauss on separate occasions precisely as to how they grandfathered the DISC legislation, and it's my understanding that we tied in the DISC legislation with legislation which currently exists in both France and in Belgium, which are referenced in today's introduced testimony by Arthur Andersen Co., where they give details in one of their appendixes. This appendix points out that in France, export trade is exempt—profits derived from export trade is exempt from domestic French taxes.

It also points out that domestic export trade in Belgium is approximately 75 percent exempt from domestic Belgium taxes. It was my understanding in conversations with Mr. Strauss and Mr. McDonald that we tied in not specifically our entire DISC encompassing all the revisions of 1976, but that we tied it indirectly to a solution of these two examples in regards to France and Belgium and their subsidiaries.

Mr. RUSSELL. Thank you for that comment. The tax provisions are under discussion. There will be further thought to those. I did want to reemphasize Senator Stevenson's point that S. 1663 is not an alternative to DISC. It is not proposed as a general legislative alternative to DISC. Trading companies established under this legislation could elect DISC or more favorable tax treatment to be established under this legislation. There are some problems we will need to work out, and we would like your views and help on those, as we go along.

FINANCING PRODUCTION FOR EXPORTS

I had one more question for Mr. Tozzoli. You referred to financing production for exports. This raises a different area. It's not one that is covered by the bill. It generates some unique political problems. The argument about financing production for export that brings us into the situation of seeming to finance for export what we wouldn't finance for domestic consumption.

How would you take care of that concern?

Mr. TOZZOLI. We are trying to approach it this way: in our own case, we intended to concentrate on those corporations who are presently not exporting. As far as we are concerned, if, as a trading company, a quasi-public organization, we are able to establish a new market where none existed before—in other words, where the company could prove it was increasing its production facilities strictly for overseas sale—then we hoped on that basis—I think that could be a good way to do it—in other words, to demonstrate that it is for production that is not presently consumed in the United States, that could be one.

No. 2, because of the urging of Commerce—I think rightly so—we are moving that somewhat in the business of the impacted industry.

Mr. RUSSELL. The Economic Development Administration would be part of your plan?

Mr. TOZZOLI. Yes. Right now we have before them a proposal in which we will identify the specific companies, and we will try to

find out what are their needs. Maybe there is no need for expansion of production facilities. I am inclined to believe in the impacted industries they must——

Mr. RUSSELL. That is very helpful. Let me throw out one final thought as an alternative to the 20 percent ownership restriction. A suggestion made to us was to permit corporations that are not small businesses, and have very large export sales already, to participate in trading companies, but not for the export of their own products. They would use the trading company as a way to get double duty out of their existing exporting network and marketing system. I won't ask you to respond to that today, but perhaps in a letter you might explore that idea.

The idea is that you could have as much as 100 percent ownership. It was suggested to us the big corporations already involved in exporting can take an initiative here to help export the products of other companies. They really don't need the benefits for their own exports, but it could encourage them to set up a subsidiary, a trading company, to export other people's products.

Well, Senator Stevenson will probably write to you with additional questions for the record. We appreciate any comments you care to add in writing for the record and would like your responses, if possible, within the next 2 weeks.

Thank you. I am sorry the Senator is delayed, but we had better adjourn the hearing. It's getting late.

[Whereupon, at 5:30 p.m., the hearing was adjourned.]

[Additional material received for the record follows in the appendix:]

APPENDIX

96TH CONGRESS
1ST SESSION

S. 864

To establish within the Department of Commerce an office to promote and encourage the formation and utilization of export trade associations, and for other purposes.

IN THE SENATE OF THE UNITED STATES

APRIL 4 (legislative day, FEBRUARY 22), 1979

Mr. DANFORTH (for himself, Mr. BENTSEN, Mr. CHAFEE, Mr. JAVITS, and Mr. MATHIAS) introduced the following bill; which was read twice and referred to the Committee on Banking, Housing, and Urban Affairs

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A BILL

To establish within the Department of Commerce an office to promote and encourage the formation and utilization of export trade associations, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the "Export Trade Associ-
5 ation Act of 1979".

6 **SEC. 2. FINDINGS; DECLARATION OF PURPOSE.**

7 (a) FINDINGS.—The Congress finds and declares that—

II—E

1 (1) in 1978 the United States suffered the largest
2 trade deficit in its history, amounting to approximately
3 $30,000,000,000;
4 (2) the trade deficit has contributed to the decline
5 of the dollar on international currency markets and has
6 led to widespread public concern about the strength of
7 the dollar;
8 (3) the exports of the American economy are re-
9 sponsible for creating and maintaining one out of every
10 nine manufacturing jobs in the United States and for
11 generating one out of every seven dollars of total
12 United States goods produced;
13 (4) foreign-government-owned and foreign-govern-
14 ment-subsidized entities compete directly with private
15 United States exporters for shares of the world market;
16 (5) between 1968 and 1977 the United States
17 share of total world exports fell from 19 percent to 13
18 percent;
19 (6) service-related industries are vital to the well-
20 being of the American economy inasmuch as they
21 create jobs for seven out of every ten Americans, pro-
22 vide 65 percent of the Nation's gross national product,
23 and represent a small but rapidly rising percentage of
24 United States international trade;

1 (7) small and medium-sized firms are prime bene-
2 ficiaries of joint exporting, through pooling of technical
3 expertise, help in achieving economies of scale, and as-
4 sistance in competing effectively in foreign markets;
5 and
6 (8) the Department of Commerce has as one of its
7 responsibilities the development and promotion of
8 United States exports.
9 (b) PURPOSE.—It is the purpose of this Act to encour-
10 age American exports by establishing an office within the
11 Department of Commerce to encourage and promote the for-
12 mation of export trade associations through the Webb-
13 Pomerene Act, by making the provisions of that Act explicit-
14 ly applicable to the exportation of services, and by transfer-
15 ring the responsibility for administering that Act from the
16 Chairman of the Federal Trade Commission to the Secretary
17 of Commerce.
18 SEC. 3. DEFINITIONS.
19 The Webb-Pomerene Act (15 U.S.C. 61–66) is amend-
20 ed by striking out the first section and inserting in lieu there-
21 of the following:
22 "SECTION 1. DEFINITIONS.
23 "As used in this Act—
24 "(1) EXPORT TRADE.—The term 'export trade'
25 means trade or commerce in goods, wares, merchan-

1 dise, or services exported, or in the course of being ex-
2 ported from the United States or any territory thereof
3 to any foreign nation.
4 "(2) SERVICE.—The term 'service' means intangi-
5 ble economic output, including, but not limited to—
6 "(A) business, repair, and amusement serv-
7 ices;
8 "(B) management, legal, engineering, archi-
9 tectural, and other professional services; and
10 "(C) financial, insurance, transportation, and
11 communication services.
12 "(3) EXPORT TRADE ACTIVITIES.—The term
13 'export trade activities' includes any activities or
14 agreements which are incidental to export trade.
15 "(4) TRADE WITHIN THE UNITED STATES.—The
16 term 'trade within the United States' means trade be-
17 tween or among—
18 "(A) the several States of the United States,
19 "(B) the territories of the United States, or
20 "(C) the District of Columbia and the several
21 States or Territories of the United States.
22 "(5) ASSOCIATION.—The term 'association'
23 means any combination, by contract or other arrange-
24 ment, of persons who are citizens of the United States,
25 partnerships which are created under and exist pursu-

1 ant to the laws of any State or of the United States, or
2 corporations which are created under and exist pursu-
3 ant to the laws of any State or of the United States.
4 The term 'association' does not include a combination
5 of any of the above with a subsidiary located in the
6 United States which is controlled by a foreign entity.
7 "(6) ANTITRUST LAWS.—The term 'antitrust
8 laws' means the antitrust laws defined in the first sec-
9 tion of the Clayton Act (15 U.S.C. 12) and section 4
10 of the Federal Trade Commission Act (15 U.S.C. 44),
11 any other law of the United States in pari materia with
12 those laws, and any State antitrust or unfair competi-
13 tion law.
14 "(7) SECRETARY.—The term 'Secretary' means
15 the Secretary of Commerce.
16 "(8) ATTORNEY GENERAL.—The term 'Attorney
17 General' means the Attorney General of the United
18 States.
19 "(9) CHAIRMAN.—The term 'Chairman' means
20 the Chairman of the Federal Trade Commission.".
21 SEC. 4. ANTITRUST EXEMPTION.
22 Section 2 of the Webb-Pomerene Act (15 U.S.C. 62) is
23 amended to read as follows:

1 "SEC. 2. EXEMPTION FROM ANTITRUST LAWS.

2 "(a) GENERAL RULE.—Any association certified ac-
3 cording to the procedures set forth in this Act, entered into
4 for the sole purpose of engaging in export trade, and engaged
5 in such export trade, is exempt from the application of the
6 antitrust laws if the association and the export trade activi-
7 ties in which it and its members are engaged or propose to be
8 engaged—

9 "(1) serve to preserve or promote export trade;

10 "(2) result in neither a substantial restraint of
11 competition within the United States nor a substantial
12 restraint of the export trade of any domestic competitor
13 of such association;

14 "(3) do not unreasonably enhance, stabilize, or de-
15 press prices within the United States of the goods,
16 wares, merchandise, or services of the class exported
17 by such association;

18 "(4) do not constitute unfair methods of competi-
19 tion against domestic competitors engaged in the
20 export trade of goods, wares, merchandise, or services
21 of the class exported by such association;

22 "(5) do not include any act which results, or may
23 reasonably be expected to result, in the sale for con-
24 sumption or resale within the United States of the
25 goods, wares, merchandise, or services exported by the
26 association or its members.

1 "(6) do not constitute trade or commerce in the
2 licensing of patents, technology, trademarks, or know-
3 how, except as incidental to the sale of the goods,
4 wares, merchandise, or services exported by the associ-
5 ation or its members.
6 "(b) ENFORCEMENT BY FEDERAL AGENCIES ONLY.—
7 "(1) STANDING.—No person other than a depart-
8 ment or agency of the United States, or an officer of
9 the United States acting in his official capacity, shall
10 have standing to bring an action against an association
11 for failure to meet the requirements of subsection (a).
12 "(2) PETITIONS BY THIRD PARTIES.—Whenever
13 any person has reason to believe that an association
14 fails to meet any requirement of subsection (a), he may
15 file a petition, alleging such failure and requesting the
16 commencement of appropriate enforcement action, with
17 the Secretary. Unless the Secretary, in consultation
18 with the Attorney General and Chairman, determines
19 that the petition does not make allegations upon which,
20 if true, an enforcement action could be based, he shall
21 conduct an adjudicatory proceeding in accordance with
22 the provisions of section 554 of title 5, United States
23 Code, for the purpose of determining the truth of the
24 matters alleged. If he determines that the allegations
25 contained in the petition are true, and that they indi-

1 cate that the association does not meet a requirement
2 of subsection (a), then he shall bring an action against
3 the association under paragraph (3).
4 "(3) REMEDIES.—Such a department, agency, or
5 officer acting in his official capacity may bring an
6 action for the revocation, in whole or in part, of an as-
7 sociation's certification on the ground that it fails, or
8 has failed, to meet a requirement of subsection (a), or
9 to enjoin or restrain an association from engaging in
10 any activity which fails to meet any condition set forth
11 in paragraphs (1) through (6) of subsection (a).
12 "(4) JURISDICTION.—Any action brought under
13 subsection (b) shall be considered as an action de-
14 scribed in section 1337 of title 28, United States
15 Code.".
16 SEC. 5. AMENDMENT OF SECTIONS 3 AND 4.
17 (a) CONFORMING CHANGES IN STYLE.—The Webb-
18 Pomerene Act is amended—
19 (1) by inserting immediately before section 3 (15
20 U.S.C. 63) the following:
21 "SEC. 3. OWNERSHIP INTEREST IN OTHER TRADE ASSOCI-
22 ATIONS PERMITTED.",
23 (2) by striking out "SEC. 3. That nothing" in sec-
24 tion 3 and inserting in lieu thereof "Nothing",

1 (3) by inserting immediately before section 4 the
2 following:
3 "SEC. 4. UNFAIR METHODS OF COMPETITION AGAINST DO-
4 MESTIC COMPETITORS PROHIBITED.",
5 and
6 (4) by striking out "SEC. 4. That the" in section
7 4 and inserting in lieu thereof "The".
8 (b) LIMITATION OF UNFAIR COMPETITION PROHIBI-
9 TION TO DOMESTIC COMPETITORS.—Section 4 of the Act
10 (15 U.S.C. 64) is amended by inserting "domestic" before
11 "competitors".
12 SEC. 6. ADMINISTRATION; ENFORCEMENT; REPORTS.
13 (a) IN GENERAL.—The Webb-Pomerene Act is amend-
14 ed by striking out section 5 and inserting in lieu thereof the
15 following sections:
16 "SEC. 5. CERTIFICATION.
17 "(a) APPLICATION.—In order to obtain certification as
18 an association engaged solely in export trade, a person shall
19 file with the Secretary a written notice of intent to meet for
20 the purpose of determining the desirability of applying for
21 certification and, within 60 days after such meeting, unless
22 such person has filed with the Secretary a written notice or
23 decision not to apply for certification, a written application
24 for certification setting forth the following:
25 "(1) The name of the association.

1 "(2) The location of all of the association's offices
2 or places of business in the United States and abroad.
3 "(3) The names and addresses of all of the associ-
4 ation's officers, stockholders, and members.
5 "(4) A copy of the certificate or articles of incor-
6 poration and bylaws, if the association is a corporation;
7 or a copy of the articles or contract of association, if
8 the association is unincorporated.
9 "(5) A description of the goods, wares, merchan-
10 dise, or services which the association or its members
11 export or propose to export.
12 "(6) An explanation of the domestic and interna-
13 tional conditions, circumstances, and factors which
14 make the association useful for the purpose of promot-
15 ing the export trade of the described goods, wares,
16 merchandise, or services.
17 "(7) The methods by which the association con-
18 ducts or proposes to conduct export trade in the de-
19 scribed goods, wares, merchandise, or services, includ-
20 ing, but not limited to, any agreements to sell exclu-
21 sively to or through the association, any agreements
22 with foreign persons who may act as joint selling
23 agents, any agreements to acquire a foreign selling
24 agent, any agreements for pooling tangible or intangi-
25 ble property or resources, or any territorial, price-

1 maintenance, membership, or other restrictions to be
2 imposed upon members of the association.
3 "(8) The names of all countries where export
4 trade in the described goods, wares, merchandise, or
5 services is conducted or proposed to be conducted by
6 or through the association.
7 "(9) Any other information which the Secretary
8 may request concerning the organization, operation,
9 management, or finances of the association; the rela-
10 tion of the association to other associations, corpora-
11 tions, partnerships, and individuals; and competition or
12 potential competition, and effects of the association
13 thereon. The Secretary may not request information
14 under this paragraph which is not reasonably available
15 to the person making application or which is not neces-
16 sary for certification of the prospective association.
17 "(b) ISSUANCE OF CERTIFICATE.—
18 "(1) NINETY-DAY PERIOD.—Based upon the in-
19 formation obtained from the application, the Secretary
20 shall certify an association within 90 days after receiv-
21 ing the association's application for certification if the
22 Secretary determines that the association and its mem-
23 bers and the proposed export trade activities meet the
24 requirements of section 2 of this Act.

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1 "(2) EXPEDITED CERTIFICATION.—In those in-
2 stances where the temporary nature of the export trade
3 activities, deadlines for bidding on contracts or filling
4 orders, or any other circumstances beyond the control
5 of the association which have a significant impact on
6 the association's export trade, make the 90-day period
7 for application approval described in paragraph (1) of
8 this subsection impractical for the person seeking certi-
9 fication as an association, such person may request and
10 may receive expedited action on his application for cer-
11 tification.
12 "(3) APPEAL OF INITIAL DETERMINATION.—If
13 the Secretary determines not to certify an association
14 which has submitted an application for certification,
15 then he shall—
16 "(A) notify the association of his determina-
17 tion and the reasons for his determination, and
18 "(B) upon request made by the association,
19 afford the association an opportunity for a hearing
20 with respect to that determination in accordance
21 with section 557 of title 5, United States Code.
22 "(c) MATERIAL CHANGES IN CIRCUMSTANCES;
23 AMENDMENT OF APPLICATION.—
24 "(1) VOIDING OF CERTIFICATION.—Whenever
25 there is a material change in—

1 "(A) the domestic and international condi-
2 tions, circumstances, and factors which make an
3 association useful for the purpose of promoting the
4 export trade of its goods, wares, merchandise, or
5 services, or
6 "(B) the association's membership, export
7 trade, export trade activities, or methods of oper-
8 ation which would cause the association to fail to
9 meet any requirement of section 2,
10 then the association shall apply to the Secretary for an
11 amendment of its certification. If an association fails to
12 apply for an amendment of its certification when re-
13 quired by the preceding sentence, then the certification
14 of the association shall be void as of the date of such
15 material change (as determined by the Secretary).
16 "(2) AMENDMENT OF APPLICATION.—The re-
17 quest for amendment shall be filed within 30 days after
18 the date of the material change and shall set forth the
19 requested amendment of the application and the rea-
20 sons for the requested amendment. Any request for the
21 amendment of an application shall be treated in the
22 same manner as an original application for certifica-
23 tion. If the request is filed within 30 days after the
24 material change which requires the amendment, and if
25 the requested amendment is approved, then there shall

1 be no interruption in the period for which certification
2 is in effect.
3 "(3) AMENDMENT UPON RECOMMENDATION OF
4 SECRETARY.—After notifying the association involved,
5 the Secretary may, on his own initiative, or upon the
6 recommendation of the Attorney General, the Chair-
7 man, or any other person—
8 "(A) require that an association's certifica-
9 tion be amended,
10 "(B) require that the organization or oper-
11 ation of the association be modified to correspond
12 with the association's certification, or
13 "(C) revoke, in whole or in part, the certifi-
14 cation of the association upon a finding (made in
15 an adjudicatory proceeding held in accordance
16 with section 554 of title 5, United States Code)
17 that the association, its members, or its export
18 trade activities do not meet the requirements of
19 section 2 of this Act.
20 "SEC. 6. GUIDELINES.
21 "(a) INITIAL PROPOSED GUIDELINES.—Within 90
22 days after the enactment of the Export Trade Association
23 Act of 1979, the Secretary, the Attorney General, and the
24 Chairman shall publish proposed guidelines for purposes of
25 determining whether an association, its members, and its

1 export trade activities will meet the requirements of section 2
2 of this Act.

3 "(b) PUBLIC COMMENT PERIOD.—Following publica-
4 tion of the proposed guidelines, and any proposed revision of
5 guidelines, interested parties shall have 30 days to comment
6 on the proposed guidelines. The Secretary, the Attorney
7 General, and the Chairman shall review the comments and
8 publish final guidelines within 30 days after the last day on
9 which comments may be made under the preceding sentence.

10 "(c) PERIODIC REVISION.—After publication of the
11 final guidelines, the Secretary, the Attorney General, and the
12 Chairman shall meet periodically to revise the guidelines as
13 needed.

14 "(d) APPLICATION OF ADMINISTRATIVE PROCEDURE
15 ACT.—The promulgation of guidelines under this section
16 shall not be considered rule-making for purposes of sub-
17 chapter II of chapter 5 of title 5, United States Code, and
18 section 553 of such title shall not apply to their promulga-
19 tion.

20 "SEC. 7. ANNUAL REPORTS.

21 "Every certified association shall submit to the Secre-
22 tary an annual report, in such form and at such time as he
23 may require, setting forth the information described by sec-
24 tion 5(a) of this Act.

1 "SEC. 8. OFFICE OF EXPORT TRADE IN COMMERCE DEPART-
2 MENT.
3 "The Secretary shall establish within the Department of
4 Commerce an office to promote and encourage to the great-
5 est extent feasible the formation of export trade associations
6 through the use of provisions of this Act in a manner consist-
7 ent with this Act.
8 "SEC. 9. AUTOMATIC CERTIFICATION FOR EXISTING ASSOCI-
9 ATIONS.
10 "The Secretary shall certify any export trade associ-
11 ation registered with the Federal Trade Commission as of the
12 date of enactment of the Export Trade Association Act of
13 1979 if such association, within 180 days after the date of
14 enactment of such Act, files with the Secretary an applica-
15 tion for certification as provided for in section 5 of this Act,
16 unless such application shows on its face that the association
17 is not eligible for certification under this Act.
18 "SEC. 10. CONFIDENTIALITY OF APPLICATION AND ANNUAL
19 REPORT INFORMATION.
20 "(a) GENERAL RULE.—Applications made under sec-
21 tion 5, including amendments to such applications, and
22 annual reports made under section 7 shall be confidential,
23 and, except as authorized by this section, no officer or em-
24 ployee, or former officer or employee, of the United States
25 shall disclose any such application, amendment, or annual
26 report, or any application, amendment or annual report infor-

1 mation, obtained by him in any manner in connection with his
2 service as such an officer or employee.
3 "(b) DISCLOSURE TO FEDERAL OFFICERS OR EM-
4 PLOYEES FOR ADMINISTRATION OF OTHER FEDERAL
5 LAWS.—
6 "(1) INVESTIGATION.—The Secretary shall make
7 an application, amendment, or annual report, or infor-
8 mation derived therefrom available, to the extent re-
9 quired by an ex parte order issued by a judge of a
10 United States district court, to officers and employees
11 of a Federal agency personally and directly engaged in,
12 and solely for their use in, preparation for an adminis-
13 trative or judicial proceeding (or investigation which
14 may result in such a proceeding) to which the United
15 States or such agency is or may be a party.
16 "(2) APPLICATION FOR ORDER.—The head of
17 any Federal agency described in paragraph (1), or, in
18 the case of the Department of Justice, the Attorney
19 General, the Deputy Attorney General, or an Assistant
20 Attorney General, may authorize an application to a
21 United States district court judge for the order referred
22 to in paragraph (1). Upon application, the judge may
23 grant the order if he determines, on the basis of the
24 facts submitted by the applicant, that—
25 "(A) in the case of a criminal investigation—

1 "(i) there is reasonable cause to believe,
2 based upon information believed to be reli-
3 able, that a specific criminal act has been
4 committed,
5 "(ii) there is reason to believe that such
6 application, amendment, annual report, or in-
7 formation derived therefrom is probative evi-
8 dence of a matter in issue related to the
9 commission of such Act, and
10 "(iii) the information sought cannot rea-
11 sonably be obtained from any other source,
12 unless it is determined that, notwithstanding
13 the reasonable availability of the information
14 from another source, the application, amend-
15 ment or annual report, or information derived
16 therefrom sought constitutes the most proba-
17 tive evidence of a matter in issue relating to
18 the commission of such criminal act, and
19 "(B) in the case of any other investigation,
20 that—
21 "(i) such application, amendment or
22 annual report, or information derived there-
23 from is probative evidence of a matter under
24 investigation,

1 "(ii) such application, amendment or
2 annual report, or information derived there-
3 from is or may be material to the administra-
4 tive or judicial proceeding in connection with
5 which the investigation is being conducted,
6 and
7 "(iii) the information sought cannot rea-
8 sonably be obtained from any other source,
9 or, notwithstanding the reasonable availabil-
10 ity of the information from another source,
11 the application, amendment or annual report,
12 or information derived therefrom sought con-
13 stitutes the most probative evidence of a
14 matter in issue relating to the commission of
15 the act being investigated.

16 "SEC. 11. MODIFICATION OF ASSOCIATION TO COMPLY WITH
17 UNITED STATES OBLIGATIONS.

18 "At such time as the United States undertakes interna-
19 tional obligations by treaty or statute, to the extent that the
20 operations of any export trade association, certified under
21 this Act or registered under this Act, before its amendment
22 by the Export Trade Association Act of 1979, are inconsist-
23 ent with such international obligations, the Secretary may
24 require such association to modify its operations so as to be
25 consistent with such international obligations.

1 "SEC. 12. REGULATIONS.

2 "The Secretary, in consultation with the Attorney Gen-
3 eral and the Chairman, shall promulgate such rules and regu-
4 lations as may be necessary to carry out the purposes of this
5 Act.

6 "SEC. 13. TASK FORCE STUDY.

7 "Seven years after the date of enactment of the Export
8 Trade Association Act of 1979, the President shall appoint,
9 by and with the advice and consent of the Senate, a task
10 force to examine the effect of the operation of this Act on
11 domestic competition and on the United States' international
12 trade deficit and to recommend either continuation, revision,
13 or termination of the Webb-Pomerene Act. The task force
14 shall have one year to conduct its study and to make its
15 recommendations to the President.".

16 (b) REDESIGNATION OF SECTION 6.—The Act is
17 amended—

18 (1) by striking out "SEC. 6." in section 6 (15
19 U.S.C. 66), and

20 (2) by inserting immediately before such section
21 the following:

22 "SEC. 14. SHORT TITLE.".

96TH CONGRESS
1ST SESSION

S. 1499

To promote and encourage the formation and utilization of export trade associations, and for other purposes.

IN THE SENATE OF THE UNITED STATES

JULY 12 (legislative day, JUNE 21), 1979

Mr. ROTH introduced the following bill; which was read twice and referred to the Committee on Banking, Housing, and Urban Affairs

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A BILL

To promote and encourage the formation and utilization of export trade associations, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the "Export Trade Activities
5 Act".

6 **SEC. 2. FINDINGS; DECLARATION OF PURPOSE.**

7 (a) FINDINGS.—The Congress finds and declares that—

1 (1) exports account for one out of every six jobs
2 in the manufacturing sector and 8 percent of the gross
3 national product of the United States;
4 (2) every billion dollars in new exports is estimat-
5 ed to provide 40,000 jobs, $2,000,000,000 in national
6 income, and $400,000,000 in Government revenue;
7 (3) there is increasingly fierce competition to
8 American goods and services in international markets;
9 (4) the ability to pool resources and expertise
10 would help equalize the bargaining position of Ameri-
11 can businesses in international transactions, particular-
12 ly of small- and medium-sized businesses; and
13 (5) the existing legislation involving export trade
14 associations is outdated and needs to be changed to
15 make export trade associations more useful.
16 (b) PURPOSE.—It is the purpose of this Act to encour-
17 age and promote the formation of export trade associations,
18 and to enable businesses to share the costs of export trade.
19 The Federal Trade Commission shall consider and process
20 applications submitted under section 6 as expeditiously as
21 possible. The Secretary of Commerce shall take appropriate
22 measures to encourage the establishment and use of such as-
23 sociations.
24 **SEC. 3. DEFINITIONS.**
25 As used in this Act—

1 (1) EXPORT TRADE.—The term "export trade"
2 means trade or commerce in goods, wares, merchan-
3 dise, or services exported, or in the course of being ex-
4 ported, from the United States to any foreign nation,
5 but does not include—
6 (A) trade or commerce in any such goods,
7 products, or merchandise subsequently imported
8 into the United States for sale for consumption or
9 resale, without regard to whether they are im-
10 ported in the same condition as when they were
11 exported from the United States or in a changed
12 condition by reason of remanufacture or other-
13 wise, or
14 (B) trade or commerce in patents, licenses,
15 trade secrets, or technology (except to the extent
16 that technology is incidental to the sale of such
17 goods, products, merchandise, or services).
18 (2) EXPORT TRADE ACTIVITIES.—The term
19 "export trade activities" includes any activities or
20 agreements which are incidental to export trade.
21 (3) UNITED STATES.—The term "United States"
22 means the several States of the United States, the Dis-
23 trict of Columbia, the Commonwealth of Puerto Rico,
24 the Virgin Islands, American Samoa, Guam, and the
25 Trust Territory of the Pacific Islands.

1 (4) ASSOCIATION.—The term "association"
2 means any combination, by contract or other arrange-
3 ment, of persons who are citizens of the United States,
4 partnerships which are created under and exist pursu-
5 ant to the laws of any State or of the United States, or
6 corporations which are created under and exist pursu-
7 ant to the laws of any State or of the United States.
8 (5) ANTITRUST LAWS.—The term "antitrust
9 laws" means the antitrust laws defined in the first sec-
10 tion of the Clayton Act (15 U.S.C. 12) and section 4
11 of the Federal Trade Commission Act (15 U.S.C. 44),
12 any other law of the United States in pari materia with
13 those laws, and any State antitrust or unfair competi-
14 tion law.
15 (6) COMMISSION.—The term "Commission"
16 means the Federal Trade Commission.
17 (7) CHAIRMAN.—The term "Chairman" means
18 the Chairman of the Federal Trade Commission.
19 (8) ATTORNEY GENERAL.—The term "Attorney
20 General" means the Attorney General of the United
21 States.
22 **SEC. 4. ANTITRUST EXEMPTION.**
23 An association certified under section 6 of this Act, en-
24 tered into for the sole purpose of engaging in export trade,
25 and engaged in export trade activities, and its members, are

1 exempt from the application of the antitrust laws except to
2 the extent that the existence of the association, or the activi-
3 ties in which it and its members are engaged, result in—
4 (1) restraint of trade within the United States,
5 (2) a substantial decrease in competition within
6 the United States, or
7 (3) a substantial restraint of the export trade of
8 any domestic competitor.
9 **SEC. 5. ENFORCEMENT.**
10 (a) EXCLUSIVE JURISDICTION OF COMMISSION.—The
11 Commission shall have exclusive jurisdiction to determine
12 whether an association certified under section 6—
13 (1) has failed to comply with the terms and condi-
14 tions of its certification, or
15 (2) has taken any action which is inconsistent
16 with the requirements of section 4.
17 (b) DETERMINATIONS.—The Commission shall make a
18 determination under subsection (a) after an investigation
19 commenced after receipt of a complaint, filed with it at such
20 time and in such manner as it may require, or upon its own
21 motion, and after notice to the association and an opportunity
22 for a hearing on the record.
23 (c) REMEDIES.—If the determination of the Commission
24 under subsection (a) is affirmative, then it may—

1 (1) in the case of an affirmative determination
2 under subsection (a)(1)—
3 (A) require the association to file an amended
4 application for certification under section 6(c),
5 (B) require the association to modify its orga-
6 nization or operations,
7 (C) revoke, in whole or in part, the certifica-
8 tion of the association, or
9 (D) refer the matter to the Attorney General
10 for prosecution under the antitrust laws, or
11 (2) in the case of an affirmative determination
12 under subsection (a)(2)—
13 (A) require the association to modify its or-
14 ganization or operations, or
15 (B) revoke, in whole or in part, the certifica-
16 tion of the association.
17 (d) CIVIL ACTIONS BY INJURED PARTIES.—
18 (1) STANDING REQUIREMENT.—No person shall
19 have standing to bring an action against an association
20 certified under section 6 for injuries arising out of the
21 export trade activities of that association unless—
22 (A) the Commission has made an affirmative
23 determination under subsection (a) with respect to
24 the activities of the association to which the
25 action relates, and

1 (B) those activities have, as a purpose or as
2 a primary effect, a result described in section 4.
3 (2) LIMITATION ON DAMAGES.—Notwithstanding
4 any other provision of law to the contrary, damages in
5 excess of the amount necessary to compensate the in-
6 jured party for losses suffered may not be awarded in
7 any action brought against an association certified
8 under section 6 for injuries arising out of its export
9 trade activities.

10 **SEC. 6. CERTIFICATION.**

11 (a) APPLICATION.—In order to become certified as an
12 association engaged solely in export trade, a person shall file
13 with the Federal Trade Commission a written application for
14 certification setting forth the following:

15 (1) The name of the association.

16 (2) The location of the association's offices or
17 places of business in the United States and abroad.

18 (3) The names and addresses of the association's
19 officers, stockholders, and members.

20 (4) A copy of the certificate or articles of incorpo-
21 ration and bylaws, if the association is a corporation;
22 or a copy of the articles or contract of association, if
23 the association is unincorporated.

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1 (5) A description of the goods, wares, merchan-
2 dise, or services which the association or its members
3 export or propose to export.
4 (6) The methods by which the association con-
5 ducts or proposes to conduct export trade in the de-
6 scribed goods, wares, merchandise, or services, includ-
7 ing, but not limited to, any agreements to sell exclu-
8 sively to or through the association, any agreements
9 with foreign persons who may act as joint selling
10 agents, any agreements to acquire a foreign selling
11 agent, any agreements for pooling tangible or intangi-
12 ble property or resources, or any territorial,
13 price-maintenance, membership, or other restrictions
14 to be imposed upon members of the association.
15 (7) The names of all countries where export trade
16 in the described goods, wares, merchandise, or services
17 is conducted or proposed to be conducted by or
18 through the association.
19 (8) Any other information which the Commission
20 may request concerning the organization, operation,
21 management, or finances of the association; the rela-
22 tion of the association to other associations, corpora-
23 tions, partnerships, and individuals; and competition or
24 potential competition, and effects of the association
25 thereon. The Commission may not request information

1 under this paragraph which is not reasonably available
2 to the person making application or which is not neces-
3 sary for certification of the prospective association.
4 (b) ISSUANCE OF CERTIFICATE.—Based upon the in-
5 formation obtained from the application, the Commission
6 shall certify an association within 90 days after receiving the
7 association's application for certification if the Commission
8 determines that the association and its members and the pro-
9 posed export trade activities meet the requirements of section
10 4 of this Act. The certification may be issued subject to such
11 terms and conditions as the Commission determines to be
12 appropriate to ensure that the association and its activities
13 meet the requirements for certification during the period for
14 which the certification is in effect, and that all members of
15 the association are treated equitably.
16 (c) MATERIAL CHANGES IN CIRCUMSTANCES; AMEND-
17 MENT OF APPLICATION.—
18 (1) VOIDING OF CERTIFICATION.—Whenever
19 there is a material change in—
20 (A) the domestic and international conditions,
21 circumstances, and factors which make an associ-
22 ation useful for the purpose of promoting the
23 export trade of its goods, wares, merchandise, or
24 services, or

1 (B) the association's membership, export
2 trade, export trade activities, or methods of oper-
3 ation which would cause the association to fail to
4 meet any requirement of section 4,
5 then the association shall apply to the Commission for
6 an amendment of its certification.
7 (2) AMENDMENT OF APPLICATION.—The request
8 for amendment shall be filed within 30 days after the
9 date of the material change and shall set forth the re-
10 quested amendment of the application and the reasons
11 for the requested amendment. Any request for the
12 amendment of an application shall be treated in the
13 same manner as an original application for certifica-
14 tion. If the request is filed within 30 days after the
15 material change which requires the amendment, and if
16 the requested amendment is approved, then there shall
17 be no interruption in the period for which certification
18 is in effect.
19 (3) AMENDMENT UPON RECOMMENDATION OF
20 COMMISSION.—After notice to the association involved
21 and the opportunity for a hearing on the record, the
22 Commission may, on its own initiative, or upon the
23 recommendation of the Attorney General or any other
24 person—

1 (A) require that an association's certification
2 be amended,
3 (B) require that the organization or operation
4 of the association be modified to correspond with
5 the association's certification, or
6 (C) revoke, in whole or in part, the certifica-
7 tion of the association upon a finding that the as-
8 sociation, its members, or its export trade activi-
9 ties do not meet the requirements of section 4 of
10 this Act.

11 **SEC. 7. GUIDELINES.**

12 (a) INITIAL PROPOSED GUIDELINES.—The Commis-
13 sion and the Attorney General shall publish proposed guide-
14 lines for purposes of determining whether an association, its
15 members, and its export trade activities meet the require-
16 ments of section 4 of this Act.

17 (b) PERIODIC REVISION.—After publication of the
18 guidelines, the Commission and the Attorney General shall
19 meet periodically to revise the guidelines as needed.

20 **SEC. 8. CERTIFICATION FOR EXISTING ASSOCIATIONS.**

21 The Commission shall certify any export trade associ-
22 ation registered with the Federal Trade Commission as of the
23 date of enactment of this Act if such association, within 180
24 days after that date, files with the Commission an application
25 for certification as provided for in section 6 of this Act, unless

1 such application shows on its face that the association is not
2 eligible for certification under this Act. If the application sub-
3 mitted by such an association shows on its face that the asso-
4 ciation is not eligible for certification under this Act, its regis-
5 tration under the Webb-Pomerene Act shall cease to be ef-
6 fective 30 days after the date on which the Commission noti-
7 fies the association of its determination of ineligibility.

8 **SEC. 9. REVIEW OF DETERMINATIONS.**

9 Whenever the Commission makes a determination under
10 this Act with respect to an application for certification, the
11 amendment, modification, or revocation of a certification, or
12 the modification of the organization or operation of an export
13 trade association, it shall—

14 (1) notify the association of its determination and
15 the reasons for its determination, and

16 (2) upon request made by the association, afford
17 the association an opportunity for a hearing.

18 **SEC. 10. ANNUAL REPORTS.**

19 Every certified association shall submit an annual report
20 to the Commission on January 2 of each year, in such form
21 as it may require, setting forth the information described by
22 section 6(a) of this Act.

1 **SEC. 11. MODIFICATION OF ASSOCIATION TO COMPLY WITH**
2 **UNITED STATES OBLIGATIONS.**

3 At such time as the United States undertakes interna-
4 tional obligations by treaty or statute, to the extent that the
5 operations of any export trade association, certified under
6 this Act are inconsistent with such international obligations,
7 the Commission or Attorney General may require such asso-
8 ciation to modify its operations so as to be consistent with
9 such international obligations.

10 **SEC. 12. REGULATIONS.**

11 The Commission, in consultation with the Attorney
12 General, shall promulgate such rules and regulations as may
13 be necessary to carry out the purposes of this Act.

14 **SEC. 13. REPEAL OF WEBB-POMERENE ACT.**

15 The Webb-Pomerene Act (15 U.S.C. 61-66) is repealed
16 as of the 90th day after the date of enactment of this Act.

96TH CONGRESS
1ST SESSION

S. 1663

To encourage exports by providing for the licensing of export trading companies by the Secretary of Commerce, and by otherwise facilitating their formation and operation.

IN THE SENATE OF THE UNITED STATES

AUGUST 2 (legislative day, JUNE 21), 1979

Mr. STEVENSON introduced the following bill; which was read twice and referred jointly by unanimous consent to the Committees on Banking, Housing, and Urban Affairs and Finance

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A BILL

To encourage exports by providing for the licensing of export trading companies by the Secretary of Commerce, and by otherwise facilitating their formation and operation.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 **SECTION 1. SHORT TITLE.**
4 This Act may be cited as the "Export Trading Compa-
5 ny Act of 1979".

1 TITLE I—ESTABLISHMENT OF EXPORT TRADING
2 COMPANIES

3 **SEC. 101. DEFINITIONS.**

4 As in this title—

5 (1) EXPORT TRADE.—The term "export trade"
6 means trade or commerce in goods produced in the
7 United States or services produced in the United
8 States exported, or in the course of being exported,
9 from the United States to any foreign nation.

10 (2) GOODS PRODUCED IN THE UNITED
11 STATES.—The term "goods produced in the United
12 States" means tangible property not less than 75 per-
13 cent of the total value, or of the value added to a ma-
14 terial or commodity through manufacturing or process-
15 ing, of which is attributable to the United States.

16 (3) SERVICES PRODUCED IN THE UNITED
17 STATES.—The term "services produced in the United
18 States" means architectural, engineering, consulting,
19 legal, training, financial, insurance, management, com-
20 munications, and other services not less than 75 per-
21 cent of the value of which is provided by United States
22 citizens or is otherwise attributable to the United
23 States.

1 (4) EXPORT TRADE ACTIVITIES.—The term
2 "export trade activities" includes any activity which is
3 incidental to export trade.

4 (5) UNITED STATES.—The term "United States"
5 means the several States of the United States, the Dis-
6 trict of Columbia, the Commonwealth of Puerto Rico,
7 the Virgin Islands, American Samoa, Guam, and the
8 Trust Territory of the Pacific Islands.

9 (6) ANTITRUST LAWS.—The term "antitrust
10 laws" means the antitrust laws defined in the first sec-
11 tion of the Clayton Act (15 U.S.C. 12) and section 4
12 of the Federal Trade Commission Act (15 U.S.C. 44),
13 any other law of the United States in pari materia with
14 those laws, and any State antitrust or unfair competi-
15 tion law, and all amendments to the foregoing.

16 (7) SECRETARY.—The term "Secretary" means
17 the Secretary of Commerce.

18 (8) ATTORNEY GENERAL.—The term "Attorney
19 General" means the Attorney General of the United
20 States.

21 SEC. 102. LICENSING.

22 (a) ELIGIBILITY.—In order to be licensed by the Secre-
23 tary as an export trading company under this section, an ap-
24 plicant shall demonstrate, to the satisfaction of the Secretary,
25 that it meets all requirements under this title for licensing

1 and that it is, or will be, organized and operated principally
2 for the purposes of—
3 (1) exporting goods and services produced in the
4 United States, and
5 (2) facilitating the exportation of goods and serv-
6 ices produced in the United States by providing export
7 services such as international market research, adver-
8 tising, marketing, insurance, legal assistance, transpor-
9 tation, including trade documentation and freight for-
10 warding, communication and processing of foreign
11 orders to and for exporters and foreign purchasers,
12 warehousing, foreign exchange, financing, and any
13 other export services determined by the Secretary by
14 regulation to be consistent with the purposes of this
15 title.
16 (b) APPLICATION.—In order to be licensed by the Sec-
17 retary as an export trading company, a firm shall file with
18 the Secretary a written application setting forth the
19 following:
20 (1) The name of the firm.
21 (2) The location of the firm's offices or places of
22 business in the United States and abroad.
23 (3) The names and addresses of the firm's officers,
24 stockholders, and members.

1 (4) A copy of the certificate or articles of incorpo-
2 ration and bylaws, if the firm is a corporation; or a
3 copy of the agreement establishing the firm, if the firm
4 is unincorporated.
5 (5) A general description of the goods or services
6 which the firm exports or proposes to export.
7 (6) The methods by which the firm conducts or
8 proposes to conduct export trade in the described
9 goods or services, including, but not limited to, any
10 agreement to sell exclusively to or through the firm,
11 any agreement with foreign persons who may act as
12 joint selling agents, any agreement to acquire a foreign
13 selling agent, and any agreement for pooling tangible
14 or intangible property or resources.
15 (7) The names of all countries where export trade
16 in the described goods or services is conducted or pro-
17 posed to be conducted by or through the firm.
18 (8) Any other information concerning the organi-
19 zation, operation, management, or finances of the firm,
20 the relation of the firm to other firms, corporations,
21 partnerships, and individuals, and competition or poten-
22 tial competition the Secretary deems necessary for pur-
23 poses of administering this title.
24 (c) OWNERSHIP REQUIREMENTS.—

1 (1) IN GENERAL.—The Secretary may not issue a
2 license to an export trading company under this section
3 if—
4 (A) any partnership, association, or corpora-
5 tion owned or controlled by a foreign corporation
6 or other foreign entity owns stock, or other secu-
7 rities with voting rights, issued by the export
8 trading company, or
9 (B) any person owns, directly or indirectly,
10 more than 20 percent of the voting stock or inter-
11 est in the export trading company.
12 (2) DIVESTITURE TO MEET CONTROL LIMITA-
13 TION.—Notwithstanding the limitation of paragraph
14 (1)(B), the Secretary shall not deny a license to an
15 export trading company solely because of such limita-
16 tion if—
17 (A) the person or persons whose ownership
18 of stock or interest exceeds the limitation submits
19 a divestiture plan under which he will divest him-
20 self of his stock or interest in excess of the limita-
21 tion over a 10-year period beginning with the
22 year in which the license is issued with—
23 (i) the first sale or transfer of stock or
24 interest occurring not later than the fifth
25 year of such period,

1 (ii) the divestiture progressing no less
2 rapidly than ratably over the years remaining
3 between the first year of divestiture and the
4 last year of the 10-year period, and
5 (iii) divestiture completed, to the extent
6 necessary to meet the limitation under para-
7 graph (1)(B) by the close of such last year,
8 and
9 (B) such reports, no less frequently than an-
10 nually, to the Secretary on the progress of the di-
11 vestiture as he may require.
12 (d) LIMITATIONS ON ACTIVITIES OF LICENSED
13 EXPORT TRADING COMPANIES.—The Secretary may not
14 issue a license under this section to, and shall revoke any
15 such license issued to, an export trading company if that
16 company engages in manufacturing directly or through a do-
17 mestic or foreign corporation which is a member of the con-
18 trolled group of corporations (within the meaning of section
19 1563 of the Internal Revenue Code of 1954) of which the
20 export trading company is a member. For the purpose of this
21 subsection, the term "manufacturing" does not include pack-
22 aging or limited fabrication and final assembly of products
23 which otherwise meet the definition in section 101(2) of
24 "goods produced in the United States." The Secretary may
25 not decline to issue such a license, or revoke such a license,

1 on the ground that the export trading company is engaged in
2 activities (other than manufacturing) other than activities in-
3 volving export trade to the extent that such other activities
4 (other than manufacturing) are necessary to encourage and
5 facilitate exports of goods and services produced in the
6 United States.

7 (e) ISSUANCE OF LICENSE.—Based upon the informa-
8 tion obtained from the application, the Secretary shall license
9 an export trading company within 90 days after receiving the
10 application for licensing if the Secretary determines that the
11 firm and the proposed export trade activities meet the re-
12 quirements of this title. The license may be issued subject to
13 such terms and conditions as the Secretary determines to be
14 appropriate to ensure that the export trading company and
15 its activities meet the requirements for licensing during the
16 period for which the license is in effect.

17 (f) MATERIAL CHANGES IN CIRCUMSTANCES; AMEND-
18 MENT OF APPLICATION.—

19 (1) VOIDING OF LICENSE.—Whenever there is a
20 material change in—

21 (A) the domestic and international conditions,
22 circumstances, and factors which make an export
23 trading company useful for the purpose of promot-
24 ing the export trade of its goods or services, or

1 (B) the export trading company's export
2 trade, export trade activities, or methods of oper-
3 ation which would cause the company to fail to
4 meet any requirement of this title,
5 then the company shall apply to the Secretary for an
6 amendment of its license.
7 (2) AMENDMENT OF APPLICATION.—The request
8 for amendment shall be filed within 30 days after the
9 date of the material change and shall set forth the re-
10 quested amendment of the application and the reasons
11 for the requested amendment. Any request for the
12 amendment of an application shall be treated in the
13 same manner as an original application for licensing. If
14 the request is filed within 30 days after the material
15 change which requires the amendment, and if the re-
16 quested amendment is approved, then there shall be no
17 interruption in the period for which the license is in
18 effect.
19 (3) AMENDMENT UPON RECOMMENDATION OF
20 SECRETARY.—After notice to the export trading com-
21 pany involved and the opportunity for a hearing on the
22 record, the Secretary may—
23 (A) require that an export trading company's
24 license be amended;

1 (B) require that the organization or operation
2 of the export trading company be modified to cor-
3 respond with the company's license; or
4 (C) revoke, in whole or in part, the license of
5 the export trading company upon a finding that
6 the company or its export trade activities do not
7 meet the requirements of this title.

8 SEC. 103. ENFORCEMENT.

9 (a) EXCLUSIVE JURISDICTION OF SECRETARY.—The
10 Secretary shall have exclusive jurisdiction to determine
11 whether an export trading company licensed under this
12 title—
13 (1) has failed to comply with the terms and condi-
14 tions of its license, has engaged in activities or fur-
15 nished services not described in its license application
16 or not permitted under the license, or has knowingly
17 violated any provision of this title, or
18 (2) has taken any action which is inconsistent
19 with the requirements of this title.
20 (b) DETERMINATIONS.—The Secretary shall make a
21 determination under subsection (a) after an investigation
22 commenced after receipt of a complaint, filed with the Secre-
23 tary at such time and in such manner as the Secretary may
24 require, or upon the Secretary's own motion, and after notice
25 to the export trading company named in the complaint and

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1 an opportunity for a hearing on the record. The complaint
2 may be filed by any person whose economic interest is, or
3 may appear to be, adversely affected by activity to which the
4 complaint relates.

5 (c) REMEDIES.—If the determination of the Secretary
6 under subsection (a) is affirmative, then the Secretary may—

7 (1) in the case of an affirmative determination
8 under subsection (a)(1)—

9 (A) require the company to file an amended
10 application for license under section 102(d).

11 (B) require the company to modify its organi-
12 zation or operations,

13 (C) revoke, in whole or in part, the license of
14 the company, or

15 (D) refer the matter to the Attorney General
16 for prosecution under the antitrust laws, or

17 (2) in the case of an affirmative determination
18 under subsection (a)(2)—

19 (A) bring an action in the appropriate Feder-
20 al district court to enjoin or restrain the company
21 from engaging in any activity which constitutes or
22 results in anything described in paragraph (1), (2),
23 or (3) of section 106, or

24 (B) revoke, in whole or in part, the license of
25 the company.

1 (d) STANDING REQUIREMENT.—No person shall have
2 standing to bring an action against a company licensed under
3 section 102 for any activity which constitutes or results in
4 anything described in paragraph (1), (2), or (3) of section 106
5 other than an officer or employee of the United States acting
6 in his official capacity.

7 SEC. 104. REVIEW OF DETERMINATIONS.

8 Whenever the Secretary makes a determination under
9 this Act with respect to an application for a license, the
10 amendment, modification, or revocation of a license, or the
11 modification of the organization or operation of an export
12 trading company, the Secretary shall—

13 (1) notify the company of the determination and
14 the reasons for the determination, and

15 (2) upon request made by the company, afford the
16 company an opportunity for a hearing.

17 SEC. 105. INITIAL INVESTMENTS AND OPERATING EXPENSES.

18 (a) ELIGIBILITY FOR LOANS AND GUARANTEES.—Any
19 export trading company licensed under this title is eligible for
20 a direct loan or financial guarantee from the Export-Import
21 Bank of the United States, and, in the case of a small busi-
22 ness, from the Small Business Administration, and, where
23 otherwise eligible, from the Economic Development Adminis-
24 tration, to meet export-related operating expenses during the
25 first 5 years of the company's operation. Any such assistance

1 shall be used only for expenses directly related to exports and
2 export services, and shall not exceed 50 percent of the total
3 operating expenses of such company in any year. In no case
4 may the credits or guarantees to any one company exceed
5 $10,000,000 in any single year or $25,000,000 during the 5-
6 year period.

7 (b) EXPORT-IMPORT BANK LOANS AND GUARAN-
8 TEES.—Subject to the limitations set forth in this title and
9 the Export-Import Bank Act of 1945, the Export-Import
10 Bank of the United States may provide loan guarantees to
11 any licensed export trading company which, in the judgment
12 of the Board of Directors of the Bank is creditworthy but is
13 unable to obtain sufficient financing or insurance on reason-
14 able terms from other sources.

15 (c) OWNERSHIP OF SECURITIES BY BANK OR BANK
16 HOLDING COMPANY.—Notwithstanding any other provision
17 of law, but subject to the other provisions of this title, and
18 rules and regulations of the appropriate regulatory agencies,
19 any bank or bank holding company chartered or incorporated
20 within the United States and any corporation organized
21 under section 25(a) of the Federal Reserve Act may purchase
22 for its own account equity securities of an export trading
23 company which is licensed under this title: *Provided, how-*
24 *ever,* That total investment in export trading companies by
25 any bank or bank holding company may not exceed 10 per-

1 cent of its capital stock actually paid in and unimpaired plus
2 10 percent of its unimpaired surplus fund.

3 SEC. 106. ANTITRUST.

4 (a) IN GENERAL.—An export trading company licensed
5 under section 102 of this title is exempt from the application
6 of the antitrust laws except to the extent that the activities in
7 which it is engaged constitute or result in—

8 (1) a substantial restraint of trade within the
9 United States or a substantial restraint of the export
10 trade of a domestic competitor,

11 (2) an unfair method of competition against a do-
12 mestic competitor, or

13 (3) an unreasonable enhancement, stabilization, or
14 depression of prices within the United States of goods
15 or services of the class exported by that company.

16 (b) INTERNATIONAL OBLIGATIONS.—Subsection (a)
17 shall not apply to an export trading company licensed under
18 this title to the extent that its application would be inconsist-
19 ent with international obligations of the United States.

20 SEC. 107. REGULATIONS.

21 The Secretary shall promulgate such rules and regula-
22 tions as may be necessary to carry out the purposes of this
23 title. The Secretary shall consult with the Attorney General
24 prior to promulgating rules and regulations to carry out sec-
25 tions 103 and 106 of this title.

1 TITLE II—TAX TREATMENT OF EXPORT TRAD-
2 ING COMPANIES AND THEIR SHAREHOLD-
3 ERS

4 SEC. 201. ESTABLISHMENT AND TAXATION OF EXPORT TRAD-
5 ING COMPANIES AND THEIR SHAREHOLDERS.

6 (a) IN GENERAL.—Chapter 1 of the Internal Revenue
7 Code of 1954 (relating to normal taxes and surtaxes) is
8 amended by adding at the end thereof the following new sub-
9 chapter:

10 **"Subchapter V—Export Trading Companies**

"Sec. 1398. Definition of licensed export trading company.
"Sec. 1398A. Election by licensed export trading company.
"Sec. 1398B. Rules applicable to the taxation of electing licensed export trading company shareholders.
"Sec. 1398C. Special rules applicable to an electing licensed export trading company.

11 "SEC. 1398. DEFINITION OF LICENSED EXPORT TRADING COM-
12 PANY.

13 "For purposes of this subchapter, the term 'licensed
14 export trading company' means an export trading company
15 licensed under section 104 of the Export Trading Company
16 Act of 1979, the license of which is valid at all times during
17 the taxable year of the company.

18 "SEC. 1398A. ELECTION BY LICENSED EXPORT TRADING COM-
19 PANY.

20 "(a) ELIGIBILITY.—Except as provided in section
21 1398C, a licensed export trading company may elect, in ac-

1 cordance with the provisions of this section, not to be subject
2 to the taxes imposed by this chapter.
3 "(b) EFFECT.—If a licensed export trading company
4 makes an election under subsection (a), then—
5 "(1) with respect to the taxable years of the
6 export trading company for which such election is in
7 effect, the company shall not be subject to the taxes
8 imposed by this chapter, and, with respect to such tax-
9 able years and all succeeding taxable years, the provi-
10 sions of section 1398E shall apply to that company,
11 and
12 "(2) with respect to each such taxable year, the
13 provisions of sections 1398B and 1398C shall apply to
14 the shareholders of the company.
15 "(c) WHERE AND HOW MADE.—An election under sub-
16 section (a) shall be made by an export trading company at
17 such time and in such manner as the Secretary shall pre-
18 scribe by regulations.
19 "(d) YEARS FOR WHICH EFFECTIVE.—An election
20 under subsection (a) shall be effective for the taxable year of
21 the export trading company for which it is made and for all
22 succeeding taxable years of the company, unless it is termi-
23 nated under subsection (f).

1 "(e) TAXABLE YEAR.—The taxable year of an export
2 trading company shall end on December 31 unless the Secre-
3 tary consents to a different taxable year.
4 "(f) TERMINATION.—The election of an export trading
5 company under subsection (a) shall terminate for any taxable
6 year during which it ceases to be a licensed export trading
7 company and for all succeeding taxable years. The election of
8 a licensed export trading company under subsection (a) may
9 be terminated at any other time with the consent of the Sec-
10 retary, effective for the first taxable year with respect to
11 which the Secretary consents and for all succeeding taxable
12 years.
13 "SEC. 1398B. RULES APPLICABLE TO THE TAXATION OF
14 ELECTING LICENSED EXPORT TRADING COM-
15 PANY SHAREHOLDERS.
16 "(a) DISTRIBUTIONS TAXED AS ORDINARY INCOME.—
17 Any amount distributed by an electing licensed export trad-
18 ing company shall be treated as a distribution to which sec-
19 tion 301(a) applies. Any amounts includable in the gross
20 income of any shareholder by reason of ownership of stock in
21 an electing licensed export trading company shall not be con-
22 sidered as a dividend for purposes of section 116.
23 "(b) SPECIAL RULE FOR INVESTMENT CREDIT.—The
24 investment credit of an electing licensed export trading com-
25 pany for any taxable year shall be allowed as a credit to the

1 shareholders of such company and the manner and to the
2 extent set forth in this subsection.

3 "(1) CREDIT.—There shall be apportioned among
4 the shareholders a credit equal to the amount each
5 shareholder would have received if, on each day of
6 such taxable year, there had been distributed pro rata
7 to the shareholders the electing licensed export trading
8 company's net investment credit divided by the number
9 of days in the company's taxable year.

10 "(2) NET INVESTMENT CREDIT.—For purposes of
11 this subsection, the term 'net investment credit' means
12 the investment credit of the electing licensed export
13 trading company for its taxable year less any tax from
14 recomputing of prior year's investment credit in ac-
15 cordance with section 47.

16 "(3) RECAPTURE.—There shall be apportioned
17 among the shareholders of an electing licensed export
18 trading company, in the manner described in paragraph
19 (1), an additional tax equal to the excess of any tax
20 resulting from recomputing of prior year's investment
21 credit in accordance with section 47 over the invest-
22 ment credit of the electing licensed export trading com-
23 pany for its taxable year.

24 "(c) SPECIAL RULE FOR FOREIGN TAX CREDIT.—

1 "(1) IN GENERAL.—For purposes of subpart A of
2 part III of subchapter N, a shareholder in an electing
3 licensed export trading company who receives a distri-
4 bution in any taxable year from such company shall be
5 deemed to have paid the same proportion of any
6 income, or profits, or excess profits taxes paid or
7 deemed to be paid by such electing licensed export
8 trading company to any foreign country or to any pos-
9 session of the United States, on or with respect to the
10 accumulated profits of such electing licensed export
11 trading company from which such distributions were
12 paid, which the amount of such distributions bears to
13 the amount of such accumulated profits in excess of
14 such income, war profits, and excess profits taxes
15 (other than those deemed paid).
16 "(2) DEFINITION OF ACCUMULATED PROFITS;
17 ACCOUNTING PERIODS.—For purposes of this subsec-
18 tion, the term 'accumulated profits' has the same
19 meaning as in section 902(c)(1), in the rules relating to
20 the application of the word 'year' with respect to ac-
21 counting periods of less than 1 year (set forth in sec-
22 tion 902(c)(2)) shall apply. For purposes of this para-
23 graph, the provisions of section 902(c) shall be applied
24 by substituting 'electing licensed export trading compa-
25 ny' for 'foreign corporations' each place it appears.

1 "SEC. 1398C. SPECIAL RULES APPLICABLE TO AN ELECTING
2 LICENSED EXPORT TRADING COMPANY.
3 "The provisions of section 482 (relating to allocation of
4 income and deductions among taxpayers) shall not apply with
5 respect to gross income, deductions, credits, or allowances
6 between an electing licensed export trading company and a
7 foreign subsidiary of such a company.".
8 (b) NET OPERATING LOSS DEDUCTION.—Paragraph
9 (1) of section 172(b) of such Code (relating to net operating
10 loss carrybacks and carryovers) is amended by adding at the
11 end thereof the following new subparagraph:
12 "(I) in the case of an electing licensed export
13 trading company which has a net operating loss
14 for any taxable year, such loss shall not be a net
15 operating loss carryback to any taxable year pre-
16 ceding the year of such loss, which shall be a net
17 operating loss carryover to each of the 10 taxable
18 years following the year of such loss.".
19 (c) RETURN OF ELECTING LICENSED EXPORT TRAD-
20 ING COMPANY—Subpart A of part III of subchapter A of
21 chapter 61 (relating to information on returns) is amended by
22 adding at the end thereof the following new section:
23 "SEC. 6039C. RETURN OF ELECTING LICENSED EXPORT TRAD-
24 ING COMPANY.
25 "Every electing licensed export trading company (as de-
26 fined in section 1398) which makes the election provided by

1 section 1398A shall make a return for each taxable year,
2 stating specifically the items of its gross income and the de-
3 ductions allowable by subtitle A, the amount of investment
4 credit or additional tax, as the case may be, the names and
5 addresses of all persons owning stock in the company at any
6 time during the taxable year, the number of shares of stock
7 owned by each shareholder at all times during the taxable
8 year, the amount of money and other property distributed by
9 the company during the taxable year to each shareholder, the
10 date of each such distribution, and such other information, for
11 the purposes of carrying out the provisions of subchapter V of
12 chapter 1, as the Secretary may by regulation prescribe. Any
13 return filed pursuant to this section shall, for purposes of
14 chapter 66 (relating to limitations), be treated as a return
15 filed by the company under section 6012. Every electing li-
16 censed export trading company shall file an annual report
17 with the Secretary summarizing its operations for such
18 year.".

19 (d) CLERICAL AMENDMENTS.—

20 (1) The table of subchapters for chapter 1 of such
21 Code is amended by adding at the end thereof the fol-
22 lowing:

"SUBCHAPTER V. Export Trading Companies.".

1 (2) The table of sections for subpart A of part III
2 of subchapter A of chapter 61 of such Code is amend-
3 ed by adding at the end thereof the following:

"SEC. 6039C. Return of electing licensed export trading company.".

4 **SEC. 201. EFFECTIVE DATE.**

5 The amendments made by this title shall apply with re-
6 spect to export trading companies licensed after December
7 31, 1979.

96TH CONGRESS
1ST SESSION

S. 1744

To amend the Export Trade Act to encourage increased utilization of the Act, to expand exemptions provided under the Act, to clarify United States Government policy with respect to the administration of the Act, to assist American exporters in international trade competition, and for other purposes.

IN THE SENATE OF THE UNITED STATES

SEPTEMBER 13 (legislative day, JUNE 21), 1979

Mr. STEVENSON (for Mr. INOUYE) introduced the following bill; which was read twice and referred to the Committee on Banking, Housing, and Urban Affairs

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A BILL

To amend the Export Trade Act to encourage increased utilization of the Act, to expand exemptions provided under the Act, to clarify United States Government policy with respect to the administration of the Act, to assist American exporters in international trade competition, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 SECTION 1. (a) FINDINGS.—The Congress finds and de-
4 clares that—

1 (1) in 1978 the United States suffered the largest
2 merchandise trade deficit in its history, amounting to
3 more than $39,000,000,000 (cost, insurance, and
4 freight basis);
5 (2) the trade deficit has contributed to the decline
6 of the dollar on international currency markets and has
7 led to widespread public concern about the strength of
8 the dollar;
9 (3) the export sector of the American economy is
10 responsible for creating and maintaining millions of
11 jobs and for earning revenues which enable the United
12 States to import those goods and materials required by
13 the American economy;
14 (4) the United States share of total world exports
15 of manufactures has steadily eroded from 25.3 per
16 centum in 1960 to 21.3 per centum in 1970 and to
17 17.0 per centum in 1978; and
18 (5) United States laws regulating the ability of
19 domestic companies to combine in joint export efforts
20 are significantly more stringent than those in other
21 countries.
22 (b) PURPOSES.—It is the purpose of Congress in this
23 Act to encourage American exports through increased utili-
24 zation of the Export Trade Act by clarifying its provisions

1 and by making the export of services eligible for inclusion in
2 this Act.

3 SEC. 2. Section 1 of the Export Trade Act (40 Stat.
4 516; 15 U.S.C. 61) is amended to read as follows:

5 "As used in this Act:

6 "(1) 'Antitrust laws' means the laws defined as such in
7 sections 12 and 44 of title 15, United States Code, the Fed-
8 eral Trade Commission Act (15 U.S.C. 41-58), and other
9 laws of the United States in pari materia, including State
10 laws on antitrust and unfair methods of competition, and all
11 amendments to the foregoing.

12 "(2) 'Association', whenever used in sections 1 through
13 5 of this Act, means any combination, by contract or other
14 arrangement, of two or more persons who are citizens of the
15 United States or which are created under and exist pursuant
16 to the laws of any State or of the United States.

17 "(3) 'Export trade' means exclusively trade or com-
18 merce in manufactured goods and products, agricultural
19 goods and products, merchandise, or architectural, engineer-
20 ing, construction, training, financing, insurance, or project or
21 general management services or the licensing for distribution
22 or exhibition of motion pictures or television films or tapes or
23 similar services which are exported, or in the course of being
24 exported, from the United States to any foreign nation. The
25 term does not include—

1 "(A) the production, manufacture, or sale for con-
2 sumption or for resale within the United States of such
3 goods, products, merchandise, or services, or any act in
4 the course of such production, manufacture, or sale for
5 consumption or for resale;
6 "(B) any act, practice, agreement, or course of
7 conduct, the effect of which is to constitute a signifi-
8 cant restraint of trade or commerce, including foreign
9 commerce, in the United States; or
10 "(C) trade or commerce in patents, licenses, or
11 know-how except as necessary to the sale of such
12 goods, products, merchandise, or services.
13 "(4) 'United States' means any of the several States,
14 the District of Columbia, the Commonwealth of Puerto Rico,
15 the Virgin Islands, the Canal Zone, American Samoa, Guam,
16 and the Trust Territory of the Pacific Islands.
17 "(5) 'Trade within the United States', wherever used in
18 sections 1 through 5 of this Act, means trade or commerce
19 between two or more States.".
20 SEC. 3. Section 2 of such Act is further amended by
21 adding at the end thereof the following two new subsections:
22 "(b) The Secretary of Commerce shall establish within
23 the Department of Commerce a program to promote and
24 maximize the formation of associations and the use of the

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1 provisions of this Act in a manner consistent with this Act
2 and the antitrust laws.
3 "(c) The Secretary of Commerce, the Chairman of the
4 Federal Trade Commission, and the Attorney General of the
5 United States and their duly authorized representatives shall
6 meet and discuss periodically as necessary to avoid conflict-
7 ing positions regarding the oversight of associations and shall
8 meet periodically with members of the private sector to
9 review the policies of the Commission and Department of
10 Justice which affect the congressional policy of stimulating
11 American exports and improving the international trading
12 competitiveness of American exports.".
13 SEC. 4. Section 5 of such Act is amended by inserting
14 "Department of Commerce" wherever the term "Federal
15 Trade Commission" appears.

HAY ASSOCIATES

UNITED STATES
DEPARTMENT OF COMMERCE

A STUDY TO DETERMINE THE FEASIBILITY OF THE EXPORT TRADING COMPANY CONCEPT AS A VIABLE VEHICLE FOR EXPANSION OF UNITED STATES EXPORTS

Contract Number 6-36234

March, 1977

HAY ASSOCIATES
Philadelphia, Pennsylvania

with
legal consultation
by

COLLIER, SHANNON, RILL, EDWARDS & SCOTT
Washington, D. C.

AMENDMENT TO A STUDY TO DETERMINE THE FEASIBILITY OF THE EXPORT TRADING COMPANY CONCEPT

Contact No. 6-36234

Pending Legislation

At this point in time, there is no legislation pending that would in any way affect the feasibility or viability of the Export Trading Company concept as we defined it. The only directly related legislative proposals that could affect the viability and, indeed, might be considered stimulative of the concept, concern expansion of the Webb-Pomerene Export Trade Act. A review of the history of Congressional efforts to initiate or amend legislation relating to export trading corporations in the last five years indicates that efforts have been focused on three areas:

1. broaden provisions of the Webb-Pomerene Act to include services;

2. exempt Webb associations from private treble damage actions and exempt individuals from criminal penalties; and

3. create greater certainty with respect to the application of anti-trust laws, by establishing pre-clearance procedures and giving the FTC sole jurisdiction to administer the law.

No legislation has been enacted into law during this period.

In 1971, Senators Inouye and Magnuson introduced the Export Expansion Act, S. 2754, which would have authorized chartered export associations, allowing the establishment of groups of firms to engage in export activities as long as they operated within the legal confines of a charter approved by the Department of Commerce. The Chairman of the FTC, Miles Kirkpatrick, testified in opposition to S. 2754, and suggested that the Export Trade Act of 1918 (the Webb-Pomerene Act) be amended to exempt trade associations from private treble damage actions and individuals from criminal penalties.

In 1972, Senator Inouye and Magnuson introduced a series of bills, S. 4114 through S. 4120. These bills included modifications reflecting the testimony received on S. 2754, and S. 4120 incorporated the FTC's suggestions regarding exemptions from treble damage actions and criminal penalties and included the export of services as an exempted activity. The other bills introduced in that series, among other things, would have established a Trade Development Corps of trained business personnel to assist the Government in programs to make American exports more competitive, authorized regional American merchandise centers offering services such as warehousing, distributing, translating, etc., established a joint export association program permitting the Government to enter into cost-sharing contracts with private firms, and expanded the kinds of goods which could be imported into foreign trade zones for manufacture and export.

In 1973, Senator Inouye and others introduced S. 1483, which would have amended the Webb-Pomerene Act by including services and excluding treble damage actions and criminal sanctions.

Also in 1973, Senator Inouye and others introduced S. 1486, which would have established a Federal Export Agency within the Department of Commerce to foster the development of export associations or joint export projects and provide special incentives to small businesses.

S. 1774, introduced in 1973 at the Administration's request, again included the exemption of services under Webb-Pomerene. The changes in anti-trust laws added a pre-clearance procedure designed to provide greater certainty with respect to application of the anti-trust laws to export trade associations, and gave the FTC exclusive authority to determine whether the activities of registered groups are in conformance with their registration statements.

Senator Inouye and Congressman Thomas Rees introduced identical bills in 1975, S. 1973 and H. R. 9449 respectively. Again, this legislation exempted

services under the Export Trade Act. In addition, the legislation established new criteria for eligibility to participate in Webb associations: export sales must be likely to be substantially increased as a result of membership in an association, and not likely to increase significantly without membership; and such individual membership in an association is essential to the functioning of the association.

The Secretary of Commerce, in consultation with the Chairman of the FTC, would be required to establish a program to promote and maximize the formation of associations and use of the provisions of the Act within the Commerce Department in a manner consistent with the Act and anti-trust laws. Lastly, in an effort to provide greater certainty in the application of the anti-trust laws, the FTC and the Attorney General would be required to meet periodically to avoid conflicting positions regarding the formation and maintenance of associations.

As of this date, Senator Inouye has indicated willingness to try to move his legislation through the Senate. However, the House Judiciary Committee, claiming a crowded calendar of higher-priority bills, has shown little interest in acting on the legislation.

Competition with Foreign Export Trading Companies

We have defined the ETC concept to insure its ability to successfully engage with any kind of competition. Three interrelated elements form the basis of competitive strength for trading companies:

- sales distribution systems;
- financing muscle; and
- minimization of transaction costs.

The European trading companies have a fourth strength, emplacement in local markets.

1. Sales distribution systems

The ETC we recommend should be competitive with any other trading company as we specifically call for investments in offices and export supporting infrastructure that do not typically exist in EMC's, but are prevalent among foreign export trading companies. Obviously, the issue of scale comes into play. The size of a Japanese trading company will support more infrastructure than the volume we anticipate for an American ETC. On the other hand, the scale requirements of Japanese companies are such that it may not be economically justifiable for them to invest in resources to support sales of smaller manufacturers. The required degree of support will clearly vary from industry to industry and country to country so it is difficult to generalize. It is our judgement, however, that as long as a strong relationship is likely between the American ETC and its supplier, the level of investment necessary to compete against foreign trading company competitions for export sales will be low enough for the ETC to comfortably afford.

2. Financing muscle

We have called for the American ETC to have the ability to create substantial amounts of credit after studying the credit-creating capability of EMC's and Japanese ETC's. We are satisfied that a ten times net worth criterion is sufficient to insure that an American ETC will be competitive to any foreign trading company without undue risk.

3. Minimization of transactions costs

The costs necessary to make a sale directly influence the price you must charge above and beyond the cost of goods sold. These costs include financing costs, marketing costs, and transportation costs. We have considered these costs in three ways:

- the size of the marketing network required;

- the form of the recommendation to create credit; and

- the recommendation to permit profits on freight brokerage.

We believe that these recommendations go a long way toward maximizing competitive ability. There is no doubt, however, that the Japanese trading company and its tremendous scale will be more competitive in this regard. The disposition to compromise on the level of profit in any one sale or on all sales, as a major influence of the Japanese business mentality, is another factor an American ETC can not be expected to match unless it is a quasi-public enterprise.

On the whole, however, we believe that transaction costs for an American ETC will be low enough to be competitive and that financing and product quality considerations will hence predominate.

Emplacement in local markets

The historical development of the European trading companies was presented in Part II, Section 1. One very important point that was made was that European trading companies flourished in part because they "owned" the product end markets. Over the years, they developed very strong infrastructure to support a flow of goods from England to these market places and reinforced physical presence with giving a "piece" of the company to important local figures. This conduct is considered unacceptable for American ETC's.

We believe the best way to compete in this environment is to match investments in infrastructure as appropriate, with a strong credit-creating ability and let the quality of the goods do the rest. After conversations with representatives of a large British trading company, it was clear to us that such a strategy could produce satisfactory results, in general. It is our judgement that the global markets for U.S. goods are so huge that

there is room for a considerable number of new participants who are capitalized well enough to undertake the risks inherent in international marketing. Meeting the "requirements for success", as we define in Part II, Section III, is the appropriate way to utilize capital employed.

Model of an Export Trading Company

The subject of a model was an early focus of discussion between Messrs. Wilbourne and Heikenen of the Department of Commerce, and Mr. Cassano of Hay Associates. There was some difficulty in defining what the output of this model should be and what kind of detail was appropriate. No resolution of the difficulty emerged prior to Mr. Heikenen's transfer out of the Office of Export Development or Mr. Wilbourne's sudden illness.

Probably, the most appropriate and important relationship to model is the increase in export volume/product that would materialize with the presence of export trading companies. Further, we have recommended that trading companies possess a number of characteristics that lend themselves to quantitative evaluation.

- They possess the power to create substantial amounts of credit.
- They invest in a network of offices abroad.
- They must be capable of participating in third country trade.
- They invest in export support infrastructure to maximize marketing capability.

The consideration of these variables is complicated by the fact that for every industry, and every country in which the trading company participates, the sensitivity to these variables will differ. The sensitivity of export volume in a given industry for various countries is beyond the scope of this study. Exchange rates, tariff and non-tariff barriers, and the presence of bilateral

agreements between countries must be considered exogenous to the model as they will not be effected significantly by structural approaches to markets--that is, a trading company approach.

As we did not uncover any significant legal, financial or competitive constraints that will affect the export producing ability of trading companies that are not implicit to the four functions mentioned above, we can propose that the fundamental model of an ETC can be given in the following equation.

$$\Delta EXP = \sum_{i=1}^{B} \sum_{j=1}^{C} EXP_o \left(1 + \Delta E_{CR_{ij}} + \Delta E_{OFF_{ij}} + \Delta E_{TCT_{ij}} + \Delta E_{INFR_{ij}}\right)$$

where:

ΔEXP	=	increase in export product due to a trading company
B	=	the businesses in which the trading company participates
C	=	the countries in which the trading company participates
EXP_o	=	base case export product
$\Delta E_{CR_{ij}}$	=	sensitivity coefficient to credit issue in a given country and business
$\Delta E_{OFF_{ij}}$	=	sensitivity coefficient to presence of offices in a given country for a particular business
$\Delta E_{TCT_{ij}}$	=	sensitivity coefficient to third-country trade in specific industries or countries
$\Delta E_{INFR_{ij}}$	=	sensitivity coefficient to supporting infrastructure in particular industries or countries.

The increase in export product due to a trading company must then be summed over the number of trading companies to get the effect on U.S. export volume. The number of trading companies that would "naturally" be created by the private sector will be effected by the profitability and the risk associated with trading.

Toward this end, we have recommended that a policy to insure receivables be created to restrain exposed risk and profits on freight brokerage be permitted to allow profitability to increase. Constraints on the number of trading companies would be availability of qualified manpower and the disposition of manufacturers to use a trading company approach--major uncertainties at this time.

As mentioned previously, it was not the intent of this study to determine the degree of interest of the manufacturing community in a trading company approach. Yet the answer to this question is necessary to determine how many trading companies might be created and hence, the ultimate impact of such a structural mechanism on the U.S. economy. In the absence of such information the equation above could be examined microeconomically, by country and industry, to determine the maximum impact of the trading company approach.

Legislative Package

The statement of work called for us to develop draft legislation that would serve to move ahead the concept if such legislation was appropriate. As our conclusions and recommendations implicitly if not explicitly reveal, we do not believe any draft legislation is appropriate. There are two basic reasons which lead us to this judgement:

1. We uncovered no significant legal constraints on the concept. As a result of our legal investigations and conversations with current exporters, bankers and the Justice Department, the concept was not seen to be restricted in any way that would necessitate legislation. Such a structural form is capable of existing under U.S. law.

2. The constraints on the viability of the concept that do exist are severe enough to bear much closer examination and discussion before any legislation specifically related to supporting the concept would be worthwhile.

   We did not uncover even a glimmer of interest in the concept by manufacturers--only exporters and bankers. In addition, we did not find

enough evidence to support the conclusion that sufficient human resources were available to meet management requirements of the concept. One can not dismiss these problems. They are vital to the feasibility of the concept.

Furthermore, the most significant operational change needed to create viable trading companies is the need for such companies to have a substantial ability to create credit. Our investigations indicate that this change might be possible without any new legislation.

Thus, we reached the conclusion that draft legislation is inappropriate at this time.

HAY ASSOCIATES

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INTRODUCTION

The United States is a nation with enormous internal markets for goods and services. Consequently, the vast majority of citizens do not realize the significance of United States trade to the domestic economy. In 1975, United States exports of goods and services exceeded $147 billion, almost 10% of gross national product. Furthermore, growth in the importance of exports to GNP has been precipitous as it has risen from $67.5 billion, or about 6.4% of GNP since 1970. A similar trend has occurred with respect to imports. In 1975, imports of goods and services to the United States were in excess of $125 billion, over 8% of GNP. These facts show that the United States is today, more than ever before, a trader nation.

The consequences of the growth in international trade have had and will continue to have a profound impact on the United States economy. In the decade 1960 to 1970, United States exports in current dollars grew at an annual rate of 8.5%. But in the period 1970 to 1975, they grew at a rate of 18.7%. This latter rate is over two times as fast as the growth of the GNP during that period, demonstrating that export trade is one of the great growth sectors of the economy. The growth in exports during this period also helped ameliorate the impact of the worst recession the United States has experienced since World War II, and sustained growth will be important to reducing the impact of imports of oil as the economy develops. Therefore, it is of vital importance that American enterprise remain competitive or increase their capability to compete in world markets.

The reality of the business world today is vigorous competition between European, Japanese and North American companies that operate on an international basis. To successfully compete in global markets, United States companies must establish business operations around the world by one manner or another. There are numerous ways to structure global operations including the use of foreign-owned subsidiaries and joint venture teams.

One means frequently utilized by foreign-based enterprise to build international trade volume is the trading companies. In Japan, for example, the ten top trading conglomerates, the Sogo Shoshas, are responsible for approximately 60% of total imports and 50% of total exports. They are considered by many businessmen to be the world's most efficient marketing channel. They have, without doubt, made a substantial contribution to Japan's impressive postwar economic growth. Trading companies

have also played a significant role in achieving economic growth for many European countries as well as Great Britain over the course of time. Yet, despite the apparently successful utilization of trading companies to build international volume for foreign-based enterprise, trading companies have not flourished in the United States. The question that needs to be answered is why haven't these companies flourished in the United States and what needs to be done to create the necessary environment for them to exist if this course of action is appropriate.

Of concern to many parties in this country is the large proportion of American companies that do not participate in export trade. According to United States Department of Commerce figures slightly less than 10% of all manufacturing entities in the United States are involved in export trade--slightly over 30,000 firms. What about the other 280,000 manufacturers? Why don't they export? Could a trading company concept produce a significant increase in the number of exporting firms?

The primary objective of this study was to determine the feasibility of an Export Trading Company (ETC) concept as a viable vehicle for expanding United States exports. This concept envisages the creation of a corporate framework whereby United States companies--especially marginal and nonexporting manufacturers--can be joined together under the umbrella of "export trading companies," as exemplified by existing trading companies operated by the Japanese, British and Dutch. The purpose of the study was to provide information to the United States Government which would identify the problems inhibiting the operation of American export trading companies and recommend solutions as to laws, regulations and practices that would create the necessary environment for such companies to compete in world markets, if appropriate.

The specific goals of the project were to:

- identify reasons why trading companies have not flourished in the American commercial, banking and legal environment;
- examine the anti-trust implications and constraints for forming and operating United States trading companies;
- review the Webb-Pomerene Act as it applies to the concept;
- analyze banking regulations and procedures as they may constrain the development and operation of trading companies;

- review pending Congressional legislation which might affect the viability of the concept;
- establish competitive and market requirements which the trading company must meet; and
- provide an operational definition of an ETC, including its organizational structure.

Well over a hundred interviews with exporters, bankers, insurance executives, manufacturers, trade specialists, lawyers, executives of foreign-based trading companies, shippers and representatives of government agencies were conducted to get the information necessary to address the issues of concern. In addition, a comprehensive survey of over 80 Export Management Companies, about one-fifth of the total universe of firms, was made to document operating difficulties and procedures of the most common variety of independent export units in this country.

The methodology of the study is presented in Appendix A.

The first part of the report establishes the problems involved in initiating international trade. They are important to address because these are the problems the trading company concept must solve effectively and efficiently if it is to be considered viable. Thus, these problems in part establish some of the structural and operational characteristics the trading company must possess. Included in Part I is also a brief explanation of alternative means by which the problems are solved.

The second part of the report reviews the development of the trading company concept, the various forms of "independent export units" which exist, the necessary tasks a trading company must perform and the characteristics it must possess to operate successfully on a global basis. In addition, some comments are made as to why giant trading companies never developed in the United States.

The third part of this report examines the legal, competitive and market constraints which have inhibited the development of trading companies in the United States and suggests courses of action that are appropriate to overcome them--creating an environment in which trading companies might thrive.

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The fourth part of the report discusses in detail the characteristics of one of the prime trade vehicles currently utilized in the United States, the Export Management Company (EMC). It also discusses the problems and potentials they face in stimulating increased export trade from marginal or nonexporting small and medium-sized manufacturers.

The fifth section of the report contains concluding remarks and recommendations.

EXECUTIVE SUMMARY

PROBLEMS AND APPROACHES TO INTERNATIONAL TRADE

Even the smallest firms in the United States tend to be intimately familiar with the requirements for success in their industries. In contrast, the management of smaller firms is generally confronted with a multiplicity of different and unique problems when they consider exporting their products including:

- language barriers;
- documentation requirements;
- fluctuating and sometimes nonconvertible currencies;
- differences in marketing taste;
- increased working capital requirements.

Most company managements are aware of "horror stories" about firms trying to break into international trade and failing--often catastrophically. Thus, in order to get a substantial number of smaller manufacturers involved in exporting, three major obstacles must be overcome:

1) Interest in exporting on the part of company management must reach a level which is sufficient to motivate them to get involved. Companies must become convinced that exporting is a positive strategic move for them, offering an attractive opportunity for increased growth and profitability. Further, the company must find some way of coping with the resource allocation problems that entering such a different market entails. Management must consider human resources limitations, financial issues, capacity issues and the additional staff support burden.

2) Information and know-how about foreign markets and risks and the administrative activities peculiar to exporting must be acquired. The exporter must acquire information which will enable him to make sound decisions about foreign involvement. He must also consider how to approach the marketing task by considering the reasonable alternatives open to him

and developing the internal capability to deal with the problems that will emerge if he decides to undertake a foreign sales effort without any outside assistance.

3) Sufficient experience must be gained in exporting to make this part of the company's business stable and important and hence warranting "permanent" investment. Without a successful market penetration effort which results in a stable sales volume, companies are not going to sustain their interest in exporting when the domestic market is booming. Such penetration will eventually require substantial specialized marketing and distribution capability.

The two fundamental approaches available to manufacturers considering exporting are to go it alone--distribute directly, or to employ some outside agency to build sales for him--indirect distribution. Within each approach, there are two options:

- Indirect Distribution
  - Sales through an organizer--companies or associations which come to the manufacturer with opportunities to sell abroad as a supplier to a larger effort.
  - Sales through indirect distributors--various independent export units such as Export Management Companies.
- Direct Distribution
  - Sales through foreign distributors--independent or exclusive local agents in a foreign market who in turn sell the goods to ultimate end-users.
  - Sales directly to foreign end-users--through a company owned distribution system, licensing agreements or joint ventures.

Each of these options has advantages and disadvantages of a cost, control and results nature. Importantly, among United States manufacturers the overwhelming tendency is to "go it alone" as soon as sales momentum starts to build. This decision, however, is not made without due consideration of what it is going to cost. Manufacturers want control over their marketing effort.

Of great importance to the feasibility of an American Export Trading Company concept is that control is least and hence easier to get in the earliest stages of export involvement, but gets increasingly difficult to wrest from the manufacturer after that. In the initial stage of foreign market penetration the economic and resource limitations of smaller companies naturally create the opportunity for domestic penetration by a trading company mechanism.

THE TRADING COMPANY CONCEPT

Throughout the world's commercial history, trading companies have been an important channel for the flow of goods--linked to the needs of merchants to pool risks. But the real impetus for trading companies began with the theory of mercantilism which spread across Europe during the 16th, 17th and 18th Centuries. With mercantilism, which included the concept of "the favorable trade balance" came the need for colonies. But the capital and risks to that capital necessary to colonize an empire and create trade were greater than any individual's capability. Thus the first joint-stock companies--trading companies--were formed to enable groups of investors and merchants to pool capital and distribute risk.

The strong commitment to the mercantilistic policies of the era had pushed the European powers, and even the United States, into Asia by the mid-nineteenth century. A threat to Japan's national survival directly influenced the creation and development of its unique general trading companies. This threat led a group of men to overthrow their government and begin to build a strong industrial sector capable of building modern weapons. In 1880, the government decided to divest itself of the enterprises it had initiated and chose a small group of business families, close to the government, to sell out to. These family businessmen gradually developed huge self-sufficient integrated industrial groups known as the Zaibatsu--run by a closely owned holding company and utilizing a trading company to distribute the companies' products.

In time, the majority of Japan's industrial distribution was handled by trading companies and manufacturers tended to perform only the production function. Because of the enormous diversification and safety of their portfolios, trading companies came to control the disposition of credit to smaller firms--in essence, controlling their existence.

Unlike the Japanese trading companies that grew through controlling manufacturers, European trading companies grew by controlling end markets--the avenues of industrial growth. But in no case did a trading company grow in a country where export trade was not considered vital. Most importantly, trading companies did not tend to emerge as a result of the interest of manufacturers but rather from some outside source.

Types of Trading Vehicles

Trading companies are just one form of independent export unit. Despite numerous variations, all independent export units can be considered as one of three types:

1) Associative Types

2) Middleman Types

3) Integrated Types

Associative export units are typically sales organizations acting on behalf of groups of firms in the same industry solely to generate foreign business. The most well-known examples of these organizations are Webb-Pomerene associations. While they have been quite common in the United States, their success, if measured by their continuity, is small. Of over 260 associations created since 1918, only 34 are in existence today.

Middleman export units are firms which act as commission representatives or export distributors for several firms, typically in allied but noncompetitive businesses. Over 1000 of these firms are thought to exist in the United States today. The most common variety of them are known as Export Management Companies.

Integrated export units are best exemplified by the British and Japanese trading companies. They combine middleman functions for a larger number of industries with extensive investments in foreign offices, warehousing, fabrication facilities and strong financial clout. Such companies are almost nonexistent in the United States. None in the United States match the size of their foreign counterparts.

Requirements for Success

It is our judgment that an American Export Trading Company is going to have to meet six fundamental criteria:

1) it must have strong ties to manufacturers;

2) it must have product specialist capabilities;

3) it must have a strong foreign sales network under its control;

4) it must have depth and continuity of management;

5) it must have the ability to create substantial amounts of credit;

6) it must have sufficient diversity of product and markets.

We consider each of these factors vital and without even one of them, we strongly believe that the ETC concept will fail.

General Economic Factors Contributing to the Absence of Trading Companies in the United States

A rigorous economic analysis of why trading companies never developed in the United States was beyond the scope of this study; however, four factors were established that have had a significant impact.

1) The availability of natural resources in the United States eliminated the need of mercantilistic policies. The country has been generally self-sufficient for the bulk of its needs over its entire history.

2) The industrial revolution emerged early in the United States which made the efficient acquisition and distribution of goods relatively easy and reduced the dependency on imports even further.

3) The size of the domestic market meant that manufacturers had ample growth opportunities at relatively lower risk.

4) The profit center concept of organizing American corporations resulted in dysfunctional situations when trading company concepts were applied to large manufacturing operations.

CONSTRAINTS TO FORMING TRADING COMPANIES IN THE UNITED STATES TODAY

There are three basic kinds of constraints to the formation of trading companies: legal, market and competitive, and financial.

Legal Constraints. The Webb-Pomerene Export Trade Act provides the legal basis for an American Export Trading Company concept; however, it does not provide a legal basis for enforcing the require-

ments for a successful trading company. Specifically, it does not provide a legal basis for requiring companies to remain associated with the trading company for an extended period of time, or for selling their products solely to the trading company. The Act does provide sufficient freedom to act as long as the domestic market share of association members in specific industries is not excessive.

In addition we did not find any legislation which prevented the formation of vertical associations of businesses as long as they do not restrain the trade of competitors or monopolize the lines of commerce.

Competitive and Market Constraints. We basically found no competitive or market constraints which have prevented trading companies from existing in the United States. However, the desire by American manufacturers to control markets themselves creates the need for a trading company to have significant marketing capability in foreign markets if it is to maintain an extended relationship with a manufacturer. Without this extended relationship it is impossible for a trading company to acquire competitive capability in the marketplace. The need to have a significant marketing capability leads to the need for the trading company to be "big."

Financial Constraints. There are substantial financial constraints affecting the ability to create a successful trading company in the United States. The financial constraints impact on the ability of the trading company to create credit and provide an adequate return on investment. In the United States, the ability of a company to create credit is strongly related to the level of its net worth. In relation to sales potential, a trading company requires a relatively low net worth: thus, this situation translates into a relatively small ability to create credit, almost regardless of the credit worthiness of the foreign buyer. Without this ability we believe the trading company concept is not feasible in the U.S

The net result of the problem will require that the United States Government support the ETC concept. We believe it could be accomplished through an extension of guarantee insurance programs provided by FCIA or OPIC; however, at this time we find little support for this device within the government.

There are also other constraints, such as the inability of a trading company to participate in profits on freight brokerage which detract from the profitability of the business.

THE EXPORT MANAGEMENT COMPANY

In general, the Export Management Company (EMC) is a firm that acts as the exporting arm for a combination of manufacturers, dealing under its own name or the name of individual manufacturers. It is the most common form of independent export unit found in the United States. It can be characterized as small, profitable, efficient, undercapitalized and run by entrepreneurs who are generally risk adverse, not inclined to build vertically or use DISC or FCIA mechanisms.

EMC's are usually run by people with a good knowledge of specific products and methods of international distribution, knowledge of problems in international trade and have good credit histories. However, they have very high unit costs, are deficient in personnel depth and hence lack long-run continuity and provide limited marketing services beyond selling.

With certain exceptions, we do not believe that the EMC provides the basis in management skills and distribution networks on which to build a viable trading company.

CONCLUSIONS

We believe a trading company concept is a viable means of conducting international business in the last quarter of the twentieth century and expanding exports from smaller manufacturers. We do not believe, however, that the umbrella concept, which envisions groups of manufacturers coming together to form export associations, can be made to work.

We believe that the incentive and capital for an American Export Trading Company must come from outside the manufacturing sector and it must be operationally characterized as follows:

1) it is integrated in nature and hence more than simply a trader;

2) it deals in imports and third-country trade as well as exports;

3) it is substantially diversified on a product and geographic basis and is a medium-sized business inself;

4) it is a strong financial, as well as marketing, vehicle;

5) it acts as an independent international department in its dealings with suppliers;

o) it is structured to consist of a head office where business unit management, administrative and other staff activities are performed; a small network of strategically located offices globally dispersed; and a network of branches, agencies, distributors and correspondents as appropriate to cover individual markets.

It is our judgment that a trading company which meets these characteristics can overcome the problems involved in initiatiating exports from small and medium-sized manufacturers. However, it may be necessary for an American Export Trading Company as we have designed it to be a quasi-public institution.

Despite our conviction that the ETC concept as we have defined it is a viable means of expanding trade, we are sceptical as to the feasibility of implementing the concept. Three major problems lead us to this position:

1) The need for manufacturer support - We uncovered virtually no support for a trading company concept among manufacturers.

2) The need for management expertise - We are stymied as to where the expertise necessary to run these companies might come from.

3) The need for government support - A consistent, coherent and supportive United States international economic policy is absolutely necessary and appears nonexistent.

RECOMMENDATIONS

1. Conduct a survey to establish the interest of manufacturers in the concept.

2. Develop an FCIA/EX-IM guarantee insurance policy which would give hold harmless protection to drafts of selected trading intermediaries and provide a means of creating credit.

3. Test the complete concept on two or three of the largest export management companies.

4. Remove the inability to participate in profits from freight brokerage from all independent export units.

5. Assist the EMC's in establishing standards and a uniform code of conduct.

PART I

PROBLEMS AND APPROACHES TO INTERNATIONAL TRADE

During the course of this study over thirty small and medium sized manufacturers were interviewed. These firms manufactured products in a wide variety of SIC classifications and consisted of nonexporters, marginal exporters and firms where exports comprised up to 40 percent of total sales. We also spoke to several individuals who have conducted surveys on problems in export expansion and reviewed the findings of their studies.

While the number of interviews conducted by ourselves and others is not statistically large, we believe that the findings of our work are representative of the concerns about export expansion of the smaller manufacturer.

The first part of this report explores the problems any firm desiring to participate in sales of goods (or services) to foreign countries must overcome. We discuss in some detail the factors which contribute to each of the problems and the various decision areas or technical area which relate to them. We will also discuss the approaches to foreign trade most commonly utilized by smaller manufacturers and the advantages and disadvantages of each.

SECTION 1

PROBLEMS OF INITIATING INTERNATIONAL TRADE

Most smaller firms are thoroughly familiar with the requirements for success in their industry in the United States. They understand the demands of the particular group of customers which must be offered, its style, quality, price and a host of other factors. Sales executives understand the channels of distribution through which the product moves on its way from the factory to the customer. In most cases, they have extensive knowledge of individuals and firms operating in the channels of distribution. These executives have a grasp of the importance of advertising and promotion, of the most effective media, of the level of promotional expenditure which has proved most satisfactory. Living in the shadow of government regulations has become second nature and management is familiar with whatever laws influence the firm's operations.

This vast store of knowledge about conditions for success in their United States industry usually results from the collective years of experience found in the smaller firm's management team.

In contrast, what is known about conditions for success in foreign markets? Smaller company managements usually have little or no experience there. The language is different. The currencies are different, fluctuate in value, and in some cases are not convertible. Nothing is known about whether markets exist for the company's products and so on.

Deciding to enter foreign markets is very difficult without any knowledge or experience. Some companies have gained experience by being suppliers to large projects organized by others. In some cases, licensing agreements were established years ago which over time produced managers with some level of comfort with foreign markets. And when the time came to expand beyond these original commitments, the decisions were less traumatic. But for most, who have yet to take their initial step, the area is frought with uncertainty.

In the process of initiating and developing an export business, there are three major obstacles which a management must overcome.

Problem 1 — Interest in exporting on the part of the company management must reach a level which is sufficient to motivate management to make important resource allocation decisions. The resources in the case of the small manufacturer may not be large in absolute terms but are significant nonetheless. Going into exporting is a critical strategic decision and will be made very carefully.

Problem 2 — Information and know-how about foreign markets and risks and the administrative activities peculiar to exporting must be acquired. Once a company management has decided to seek export business, there is a formidable hurdle getting enough information to decide where to begin--what markets--and how to go about it. Problems of understanding language and customs, identifying agents, acquiring the skills to provide necessary documentation, etc. when taken together, provide a real challenge for a small company. Also, the additional or different financing required is troublesome. This information and know-how area is the one where most have focused who have tried to help small companies export.

Problem 3 Sufficient experience must be gained in exporting so that foreign markets can become a stable and important enough part of the business to warrant "permanent" investment. At some point in their development, export markets either become established as a critical element in the company's future plans or are deemphasized as being of strategic importance. When a company reaches the point where it determines that exporting is attractive, its needs undergo a dramatic escalation. Here is where development of management capability and investment in people and facilities dedicated to exporting are needed to achieve potential and sustain growth. At this point today, companies see no alternative to going it alone.

The significance of recognizing and understanding these problems or critical points in the initiation and development of international trade is that they become the focal points for possible injection of help of one kind or another. In relation to an American Export Trading Company, these problems become requirements which any viable trading company concept will have to be responsive.

Each of these three problem areas will be discussed in some detail. The objective of the discussion will be to explain more fully the nature of the problems or needs of the small business and develop a basis for what an ETC must do in regard to each problem. Exhibit I-1 indicates the various decision areas or technical areas that will be discussed.

Problem 1: INTEREST IN EXPORTING

A. One of the major obstacles to dramatically increasing the numbers of small exporting companies is proving to these companies that exporting is a positive strategic move for them. Companies which have decided that they will benefit from export markets will not be denied. Those which have not thought about it or are uncertain need a lot of pursuading. While this may seem like a useless generalization, the fact is that this is the fundamental problem for many nonexporting companies. At one point in our study, we randomly called approximately 40 firms with under $50 million in sales who attended a meeting sponsored by the New York Regional Office of the Department of Commerce. The purpose of the meeting was to get together "interested" marginal or nonexporting manufacturers, export management company representatives, other export professionals, and speakers in an attempt to help these manufacturers start or increase their exporting effort. The interest of these firms was indicated by their decision to attend the meeting.

PROBLEMS FACING SMALL COMPANIES IN INITIATING AND DEVELOPING INTERNATIONAL TRADE

DECISION AND ACTIVITY AREAS

Problem 1: INTEREST IN EXPORTING

Decision Areas:
- Recognition of strategic value of export markets
- Allocation of resources to exporting
- Decision to enter

Problem 2: INFORMATION AND KNOW-HOW ACQUISITION

Activity Areas:
- Marketing Intelligence
- Market Development
- Financing
- Insurance
- Transportation
- Documentation

Decision Areas:
- Level of activity
- Method of market development

Problem 3: "PERMANENT" INVESTMENT IN EXPORTING

Decision Areas:
- Commitment of additional resources
- Method of further development

Activity Areas:
- Development/acquisition of management
- Development/acquisition of specialists
- Dedicated facilities

EXHIBIT I-1

While the meeting may have been an overall sucess, we found in our conversations with participants that almost 30 out of the approximate 40 firms we called were not at all interested in exporting--but only curious and were not influenced at all by the proceedings. Furthermore, a substantial number of the marginally exporting companies (less than 10 percent of corporate sales) international sales managers we talked to over the course of this study cited major problems at getting senior management committed to expanding international programs.

As a result of our total interviewing experience, there is little evidence that there have been any effective programs to help marginal and nonexporting firms come to a positive decision about exporting. There are a number of factors which contribute to what we label "lack of interest" which must be faced.

1) Exporting must be viewed as offering an attractive strategic opportunity which will result in increased sales and profits. Some companies reach this conclusion defensively, i.e. they run out of markets for their products domestically and look for new markets which will enable them to maintain their momentum. These are the companies which will get into the export business aggressively with a willingness to take risks. They have something to gain and they know it. Perhaps it would have been advisable for many of those companies to seek export business earlier, but as long as there are untapped markets at home they generally do not look abroad.

   Some companies are introduced to export markets gradually so that the decision to export more aggressively is easier--there is less uncertainty for them as they have gained some comfort and experience. But the decision to actively seek exports is still one that they will have to be convinced is right for business reasons. They are convinced by their experience whereby they see that export business is an attractive relative opportunity; or, like the companies described earlier, they develop to the point where they need new markets. "Organizers" and Export Management Companies (EMC's) play an important role here because they offer the company an opportunity to get their feet wet.

In any event, the management of these companies must come to the point where they believe that export markets are a source of desirable business which they cannot afford to ignore.

2) Management must accept the fact that exporting requires a diversion or reallocation of resources. However modest the resources that must be devoted to exporting seem to an outsider, the decisions are of major consequence for a small manufacturer. Important considerations include:

- Management Time

  Because of the risks and uncertainities and its high visability, the exporting activity demands management time.

- Financing

  Whether it be debt or equity capital, exporting absorbs financing capability. In addition, because of the longer payback periods and risk, the financial aspects of business become more complicated.

- Capacity

  Output that is diverted to exporting is not available for domestic markets. This is of particular concern when a company has not yet reached the limits of its markets at home.

- Staff Support

  The comparatively onerous paperwork requirements of export business require reassignment or addition of clerical and staff help. For small companies often undermanned this can be problematical.

Commitments to export is difficult to establish in the non-exporting firm and the difficulty is compounded by the uncertainty of dealing in far-away places. Management must have a strong conviction that the allocations will be worthwhile.

3) Any program to increase the number of small and medium-sized exporting companies must include a method for helping manufacturers recognize and evaluate the potential of export on their business. The exposure represented by exporting is significant for small businesses. While the decisions described here are the same for large and small businesses, the exposure is a much greater concern to the managements of the smaller enterprises. The consequences for small companies are that the decisions to enter export markets will be made much more conservatively and the rate of expansion in the early phases will be controlled much more closely. Most of the efforts which have been directed at these companies have dealt with how to begin exporting rather than whether to export. For those who could benefit from exporting, the advantages should be pointed out early and in a convincing way.

Problem 2: INFORMATION AND KNOW-HOW ACQUISITION

B. The next major obstacle to companies who have decided to export is to acquire the knowledge and skill necessary to select the best market opportunities and carry out the exporting process. The knowledge and skill required to export is not a natural extension of the processes perfected to serve the domestic markets. Language, currency, political risk, lack of understanding and affinity for foreign markets represent challenges which require new skills and attitudes.

Aside from these underlying differences, these are specific capabilities required which relate to exporting. These fall into three categories: informational, relating to developing data about foreign market opportunities; financial, understanding and using special export-related financing vehicles; and, technical, relating to the specialized "back office" requirements of exporting.

1) The exporter must acquire information which will enable him to make sound decisions about foreign sales opportunities. Which markets around the world have potential? Which one or ones should be approached first? These are the questions the small or medium-sized manufacturer must be in a position to answer. To do this, he must have data about the same kinds of

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issues as for his domestic markets. For a variety of reasons the manufacturer can rarely rely on his own experience and data sources are not as readily available. The Department of Commerce provides data about foreign markets, but often, particularly in the case of small specialized manufacturers, the data is too broad and general to be of any use. The kinds of market intelligence data which are needed are for each product to be exported in each geographical market or country include:

- End-Users

  Identification of the final users of the product including whatever data would define the market need.

- Buying Practices

  The requirements of users which the exporter must satisfy and the methods by which customers make purchasing decisions with which the exporter will need to conform.

- Potential Size and Growth

  The size in units and value of the market represented by the aggregate of end-users; also, the rate at which the market is expected to grow.

- Competition

  The competitors in the market, both other exporters and domestic companies; this includes an understanding of competitive capabilities and market shares.

- Market Structure

  The levels of distributions present and the ways in which the markets operate.

- Trade Considerations

  Tariff and nontariff barriers, country attitudes, risks, etc. associated with a particular country/market; these are factors which are unique to exporting which a new exporter will learn to have to understand and deal with--particularly since they are of overriding importance.

- Trends

  Changes that are taking place in the market, in terms of competitors, market structure buying practices, trade conditions, etc.

2) The exporter must decide how to approach the market by evaluating the reasonable alternatives available. There are essentially two fundamental options for the firm to consider: performing the marketing activities itself or letting someone else perform them for it. The decision or approach will usually require a trade-off between the cost of marketing and the desire to control the marketing effort. A detailed examination of the exporter's options appears in Part 1, Section II.

   Less than 15% of the manufacturers we interviewed began their exporting by utilizing a direct approach: generally, because the approach required too great a leap forward in understanding and capability and too great an investment. In fact, even when the smaller sized manufacturer has established a program important enough to warrant a permanent staff working in a foreign market, they often choose to retain foreign agents so as to take full advantage of their knowledge of the market.

3) The exporter must develop the capability to meet the unique financial requirements of exporting which include different risks, broader use of intermediaries, longer payment periods and usually the need for additional working capital and capital investment. Beyond the uncertainties that require thoroughly investigating foreign markets, the small or medium-sized company considering exporting will be faced with a new and unsettling set of problems in the area where he is usually weakest--finance. He will see new risks he doesn't understand or like, new financing vehicles

and attitudes in the financial community, perhaps the need for additional funds and sometimes lower margins. What seemed like a good decision may now appear to be more trouble than it is worth. More specifically, the new exporter is confronted with:

- A Different Risk Matrix

  The manufacturer not only is confronted with higher marketing risks as a result of selling in an area where he may not fully be aware of customs and practices, but often he must accept greater commercial risks in dealing with foreign buyers. In cases of dispute, legal problems of settlement can be complex. The manufacturer must also contend with foreign exchange risk which can wipe out or dramatically increase the profitability of his sales without much forewarning. There is also the problem of political intervention in his business, the creation of tariff or nontariff barriers which will have a dramatic impact on his sales volume and hence the stability of his business.

- Broader Use of Intermediaries

  In contrast to domestic business, the bulk of United States international trade is financed by commercial banks. Only a small amount of business to foreign businesses is done on open account or consignment. The increasing use of banking services is also accompanied by a corresponding increase in documentation of all kinds. There are, of course, charges for the use of these services, which are unnecessary in a domestic transaction, increasing the unit costs of international sales.

- Longer Payment Periods

  Most goods destined for foreign markets are shipped by sea. The bulk of financing arrangements call for payment no sooner than the

goods are accepted by the buyer after arrival. The result is that delays in payment up to six months or more are not uncommon. These delays are often extremely difficult for the small manufacturer to cope with.

- Working Capital and Increased Investment

  A direct outcome of longer payment periods is the need for a greater level of working capital. The need for specialized staff and greater use of intermediaries also increase the normal costs of doing business. Often, however, additional capital investment is called for to support an international sales effort, be that in the form of offices or tools for such purposes as metrication of the product.

- Margins

  Generalities cannot be made about whether export is more or less profitable than domestic business. Research indicates that results are mixed--some businesses indicate greater margins for products sold in foreign markets compared to domestic and some indicate lesser margins. The findings are different from company to company and vary over time. However, there are costs associated with exporting which either exceed or are in addition to those for domestic markets. In a Conference Board Study a comparison of export marketing services and costs between domestic and international activities was made. Among the areas where exporting affected margins were:

  - greater promotional expense in advertising required and for market coverage;

  - higher discounts and commissions, five to eight percent more for foreign agents and distributors;

- high costs of ocean freight, sometimes accounting for as much as 25 to 30% of the final price to the consumer;
- costs of landing merchandise in the foreign port;
- greater amounts of paperwork.

Of course, these costs can and often are offset by higher prices which can be realized in foreign markets thereby allowing the export business to be more profitable. At the same time there are companies exporting who price below full cost for any number of reasons.

For the beginning company in exporting, the decision as to whether to export will be affected greatly by the company's evaluation of costs and achievable margins. To the extent that management makes the wrong assumptions and comes to the wrong conclusions, the decision to export is likely to be a negative one.

4) The exporter must have access to or develop the capability to carry out the specialized functions necessary to support export activity: transportation, insurance, documentation. There is a body of specialized know-how necessary to export. While this knowledge is easy to acquire and can be applied by fairly low level personnel it must be either provided by third parties such as indirect distributors or organizers, or in-house capabilities must be developed.

- Transportation

  It is a complicated task. There are hundreds of ocean shipping rates by commodity which change frequently, which differ in market area and direction of trade. It is time-consuming and costly to keep up with all changes and utilize them to best advantage.

- Insurance

  There are insurance policies to cover maritime risks, damage in shipping and on political and commercial default of foreign

buyers. The availability sometimes depends on the country and product--and is costly, and ability to modify terms as a result of business curriculum may be limited.

- Documentation

There can be an enormous number of documents involved in international trade which must be compiled, complied with, and maintained including bills of lading, import licenses, supporting data for compliance with various government sponsored programs such as FCIA, other insurance policies for maritime risks and other documents necessary to support letters of credit when required. To avoid payment delays, documentation must conform precisely to the terms and conditions of sale and this documentation must be carefully prepared for each international transaction.

Problem 3: "PERMANENT" INVESTMENT IN EXPORTING

C. After a company has gained some experience in exporting, it faces the decision as to whether to make more permanent investments to develop export business. As has been discussed earlier, most companies start small and many start using third parties, i.e. indirect distribution or organizers. If all goes well, and export business proves to be profitable and offer good growth potential, management finds itself with the question of whether to intensify efforts and make a greater investment in people and facilities. At the same time, it expands the amount of management attention it develops to foreign markets.

1) Intensifying export activities beyond beginning levels usually involves a shift from indirect to direct distribution. When companies become convinced of the potential of exports, they become jealous of the fees paid to third parties and seek to retain these fees for themselves as profits. They also conclude that they can promote their products better by developing their own marketing staff capability. This is the time when the relationship between the company and an indirect distributor who may be serving him becomes troubled.

Exhibit I-2 uses the product life cycle to demonstrate the development of international markets where indirect distribution (where the firm uses outside marketing assistance to sell abroad) is chosen for the Introductory Phase; it is often rejected at the beginning of the Results Phase. The "rule of thumb" used is that when sales revenues in exports reach the $1 million level, the manufacturer "goes it alone"; that is, he decides to use direct distribution. This break with the intermediary results from his objective to gain control, maximize his returns and his willingness to begin to invest in a permanent exporting capability.

2) The shift to direct distribution requires the development of marketing and support organizations and a management capability. Depending upon the method of market development selected by the manufacturer, a marketing organization of greater or lesser proportions must be established. When a manufacturer selects an indirect approach, almost no additional marketing organization is required. Once a decision to go direct is made, a marketing staff will need to be created; this is usually comprised of an international marketing manager, several sales people traveling out of the United States and adequate clerical staff. Once this change has occurred the nature of the development of the exporting activity changes--it now becomes a question of efficiencies, the quality of effort and the rate of development that is desired.

EARLY PHASES IN THE DEVELOPMENT OF
INTERNATIONAL TRADE COMPANY MANAGEMENT OBJECTIVES

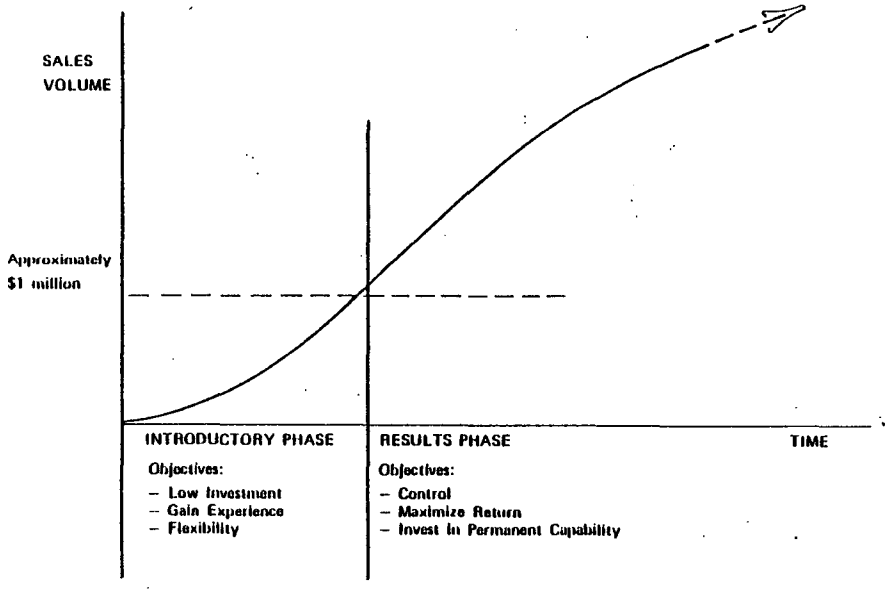

EXHIBIT I-2

SECTION 2

ALTERNATIVE MEANS OF PARTICIPATION

The two fundamental approaches to export marketing, direct and indirect, were introduced in Section I. This section will expand on the approaches and overlay the concerns of smaller manufacturers in utilizing each. Because the normal development pattern of international business in the United States ends in foreign direct investment, a few comments about this activity are also required. In fact, exporting usually continues in this final stage of development since direct involvement in foreign markets usually means export of parts or sub-assemblies and often the development of new export markets for products that had been previously limited to domestic markets.

A. There are four options for the potential exporter to consider, not all of which may be realistic for many products or companies initially. The four options for approaching exports are discussed below in ascending order of resource commitment. The first two options correspond to the indirect approach, the second two options correspond to the direct approach.

1) Sales through an "organizer". This type of exporting is an effective way for a company to begin but is not one over which the company usually has much control. Essentially, the organizers come to the companies with opportunities to sell abroad as a subcontractor or supplier to a larger effort. The organizer has taken care of finding the customer and will be responsible for handling the financing abroad, shipping, etc. So while this is export business, from the standpoint of the small manufacturer, it makes few of the demands that actual exporting would. Organizers are generally larger companies including Trading Companies putting together packages of products into systems or turnkey projects. However, for the purposes of this analysis, included in this category are all forms of unsolicited orders.

For the substantial majority of firms we interviewed that are currently exporting, the unsolicited orders from companies operating abroad--foreign as well as domestic --represented the initial exposure to international trade.

2) Sales through indirect distributors. Indirect distributors include Export Management Companies (EMC's) and Piggyback Exporters (American manufacturers who distribute noncompetitive products of the manufacturers through their established distribution systems). From the standpoint of the small company, they provide a way to get exposure in foreign markets without having to engage in any of the market intelligence activities outlined above. In both cases, the indirect distributors act as the marketing department covering all activity in specified markets. Piggybackers and EMC's have been effective in getting small and medium-sized companies involved in exporting. In some cases these relationships are begun by the EMC's or piggybackers seeking products of specific kinds or seeking specific manufacturers. In the case of EMC's, the manufacturer can initiate the relationship if he learns about their services, identifies those who would be interested in his products, and chooses to use this method of distribution.

3) Sales through direct distributors. The small company also has the option of going through direct distributors, that is, identifying and enlisting agents in foreign markets with whom he will deal directly. To do this properly, however, the company must go through the market evaluation and selection steps described previously as well as search for and decide on agents. Generally, these are time-consuming and formidable tasks which cause the company to delay entry into foreign markets--for reasons discussed earlier--or do such a poor job of entry that the export effort is discouraged and abandoned. This option is one where the company has total freedom to select whatever levels of activity are appropriate and whatever markets and agents. It is most successful when the person in the company directing the effort has had substantial experience in the appropriate product/markets abroad.

4) Sales direct to end-users. This option can be executed in several ways. Companies can enter into licensing agreements with foreign manufacturers which generally enable the domestic company to participate in foreign markets without concern for much of special services normally required with shipment of goods. The experience of many companies, however, is that these prove not to be satisfactory arrangements and often the ability to capture market potential is lost. Many firms who have licensed have found that they have created a competitor in the process. A second option for achieving direct distribution is joint venturing with a foreign firm, be it a manufacturer or a distributor. This again enables the domestic partner to reduce the amount of export-related work that is required by transferring it to the foreign partner. The third and most extreme situation is where the company involves itself directly in the foreign markets with the end-users. This involvement may vary from sending traveling salesmen from United States offices--to having permanent staff and facilities in foreign markets.

The four options of approach are arrayed in Exhibit I-3. The methods of participation are related in this Exhibit to the phases of export development which we describe as the Introductory Phase, the Results Phase, and the Investment Phase. The first two of these phases were discussed briefly earlier. The third phase is added to help define the period in which a company seeks to consolidate its successes from earlier efforts and leverage its position in the export markets by investing in permanent facilities in foreign markets to establish its presence. Until a company makes such investments, it can never have a solid foothold preventing free and easy entry by other competitors.

The significance of looking at the full range of alternatives and the pattern of development of exporting and international business in this way is to better understand where and how an American Export Trading Company concept will need to fit in. An Export Trading Company must aid management in achieving their objectives, must substitute or supplement organizational capabilities and must fit into or alter in a natural way the normal pattern of flow of development of export activities.

PHASES OF EXPORT DEVELOPMENT

COMPARED TO METHODS OF PARTICIPATION AND ORGANIZATIONAL CAPABILITIES

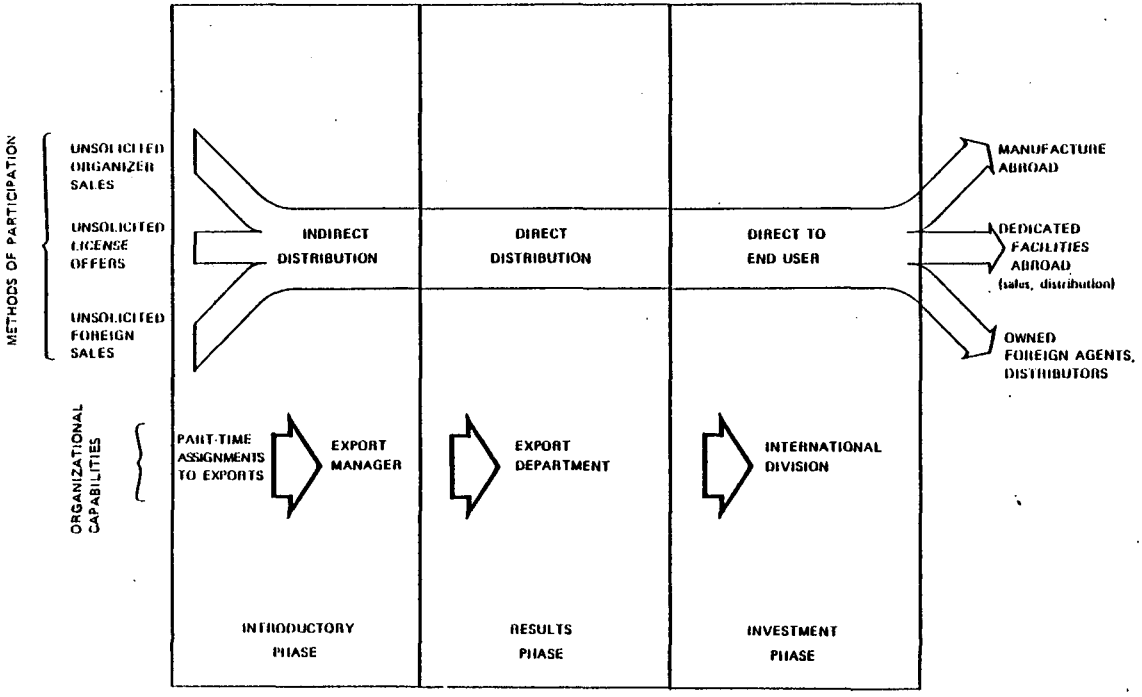

EXHIBIT I-3

B. As soon as he can see momentum building in exports, the American manager will opt for "going it alone" in order to gain control over activity and profit. This shift which probably takes place sooner than it should in many cases is as much a sociological phenomenon as a careful, analytical, decision-making process. Undoubtedly, American managers are different than others in other parts of the world in this regard and certainly their attitude contributes to the lack of prosperity of a "trading class." Time and time again this theme comes through while discussing the Export Trading Company concept with manufacturers, small and big alike.

Nonetheless, in deciding among the alternative ways to begin and develop the potential of international markets, the management of a small company must prioritize and choose based on considerations of cost, control and requirements on management time. Exhibit I-4 highlights the advantages and disadvantages of the alternative methods of developing markets in these terms.

C. The cost of exporting is perceived by manufacturers as related to control: "At what cost will it pay to do it ourselves?". The cost per unit of goods exported begins low, rises, and then declines as the exporter moves from indirect to direct distribution and grows to achieve scale economies. In absolute terms, the cost of exporting rises through the same steps.

Since the exporter desires to control the export activity at the earliest opportunity, he decides to switch as soon as the absolute cost of the commission reaches a point which he thinks equates to hiring his own export manager or sales force. He uses as a rationale that a full-time person could provide better coverage than the indirect distribution. But very often the real motivation is simply to depend on fewer intermediaries--and share the proceeds with fewer people. This tendency is undoubtedly underscored by the low level of performance of the intermediaries who themselves are often small organizations of limited time and talent.

SUMMARY OF EXPORT MARKET DEVELOPMENT ALTERNATIVES

ADVANTAGES & DISADVANTAGES

	COST	CONTROL	REQUIREMENTS ON MANAGEMENT
Sales through Organizer	– Favorable margins although these may be controlled by organizer – costs minimized, however.	– Dependence on organizer to develop business opportunities	– Minimal beyond what would be required normally when working as a subcontractor
Indirect Distributors	– Commissions are largest of any alternative – additional layer – Commissions less than costs of direct distribution below certain volume level points.	– Minimal control over level of activity or exposure in markets – a primary advantage	– Minimal time required, true in marketing areas particularly – a primary advantage
Direct Distributors	– May cost more than indirect at early stages – Tradeoff is increased control	– Much greater control than through indirect channels. – Increased control is primary reason most choose direct distribution. – Control limited still by dependency on foreign agents, however	– Dramatically increased requirements since management must oversee all functions of exporting – Tradeoff is control
Direct to End User	– Highest cost since this requires extensive market coverage – Usually one used in advanced exporting programs, however, with scale or potential	– Maximum control, even when foreign agents are used in parallel with direct efforts.	– Maximum time required since management must oversee full-scale marketing effort, large volume exports, perhaps warehouses, manufacturing facilities, etc.

EXHIBIT I-4

D. The control over exports is least in the early stages and increases in every stage after that. Because of initial uncertainty, stability and commitment to exporting, companies tend to consider the indirect distribution as a way to get started--and a rather unnatural, certainly temporary, state of affairs. As we will document in Part IV, this is a well-known fact of life for Export Management Companies, but it is also a critical cause of the absence of a more influential trading segment in our economy. Because there is a natural ceiling on the size to which most companies will grow under a trading intermediary, the EMC, for example, cannot benefit from any of the scale economies of its customers. EMC's must always deal in many small accounts and must always expend significant effort in developing new relationships with manufacturers to replenish those "graduating" from the other end. Unless a trading company can increase its longevity with customers through greater and visible competency or through clearly lower unit costs, it will fall prey to the same limiting factors. The central notion is control as the dominant consideration of United States managers actions. Any successful program to affect exports must understand this phenomenon and accommodate it.

E. The requirements for management expertise and time increases as indirect distribution is replaced with direct distribution and eventually marketing directly with customers. To a large extent, indirect distributors, organizers and licensing arrangements can be "management for hire." The exporter using these vehicles needs to make only certain strategic decisions and then can turn over much of the implementation to the intermediary. At first, management is one of the scarcest resources for the small company, and they are anxious to have significant help. But as exporting proves itself and the decisions are made to take control, the companies are more than willing to create management positions and the evolution of the management process occurs.

At this point in the report it is thus clear that the best time for a trading intermediary to approach a manufacturer to offer his services is before the manufacturer starts exporting and establishes control over the marketing effort. In the initial stage of foreign market penetration the economic and resource limitations of smaller companies naturally create the opportunity for domestic penetrations by a trading company mechanism.

PART II

THE TRADING COMPANY CONCEPT

The first part of this report explored the problems any firm desiring to participate in sales of goods (and services) to foreign countries must overcome and the various means utilized. The nature of the problems to be overcome determine the alternative organizational structures that are appropriate to achieve the purposes of the firm.

In this part of the report, we will discuss in depth one structural response to overcome the problems of international trade, the trading company. We will briefly explain the modern origins of the concept, the various forms of trading companies, the necessary tasks it must perform and characteristics it must possess to successfully overcome problems in international trade and basic economic reasons why this structural form is largely missing from the United States today.

We believe that it is extremely important to understand the history of trading companies because the feasibility/creation of these companies in other countries was largely a function of the environments within those countries and priorities established by their governments. Any attempt to create an American Export Trading Company must likewise bridge the interest gaps between the public and private sectors.

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SECTION I

THE HISTORY AND NATURE OF THE MODERN TRADING COMPANY

A. Throughout the world's commercial history, trading companies have been an important channel for the flow of goods-linked to the needs of merchants to reduce risks. As early as the Eleventh Century, the city-state of Venice had established a thriving trade with Asia. Strictly speaking, the trade of this period was not carried on by "companies" but families; however, the concept of a joint-stock venture whose task was to acquire manufactured goods or commodities from one party and transport them to distant locations for sale--a trading company if you will--emerged shortly thereafter. By the time of Columbus, Oriental products were highly valued all over Europe. Spices such as pepper, cinnamon, ginger, nutmeg and cloves were in great demand. Europeans also prized tropical foods like rice, figs and oranges as well as perfumes--often used as a substitute for soap--raw silk, cotton, rugs, damask, dyestuffs, fine steel products, precious stones and various drugs. Europeans energetically sought goods to offer in exchange, such as woolen cloth, furs and lumber.

The cost of trading goods over long distances, however was extremely high. To transport spices from the Indies, silk from China, or rugs, cloth and fine steel from the Middle East entailed much time and risk. The combined sea-land routes were long and complicated, with pirates or highway robbers a constant threat. Every major landowner through whose territory the caravans passed demanded some compensation. Few merchants actually operated on a continental scale; typically goods passed from hand-to-hand many times with each middleman taking a profit.

By the Fifteenth Century, merchants in Europe began to look for a cheaper way of obtaining Oriental products and the era of the trading company was about to begin. The trading company concept was to become a major tool for obtaining economic growth for most European countries and Japan, but conspicuously absent as a major force in the United States.

B. The beginnings of the European trading company concept are intimately linked to the theory of mercantilism. During the Sixteenth, Seventeenth and Eighteenth Centuries, according to prevailing opinion all over Western Europe, colonies were important for a variety of economic reasons. Economic thinkers believed that the possession of gold and silver was the best barometer of national prosperity. This theory called mercantilism led European powers to seek colonies as neither of these precious metals were available in any quantity in Europe. The predominance of Sixteenth Century Spain seemed to contemporaries to prove the importance of these precious metals in achieving national power. Later on, the theory was extended to include the concept of "the favorable trade balance" and mercantilism came to mean concentrating on producing for export and limiting imports of ordinary goods and services in every way possible. Thus, even colonies that did not contain precious metals were valuable if they yielded raw materials that would otherwise have to be purchased from foreign sources or if they provided markets for the manufactured products of the mother country.

The capital and risks to that capital necessary to colonize an empire and create trade were greater than any individual's capability, including the monarchy. Organizations, known as joint-stock companies, the ancestors of modern trading companies, were formed to colonize and create trade. These joint-stock companies enabled groups of investors and merchants to pool their capital and limit individual risks.

C. A threat to Japan's national survival directly influenced the creation and development of its unique General Trading Companies. The strong commitment to the mercantilistic policies of the era had pushed the European powers and even the United States into Asia by the mid-Nineteenth Century. By the late 1860's, Japan was one of the few countries in East Asia yet to be conquered. The threat of conquest by European powers, among other reasons, led a small group of men to overthrow the decaying Tokugawa feudal system that had ruled Japan for over two hundred years and initiate what is called the Meiji Restoration. One of the first priorities of the Meiji leadership was to build sufficient military strength to ensure Japan's survival. Previous encounters with the weaponry of the West

led the new government leaders to the conclusion that Japan must industrialize in order to build a modern armed forces. The importance of exports quickly became manifest. Japan needed exports to pay for modern weapons and machines, to send Japanese abroad for training and to hire foreign advisors to help in the industrialization process. A period of exploration by foreign agents quickly taught the Japanese that foreign trade required specialized technological knowledge, familiarity with foreign markets and financial resources. In 1872, with active encouragement by the Meiji leadership, Mitsui, which had been a successful merchant family for many years, became the first Japanese trading company. However, for a decade or so, Japanese trading companies were not much different than the earlier British trading companies.

1) The Japanese Government took an active role not only in the financing but also in the operation of the industrial sector from its initiation. A few of the more progressive families within the Tokugawa fuedal system had started modern industrial enterprises prior to the Restoration over which they maintained direct control. Since most of the Meiji leadership came from these families, the idea of government leadership in industry was intrinsic to them. The new national government took over the businesses started by the feudal families and pioneered new businesses in industries such as railroads, mining and shipbuilding.

2) The unique industrial group structure stemmed from a decision made by the Japanese government in 1880 to divest itself of the enterprises it had initiated. Despite the fact that the Meiji government actively participated in international expositions around the world, gave numerous studies to newly established companies for international trade and established banks and insurance companies, the effect of this assistance was slow to emerge. Profits were small and there was a consensus that the government needed to devote its total efforts toward making broad economic policies rather than initiating and managing specific businesses. By this time a small group of businessmen close to the government leaders had emerged, however,

and could be depended on to serve as an instrument of the national will. The ruling elite chose to favor this small group of businessmen including the leaders of Mitsui and Mitsubishi. The government enterprises were sold at low cost to these family-owned firms, heavy subsidies were provided for the development of key industries and protection against import competition was strengthened. These family-owned companies evolved gradually into a unique Japanese institution--the Zaibatsu--giant diversified companies under the control of a family-owned holding company. Over a period of two to three decades, with extensive government support, these groups came to include banks, insurance companies, shipping firms, a large number of manufacturers, and of course trading companies. It is important to note that the Trading Company was not the controlling element of the industrial group. This was the concern of the family-run holding company. Further, these groups should not be thought of as integrated, but self-sufficient. The trading company came into being because it didn't make economic sense for the family to run a large number of separate distribution systems, especially in international trade where quantity buying of a variety of raw materials for many of their businesses was called for.

D. The astounding growth of the Japanese General Trading Companies or "Sogo Shosha" is due to their direct and indirect control over the survival and growth of much of Japan's manufacturing sector. Over time, the Zaibatsu trading companies developed the skills to mobilize a large number of small industries which would shortly prove to be their real source of growth. The relationship between the trading companies and small firms became known as "Keiretsu." The trading company supplied its Keiretsu with raw materials, a broad range of management assistance, and most importantly, credit. In turn the Keiretsu allowed the trading company to develop markets and sell its products abroad--albeit with strong government control tending to restrict export licenses to these few family companies.

Examining the growth of the trading companies from the beginning of World War I to 1940, however, it appears that the ability of these companies to obtain and create credit was their principal source of growth. The commercial environment of this era could be described as explosive growth in industrial capacity during the war

years, followed by a recession in the later half of the 1920's. Then in 1927, Japan experienced a bank panic which saw the demise of some of the largest as well as the smallest banks. The beginning of the 1930's brought with it the depression and finally the period was closed by rapid industrial expansion in preparation for war.

By the late 1920's the turbulent economic events had caused a dual structure in the capital markets of Japan to appear. The large firms, among them Zaibatsu-related firms, obtained both capital and short-term credit from the banks in both good times and bad. In good times, the larger firms were the banks' most favored customers; in bad times, the banks couldn't afford to withhold credit to these large firms where most of their credit risk was placed. For small and medium-sized firms, this situation was entirely different. When the economy was booming, they could obtain credit only after the financial needs of the larger firms had been met and when the economy was down, they were the first to be denied. Such a difference in credit availability had a profound impact on the business community in Japan, as well over half the corporate capital is borrowed from banks rather than from issuing stock.

Thus, during the 25 year period between 1914 and 1940, many small and medium-sized firms either chose or were forced to become "child" firms of the Zaibatsu to have access to capital. During the same period, Mitsui's equity capital rose from less than 37 million yen to over 218 million yen and its "created credit" (accounts payable and notes outstanding) rose from 73 million yen to 569 million yen.

E. The modern European trading companies emerged from the opportunities created by imperialistic expansion. A good example of how and why European trading companies grew is provided by Inchcape and Company Limited. The group is headquartered in London with subsidiaries scattered throughout the Near and Far East, Africa and the Caribbean--principally former British territories. As a group today it is engaged in: motor vehicle distribution and assembly; shipping, marine service and lighterage; timber and construction; engineering; tea production; investment trusts; insurance broking; and merchant banking. They are general merchants, agents and secretaries.

This particular trading company had its origins like a great number of other British trading companies in the Nineteenth Century. The two major ingredients which accounted for the company's development were the Empire and the Scots. Both were essential. Scotland had long produced conscientious, bright and business-oriented young men far in excess of its ability to absorb them. In the Nineteenth Century as the young Scot looked about for opportunity, the growing British Empire--particularly India, Africa and the Far East--offered an attractive option (it was the equivalent of "go West young man"). It took very little capital to set up a trading business in these locations and British exporters were prepared to take some chances as were the money lenders in the Bazaars and the shipping companies who needed the traffic.

F. Unlike the Japanese trading companies that grew through controlling manufacturers rather directly, the European trading companies grew by "controlling" end-markets, the avenue of manufacturing growth. In their early years, both the European and Asian trading companies operated somewhat similarly; however, their ability to survive and the relative differences in size which were to emerge are clearly related to the differences between the two in their relationships to the manufacturing sector.

A strong tie was created between the European trading companies and their manufacturer suppliers through extremely strong market-back knowledge. Over the years, investments in infrastructure gave the trading companies such a headstart in the marketplace that only a determined and expensive effort by the manufacturers could be expected to produce better results. Manufacturers, however, were not limited by such structural considerations as a two-tier banking system and had the option of going direct to end-users if desired. Thus, absolute control over manufacturers was nonexistent except in those cases in which the trading company was formed by a manufacturer primarily to distribute its own products, e.g. Unilever.

G. Trading companies succeeded in countries where export trade was considered vital. It has been mentioned, but it must be explicitly stated, that trading companies reached their most successful results in countries whose governments were strong proponents of export trade. Just as important, trading was respected as a legitimate profession, distinct

from manufacturing in those countries. In neither Japan nor Europe would trading companies have been formed without the direct support of the various governments.

An important observation to note from this section is that the trading companies did not tend to emerge as a result of the interest of manufacturers, but rather some outside source. In the case of the Japanese industrial group, it was the family owners who desired these companies in order to minimize purchase expenses. In the case of the British example, it was the desire of the entrepreneur to carve out an existence in a new land.

SECTION 2

VARIOUS FORMS OF TRADING VEHICLES

Up to this point, the term "Trading Company" has not been defined. This is because there is not really one definition which is all inclusive. In fact, there are a number of forms which a trading company or "independent export unit" can take. There is, however, a relation between the form a trading company can take and the business problems it should be expected to solve--the more business problems a trading company solves, the bigger it will be.

This section will define specific kinds of independent export units, the nature of their operations, organizational structures and other characteristics. We will reserve the title "trading company to our own concept unless it is specifically being applied to the Japanese variety. Exhibit II-1 defines the various kinds of independent export units found in the U.S. today.

A. There are three fundamental forms of independent export units. Despite numerous variations on a theme, independent export units can be classified as one of three types:

1) Associative Types
2) Middleman Types
3) Integrated Types

Each type has unique characteristics and capabilities. The first two have been relatively common in the United States, while practically none of the last type have ever existed domestically.

1) Associative export units are typically sales organizations acting on behalf of groups of firms in the same industry solely to generate foreign business. The most well-known examples of associative organizations in the United States are the Webb-Pomerene associations. Webb-Pomerene associations are groups of firms which combine their resources for the sole purpose of engaging in export trade and exempted from provisions of the Sherman Act. Since the law was enacted in 1918, 200 Webb-Pomerene associations have been created. However, at present, there are only 34 operating. A

INDEPENDENT EXPORT UNITS

The terms used to describe independent export firms have never been precise—for one thing, rarely do such firms engage in only one basic type of export activity. The definitions given below are the ones used in this report to facilitate a discussion of export firm-client relationships.

No Assignment of Responsibility from a United States Client

Purchasing Agent

Foreign purchasing agents are variously referred to as "buyer for export," "export commission house," or "export confirming house." They operate on behalf of, and are remunerated by, an overseas customer. They generally seek out the United States manufacturer whose price and quality match the demands of their overseas principals.

Foreign purchasing agents often represent large users of materials abroad—governments, utilities, and railroads, for example. They do not offer the United States manufacturer stable volume except when long-term supply contracts are agreed upon. Purchases may be completed as domestic transactions with the purchasing agent handling all export packing and shipping details, or the agent may rely on the manufacturer to handle the shipping arrangements.

Export Broker

The export broker receives a fee for bringing together the United States seller and the overseas buyer. The fee is usually paid by the seller, but sometimes the buyer pays it. The broker takes no title to the goods, and assumes no financial responsibility. A broker usually specializes in a specific commodity, such as grain or cotton, and is less frequently involved in the export of manufactured goods.

Export Merchant

Export merchants are sometimes referred to as "jobbers." They seek out needs in foreign markets and make purchases in the United States to fill these needs. Conversely, they often complement this activity by importing to fill needs in the United States. Export merchants often handle staple, openly traded products, for which brand names or manufacturers' identifications are not important.

Compensation is in the form of a markup that the merchant bases on market conditions. Manufacturers sell to the export merchant in an ordinary domestic transaction. The merchant generally purchases from the low-bidding manufacturer or middleman. Many merchant houses, to stabilize their businesses, also operate as export distributors or export commission representatives.

Assignment of Responsibility from a United States Client

Export Management Company

Export Management Company (EMC) is the term used to designate an independent export firm that acts as the export sales department for more than one manufacturer. The export management company usually operates in its own name, but sometimes it operates in the name of a manufacturer-client for export markets. It may act as an independent distributor, purchasing and reselling goods at an established price or profit margin, or as a commission representative taking no title and bearing no financial risks in the sale.

Manufacturer's Export Representative

Export Management companies often refer to themselves as manufacturer's export rep-

resentatives whether they act as export distributors or export commission representatives.

Export Distributor

The export distributor assumes financial risk. The firm usually has exclusive right to sell a manufacturer's products in all or some markets outside the United States. The distributor pays for goods in the United States in a domestic transaction and handles all financial risks in the foreign sale. The firm ordinarily sells at manufacturer's list price abroad, receiving an agreed percentage of list price as remuneration. The distributor may operate in its own name or in the manufacturer's. It handles all shipping details. The export distributor usually represents several manufacturers and often is an export management company.

Export Commission Representative

The export commission representative assumes no financial risk and is sometimes termed an "agent," although this term is generally avoided because of the legal connotations of the term. The commission representative is assigned all or some foreign markets by the manufacturer. The manufacturer carries all accounts, although the representative often provides credit checks and arranges financing. The representative may operate in its own name or in the manufacturer's. Generally, export commission representatives handle several accounts and often are export management companies.

Cooperative Exporter

The cooperative exporter, sometimes called a "mother hen," a "piggyback" exporter, or an "export vendor," is an export organization of a United States manufacturing company retained by other independent manufacturers to sell their products in some or all foreign markets. Cooperative exporters usually operate as export distributors for other manufacturers, but may operate in special cases as commission representatives. They are not regarded as a form of an export management company.

Webb-Pomerene Association

Webb-Pomerene associations are organizations jointly owned, maintained, or supported by competing United States manufacturers especially and exclusively for export trade. Special legislation gives them qualified exemption from antitrust laws. They may provide informational services to their members, as well as buy and sell abroad, and may engage in other activities such as setting prices and allocating orders.

Foreign Freight Forwarder

Foreign freight forwarders are licensed by the Federal Maritime Commission and are considered an integral part of the American merchant marine. They are highly specialized in traffic operations, overseas import regulations, customs clearances, and shipping rates and schedules. They assist manufacturers or combination export managers in determining and paying freight, fees, and insurance charges. Forwarders may also do export packing. For a fee paid by the overseas customer, they usually handle goods from port of exit to overseas port of entry. They may also move inland freight from factory to port and, through affiliates abroad, handle freight from foreign port to customer.

A licensed forwarded may receive brokerage or rebates from shipping companies for booked space. Some export companies and manufacturers engage in freight forwarding or some phase of it on their own, but they may not, under law, receive brokerage from shipping lines.

Source: The Conference Board
& Hay Associates

detailed examination of the Act and issues relating to the disastrous decline in number of Webb Associations is provided in Part III-Section 1. At this time, it is sufficient to note that several recommendations of the Federal Trade Commission and a handful of court decisions have generally restricted the ambit of antitrust exemptions initially believed to be generated by the Act. Exhibit II-2 lists the Webb-Pomerene Associations currently operating under F. T. C. supervision.

Associative organizations generally do not take title to the goods they market abroad. Thus all financial risk is shared by the firms which comprise the association. This is an important distinction for, as we shall explain shortly, the acceptance of title by a trading company sharply impacts on the size such an organization can reach in the United States. It is also important to note that the relationship between the associative organization and its suppliers is extremely strong: in fact, the company exists only to serve the marketing needs of its suppliers-which are its sole owners as well.

Associative organizations, both domestic and foreign, tend to be horizontally integrated companies consisting solely of competitors in one industry, although the Webb-Pomerene Act does not in any way prohibit the formation of vertically integrated or multi-industry companies. Furthermore, successful associative trading companies generally tend to deal in standard commodities such as food, wood and paper products. Indeed, the horizontal nature of an associative trading company has had a strong impact on limiting its usefulness to dealing in basic commodities. The basic marketing strategy of most American manufacturers rests heavily on the concept of product differentiation and use of brand names. Many manufacturers have avoided or quickly terminated joint exporting because they are unwilling to blend the individual image they have developed, sometimes over decades, with that of their competitors into a common associative image.

A typical associative organization has no or few sales offices located in foreign countries. Most act only as a clearing house for international sales. Operational support is given the association in the form of membership dues.

EXHIBIT II-2

ASSOCIATIONS REGISTERED UNDER THE WEBB-POMERENE EXPORT TRADE ACT

ASSOCIATIONS	PRODUCT
AFRAM FILMS, INC.	Motion Picture Films
AMATEX EXPORT TRADE ASSOCIATION, INC.	Textile Machinery
AMERICAN ALFALFA EXPORT CORPORATION	Alfalfa
AMERICAN MOTION PICTURE EXPORT CO. (Africa), INC	Motion Picture Films
AMERICAN RAILWAY CAR EXPORT ASSOCIATION	Railway Car
AMERICAN WOOD CHIP EXPORT ASSOCIATION	Wood Chips
AMERTOOL SERVICES CORP.	Machinery
AMTAN, LTD.	Leather and Leather Products
ANTHRACITE EXPORT ASSOCIATION	Anthracite Coal
CALIFORNIA DRIED FRUIT ASSOCIATION	Dried Fruit
CALIFORNIA RICE EXPORT ASSOCIATION	Rice and By-products
FLOUR MILLERS' EXPORT ASSOCIATION	Flour
FOURDRINIER WIRE CLOTH EXPORT ASSOCIATION	Wire Cloth
KAOLIN CLAY EXPORT, INC.	Kaolin Clay and other Products
MOTION PICTURE EXPORT ASSOCIATION OF AMERICA, INC.	Motion Picture Film
NORTH COAST EXPORT COMPANY	Wood Chips and Saw Dust
NORTHWEST DRIED FRUIT ASSOCIATION	Dried Fruit
OHIO ALFALFA EXPORT CORP.	Dehydrated Alfalfa and Suncured Alfalfa in Meal or Pelletted Form
PACIFIC AGRICULTURAL COOPERATIVE FOR EXPORT, INC.	Fruit and Nuts
PACIFIC COAST AGRICULTURAL EXPORT ASSOCIATION	Dried Fruit
PACIFIC COAST FOOD EXPORT ASSOCIATION	Food
PENCIL INDUSTRY EXPORT ASSOCIATION	Pencils and Pens
PHOSPHATE CHEMICALS EXPORT ASSOCIATION	Phosphate Chemicals
PHOSPHATE ROCK EXPORT ASSOCIATION	Phosphate Rock
PLUTONIUM EXPORT ASSOCIATION	Plutonium
PLYWOOD INTERNATIONAL	Plywood
POTASH EXPORT ASSOCIATION, INC.	Potash
PULP, PAPER & PAPERBOARD EXPORT ASSOCIATION of the UNITED STATES	Paper and Tall Oil
SULPHUR EXPORT CORPORATION	Crude Sulphur
TALMEX EXPORT CORPORATION	Animal and Marine By-products
USA-TEX	Textile Products
VEGETABLE OIL EXPORT CORPORATION	Soybean Oil and Related Products
WALNUT EXPORT SALES COMPANY, INC.	Walnut Lumber, Logs Veneer, and some Oak
WOOD FIBRE EXPORT INC.	Wood Chips

Source: Federal Trade Commission

a) An interesting exception to the horizontally integrated associative company is Amatex Export Trade Association. This association represents approximately 31 member manufacturers. It is a nonprofit Webb-Pomerene Association organized solely to generate textile machinery export sales.

Amatex acts as a general sales agent for members participating in its export sales contracts. It is designed to provide and service full projects and turn-key operations such as complete spinning mills, weaving mills, fully integrated mills to include dyeing and finishing and others. Amatex will design, engineer, sell, negotiate and erect complete textile mill projects, but by law, it supplements and does not necessarily replace the export activities of its member companies.

The association has at least two and usually more members in each of the four textile manufacturing areas; spinning, preparatory, weaving and dyeing and finishing. When a project is identified, and this can happen through Amatex's efforts or those of a member company, Amatex will request bids from all of its members. The decision as to which manufacturers are to be used is, whenever possible, left up to the buyer. Amatex will only make a choice when necessary. Any company may submit a bid directly to the buyer as well as through Amatex.

The advantage for a manufacturer to use Amatex is that the association has a total mill capability while none of the manufacturers do. It also has the ability to pull a project together which is important when dealing with highly individualistic companies. The weakness of the association is felt by its management to be limited growth through lack of financing ability. Title never passes to Amatex and the credit is supported by the manufacturers. But when domestic sales are up, manufacturers leave as soon as possible (they must join for a period of 2½ years). They return in hard times. Thus, the tie to the manufacturer who supplies the trading vehicle is less than might be anticipated.

2) Middleman export units are firms which may act as commission representatives or export distributors for several firms, typically in allied but noncompetitive businesses. This form of export unit is the most common found in the U.S. today. Over 600 different companies of this kind are listed with the Department of Commerce. Professional organizations representing the interests of these firms believe that over 1,000 Export Management Companies, as these middleman companies are referred to in the U.S., are currently operating. In the past, however, there have been and in Europe today there still are a number of names used to denote export trading companies of the middleman sort including: export merchants, export brokers, combination export managers and manufacturer's export representatives to name a few. The terms used to distinguish the various kinds have never been precise or mutually exclusive. In general, however, all these firms act as either commission representatives or export distributors or both.

When they act as commission representatives of a company they are usually agents pursuing, closing and processing export sales under their representative names and take very little business risk. Usually they are compensated by commissions on the foreign sales. When the export trading company acts as an export distributor, he performs the same marketing tasks as the commission representatives, but he also takes title to goods, assumes the financial risks of foreign accounts and sometimes integrates forward into warehousing and fabricating and is paid by mark-up.

Part IV of this report examines in detail the Export Management Company. At this point, however, it is of interest to note that most EMC's have no foreign sales offices, but sell to independent foreign distributors who distribute and service the products themselves. They do not tend to distribute exported products directly to end-users. Also of interest is the fact that for a large EMC, the ratio of long term debt to net worth runs between 20 and 30% and the ratio of accounts receivable to net worth is about three to one. The largest EMC sales level we are aware of is approximately $50,000,000. To our knowledge, no EMC has ever been founded by a group of manufacturers to service their export needs.

3) Integrated Trading Companies are best exemplified by the British and Japanese trading companies which combine middleman functions for a larger number of industries and a direct marketing capability.

The Japanese Trading Company

The "Sogo Shosha", or general trading companies of Japan, have no exact counterpart anywhere else in the world and the words "trading company" have almost become synonomous with them. Each of the ten largest trading companies include in their main business lines export, import and domestic sales of product lines and services that literally span the breadth of man's activities. For example, almost all of the largest trading companies have extensive dealings in iron and steel, machinery, textiles, oil and gas, chemicals, foods, general merchandise, construction, real estate, leasing and insurance. Some of the reasons which led to this situation were discussed in Part II, Section 1.

One of the outstanding features of a Soga Shosha is their proven ability to obtain immense economies of scale in transportation, warehousing and other important areas of international trade, simultaneously diversifying business risk through the large number of products it markets and transactions it makes. The diversification of business risk and size of these companies are important elements in its ability to secure adequate financing for its operations.

Another distinctive feature of the Sogo Shosha is their ability to provide all the information and know-how required to set up major projects in such diverse fields as recreation, housing, regional development, education, medicine and fashion.

In Japan, the production function has been divorced from the international marketing function for most of industry. As a result, the Sogo Shosha have grown to enormous size. Exhibit II-3 shows the size of the ten largest general trading companies in Fiscal 1972 (the latest year for which a large quantity of translated

EXHIBIT II-3

SALES OF THE TEN LARGEST
JAPANESE TRADING COMPANIES
FISCAL 1972

	BILLIONS OF YEN MILLIONS OF DOLLARS Sales	
	Yen	Dollars
Mitsubishi	5182	18,297
Mitsui	4956	17,500
Marubeni	3400	12,026
C. Itoh	3174	11,207
Sumitomo	2415	8,496
Nissho Iwai	2393	8,467
Tomen	1551	5,471
Kanematsu-Goshu	1193	4,215
Ataka	1165	4,125
Nichimen	1164	4,124
TOTAL	26,592	93,938

Source: Yukashoken Hokokusho

Sales in U.S. dollars between 4/72 – 9/72 are based on $1/Y 308 exchange rate
Sales between 10/72 – 3/73 are based on a rate of $1 Y265
(two rates used because of Trading Comoany practices)

Note: Strictly speaking, only the Yen figures are accurate basis for comparison.

statistics are available). Sales in the Japanese fiscal year 1972 (April 1 to March 31, 1973) totaled $94 billion or about 30% of Japan's GNP and slightly more than twice the size of the government's budget. These firms were responsible for 51% of total exports and 63% of total imports during Fiscal 1972.

The worldwide sales networks of the ten largest trading companies is likewise impressive. In 1973, the Sogo Shosha had over 800 offices worldwide and almost 5,000 employees stationed abroad. Exhibit II-4 shows the multinational commercial presence of these companies.

The organization structure of Marubeni Inc., the third largest Sogo Shosha, is shown in Exhibit II-5. As can be seen, the company is divided into product groups and staff groups. The division most unique to the company and general trading companies is the Coordination Division. This division is responsible for formulating middle and long-range managerial plans. These are comprehensive business programs based on domestic and international research. Here the daily activities of office and subsidiaries around the world are monitored. These activities include import-export freight operations, intermodal transportation and insurance arrangements.

Today, each general trading company is the nucleus of a core of industrial groups. Exhibit II-6 shows the enterprises belonging to the Mitsui Group, among which there are differences according to historical background, extent of participation in group investments and economic ties. The enterprises listed in this exhibit have a close relationship with Mitsui financing institutions centering on the Mitsui Bank, conduct large economic transactions with Mitsui & Company, the general trading company, and are members of the Mitsui Group's policy making bodies, the "Getsuyo-kai" (Monday Conference) and "Nimoku-kai" (Mitsui Public Relations Committee). Also included in the Mitsui Group are a large number of large and small domestic enterprises and various kinds of joint venture companies with foreign firms; however, the firms listed here are those having a comparatively close relationship with the Group.

EXHIBIT II-4

THE MULTINATIONAL COMMERCIAL PRESENCE OF THE 10 LEADING TRADING COMPANIES, MARCH 31, 1973[a]

Company	Branches	Wholly-Owned Subsidiaries	Subunits of the Branches or Branches of the Subsidiaries	Number of Personnel from the Parent Company	Number of Local Personnel
Mitsubishi	14	23	82	763	2,460
Mitsui	15	20	79	802	2,133
Marubeni	15	17	65	592	2,041
C. Itoh	8	11	90	584	1,500
Nissho-Iwai	5	12	87	560	1,120
Sumitomo	8	10	68	476	973
Tomen	9	11	55	334	632
Nichimen	9	12	46	306	572
Kanematsu-Gosho	6	9	44	330	850
Ataka	6	7	50	234	407

Source: Company records.

[a]These entities include only those established for general trading.

ORGANIZATION STRUCTURE
MARUBENI CORPORATION
EXHIBIT II - 5

Auditor (Statutory)

President's Office	Textile Division-1	Textile Division-2	Textile Division-3	Iron & Steel Division	Iron & Steel Material Division	Non-Ferrous & Light Metals Division
Public Relations Office						
Legal Dept.	Textile Administration Dept.-1	Textile Administration Dept-2	Textile Administration Dept.-3	Iron & Steel Administration Dept.	Iron & Steel Material Administration Dept.	Non-Ferrous & Light Metals Administration Dept.
Audit Dept.	(Textile Administration (Tokyo) Dept.)	(Textile Administration (Tokyo) Dept.)	(Textile Administration (Tokyo) Dept.)	Steel Development Dept.	Iron & Steel Material Development Dept.	Overseas Mining Projects Dept.
History Compilation Dept. (Company History)	Cotton Dept.	Staple & Yarn Dept.-1	Knitting Yarn Dept.	Steel Sheets Dept.	Iron Ore Dept.	Non-Ferrous Ores Dept.
Personnel (Personnel & Welfare Dept. Training Dept.)	Wool Dept.	Staple & Yarn Dept.-2	Knit Goods Dept.	Steel Plates & Tubular Goods Dept.	Steel Materials Dept.	Non-Ferrous Metals Dept.
	Overseas Staple & Yarn Dept.	Fabrics Dept.-1	Industrial Textile Dept.	Steel Structural Materials & Fabrication Dept.	Ferro Alloy Dept.	Mining Equipment & Supplies Dept.
Administration, Market Planning, Credit (Administration Dept. Communication Dept. Market Planning Dept. Credit Dept.)	Overseas Fabrics Dept.	Fabrics Dept.-2	Furnishing Dept.	Special Steel & Wire Dept.	Refractories & Minerals Dept.	Light Metals Dept.
	Overseas Textile Made-up Goods Dept.	Printed Textile Dept.	Special Procurement Dept.	Overseas Iron & Steel Dept.-1	Coal Dept.	Mine Engineering Dept.
	Textile Goods Import Dept.	Textile Made-up Goods Dept.	(Textile (Tokyo) Dept.-2)	Overseas Iron & Steel Dept.-2	Iron & Steel Material (Osaka) Dept.	Non-Ferrous & Light Metals (Osaka) Dept.
Finance & Accounting (Finance Dept. Accounting Dept. International Finance Dept.	(Textile (Tokyo) Dept.-2)	(Textile (Tokyo) Dept.-1)	(Textile (Nagoya) Dept.)	Iron & Steel (Osaka) Dept.	Iron & Steel Material (Nagoya) Dept.	Non-Ferrous & Light Metals (Nagoya) Dept.
	(Textile (Nagoya) Dept.)	(Textile (Nagoya) Dept.)		Iron & Steel (Nagoya) Dept.		
Co-ordination (Co-ordination Dept. International Dept. Affiliated Enterprise Dept. Transport & Insurance Dept.)		Textile Development Dept.			Overseas Resources Research Dept.	
Domestic Branches & Offices						
Overseas Branches & Offices						
Overseas Subsidiaries						

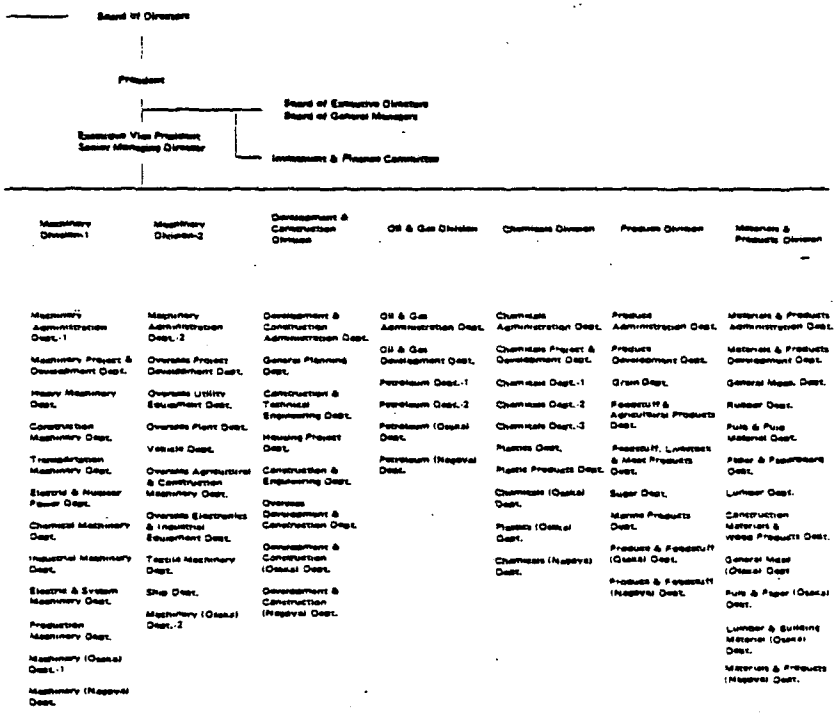
Board of Directors
President
Board of Executive Directors
Board of General Managers
Executive Vice President
Senior Managing Director
Investment & Finance Committee
Machinery Division-1
Machinery Division-2
Development & Construction Division
Oil & Gas Division
Chemicals Division
Produce Division
Materials & Products Division
Machinery Administration Dept.-1
Machinery Project & Development Dept.
Heavy Machinery Dept.
Construction Machinery Dept.
Transportation Machinery Dept.
Electric & Nuclear Power Dept.
Chemical Machinery Dept.
Industrial Machinery Dept.
Electric & System Machinery Dept.
Production Machinery Dept.
Machinery (Osaka) Dept.-1
Machinery (Nagoya) Dept.
Machinery Administration Dept.-2
Overseas Project Development Dept.
Overseas Utility Equipment Dept.
Overseas Plant Dept.
Vehicle Dept.
Overseas Agricultural & Construction Machinery Dept.
Overseas Electronics & Industrial Equipment Dept.
Textile Machinery Dept.
Ship Dept.
Machinery (Osaka) Dept.-2
Development & Construction Administration Dept.
General Planning Dept.
Construction & Technical Engineering Dept.
Housing Project Dept.
Construction & Engineering Dept.
Overseas Development & Construction Dept.
Development & Construction (Osaka) Dept.
Development & Construction (Nagoya) Dept.
Oil & Gas Administration Dept.
Oil & Gas Development Dept.
Petroleum Dept.-1
Petroleum Dept.-2
Petroleum (Osaka) Dept.
Petroleum (Nagoya) Dept.
Chemicals Administration Dept.
Chemicals Project & Development Dept.
Chemicals Dept.-1
Chemicals Dept.-2
Chemicals Dept.-3
Plastics Dept.
Plastic Products Dept.
Chemicals (Osaka) Dept.
Plastics (Osaka) Dept.
Chemicals (Nagoya) Dept.
Produce Administration Dept.
Produce Development Dept.
Grain Dept.
Foodstuff & Agricultural Products Dept.
Foodstuff, Livestock & Meat Products Dept.
Sugar Dept.
Marine Products Dept.
Produce & Foodstuff (Osaka) Dept.
Produce & Foodstuff (Nagoya) Dept.
Materials & Products Administration Dept.
Materials & Products Development Dept.
General Metal Dept.
Rubber Dept.
Pulp & Pulp Material Dept.
Paper & Paperboard Dept.
Lumber Dept.
Construction Materials & Wood Products Dept.
General Metal (Osaka) Dept
Pulp & Paper (Osaka) Dept.
Lumber & Building Material (Osaka) Dept.
Materials & Products (Nagoya) Dept.

EXHIBIT II - 6

List Of Mitsui Group Members And Related Enterprises

Brackets indicate membership in various intra-group committee meetings. (G) stands for Getsuyo-kai. (N) stands for Nimoku-kai and (K) for Koho-iinkai (Mitsui Public Relations Committee).

1 Mitsui Bank, Ltd. (GXNKK)
2 Nippon Flour Mills Co., Ltd. (GXN)
3 Toray Industries, Inc. (GXNKK)
4 Oji Paper Co., Ltd. (GXN)
5 Mitsui Toatsu Chemicals Inc. (GXNKK)
6 Mitsui Petrochemical Industries, Inc. (GXNKK)
7 Japan Steel Works, Ltd. (GXNKK)
8 Mitsui Mining & Smelting Co., Ltd. (GXNKK)
9 Tokyo Shibaura Electric Co., Ltd. (GXN)
10 Mitsui Shipbuilding & Engineering Co., Ltd. (GXNKK)
11 Mitsui Mining Co., Ltd. (GXNKK)
12 Hokkaido Colliery & Steamship Co., Ltd. (GXNKK)
13 Mitsui Construction Co., Ltd. (GXNKK)
14 Sanki Engineering Co., Ltd. (GXNKK)
15 Mitsui & Co., Ltd. (GXNKK)
16 Mitsukoshi Ltd. (GXN)
17 Mitsui Real Estate Development Co., Ltd. (GXNKK)
18 Mitsui Warehouse Co., Ltd. (GXNKK)
19 Mitsui O.S.K. Lines, Ltd. (GXN)
20 Mitsui Trust and Banking Co., Ltd. (GXNKK)
21 Mitsui Mutual Life Insurance, Company (GXNKK)
22 Taisho Marine and Fire Insurance Co., Ltd. (GXNKK)
23 Denki Kagaku Kogyo Kabushiki Kaisha (GXK)
24 Toshoku Ltd. (G)
25 Toyo Menka Kaisha Ltd. (G)
26 General Sekiyu K. K. (G)
27 Showa Aircraft Industry Co. (G)
28 Mitsui Aluminium Co., Ltd. (G)
29 Mitsui Alumina Co., Ltd. (G)
30 Mitsui Consultants Co., Ltd. (G)
31 Mitsui Harbor Development Co., Ltd. (G)
32 Mitsui Air & Sea Service Co., Ltd. (G)
33 Mitsui Cement Co., Ltd. (G)
34 Mitsui Seiki Kogyo Co., Ltd. (G)
35 Mitsui Agriculture and Forestry Co., Ltd. (GXK)
36 Mitsui Miike Machinery Co., Ltd. (GXK)
37 Toyo Engineering Corporation (GXK)
38 Mitsui Sugar Co., Ltd.
39 Mitsui Ocean Development & Engineering Co., Ltd. (K)
40 Mitsui Kanko Development Co., Ltd. (K)
41 Mitsui Knowledge Industry Co., Ltd.
42 Mitsui Pharmaceuticals, Inc. (K)
43 Mitsui Oil Exploration Co., Ltd. (K)
44 Mitsui Development Co., Ltd.
45 Mitsui Leasing & Development Ltd.
46 Nippon Atomic Industry Group Co., Ltd.
47 Mitsui Kaneko Epoxy Corporation
48 Mitsui Kozan Coking Industry Co., Ltd.
49 Mitsui Precast Concrete Construction Co., Ltd.
50 Highway Toll Systems Co., Ltd. (K)
51 Taito Co., Ltd.
52 Kanebo Ltd.
53 Jujo Paper Co., Ltd.
54 Kanegafuchi Kagaku Kogyo
55 Toagosei Chemical Industry Co., Ltd.
56 Daicel Co., Ltd.
57 Fuji Photo Film Co., Ltd.
58 Central Glass Co., Ltd. (K)
59 Onoda Cement Co., Ltd.
60 Nippon Mining Co., Ltd.
61 Fujikura Cable Works, Ltd.
62 Toshiba Machine Co., Ltd.
63 Nippon Denso Co., Ltd.
64 Yuasa Battery Co., Ltd.
65 Hino Motors Corporation
66 Toyota Motor Co., Ltd.
67 Taiheyo Konatsu Inc. (K)
68 Ishikawajima-Harima Heavy Industries Co., Ltd.
69 Mitsui Oil Supply Company, Limited
70 Toyo Bearing Mfg. Co., Ltd.
71 Shinnippon Air Conditioning Engineering Co., Ltd.
72 Mitsui Lumber Co., Ltd. (K)
73 Nishi Nippon Electric Wire & Cable Co., Ltd. (K)
74 Toshiba Shoji Co., Ltd. (K)
75 Asia Air Survey Co., Ltd.
76 Showa Electric Wire & Cable Co., Ltd.
77 Toyo Carrier Engineering Co., Ltd.
78 Nippon Formula Feed Mfg. Co., Ltd.
79 Daito Woolen Shipping & Weaving Co., Ltd.
80 Fujisankikokankoji K. K.
81 Ishikawajima Koechring Co., Ltd.
82 Toyo Soda Mfg. Co., Ltd.
83 Mitsui Wharf Co., Ltd.
84 Sapporo Breweries, Ltd.
85 Asahi Breweries, Ltd.
86 Aichi Steel Works, Ltd.
87 Toyo Seikan Kaisha, Ltd.
88 Toshiba Tungsiov Co., Ltd.
89 Kanto Auto Works, Ltd.
90 Toyoda Automatic Loom Works, Ltd.
91 Tsubakimoto Chain Co.
92 Takaoka Electric Mfg. Co., Ltd.
93 Kokusai Electric Co., Ltd.
94 Stanley Electric Co., Ltd.
95 Alps Electric Co., Ltd.
96 Mitsumi Electric Co., Ltd.
97 Tokyo Electric Co., Ltd.
98 Ibigawa Electric Industry Co., Ltd.
99 Sankyo Co., Ltd.
100 Kanebo Nakatsaki Pharmaceutical Co., Ltd.
101 Toshiba Ceramics Co., Ltd.
102 Fujita Corporation
103 Japan Development & Construction Co., Ltd.
104 Daito Kogyo Co., Ltd.
105 Japan Gasoline Co., Ltd.
106 Fujiko Co., Ltd.
107 Naigai Amimono Kabushiki Kaisha
108 Atsugi Nylon Industrial Co., Ltd.
109 Hokshu Paper Co., Ltd.
110 Takasaki Paper Mfg. Co., Ltd.
111 Nippon Art Paper Mfg.
112 Tosho Printing Co., Ltd.
113 Akimoku Kogyo Co., Ltd.
114 Tsubakimoto Machinery & Engineering Co., Ltd.
115 Tokyo Theatres Company, Incorporated
116 Tokyo Broadcasting System
117 Yomiuri Land Co., Ltd.
118 Fujita Tourist Enterprises Co., Ltd.
119 Sagami Railway Co., Ltd.
120 Inui Steamship Co., Ltd.
121 Meiji Shipping Co., Ltd.

SOURCE: MAINICHI NEWSPAPERS

All of those enterprises have a deep historic relationship with the Mitsui Group from the days of the pre-war Zaibatsu. According to Japanese executives, however, there is a significant difference between the pre-war and present day Groups. The holding company concept of the pre-war era exercised unified control over the companies under its wing from the standpoints of personnel, materials and stocks. Today, the holding company concept is outlawed by Japan's Anti-Monopoly Law and unified control is not, strictly speaking, possible. The various enterprises maintain more freedom of action, but efforts to consolidate the power of the Groups are considerable as evidenced by the strong policy-making bodies.

The general trading companies play a central role in the industrial groups because, unlike any other country, the bulk of the buying and selling functions is handled by them. As mentioned previously, in general, Japan's manufacturers confine their operations to production and leave the marketing to the trading companies. The trading companies are the organizers and coordinators of the enterprise groups--it is their key role in the selling process, their financial clout, and their world representation rather than direct ownership which give the trading companies such a unique position in Japan. Nonetheless, in recent years the Japanese trading companies have extended their ownership control over some of the other group members through direct investment. This extension of control has been greatly assisted by a regulation which limits investments in a corporation by banks to 10%.

Exhibits II-7 and II-8 show the balance sheet and income statement for Marubeni Inc. for the year 1973. Among the most significant figures are the size of the long-term debt commitment to total capital employed and the relative profitability of the company. Approximately 86.4% of total capital is long-term debt. Return on sales is a mere 0.2 of one percent (which compares to a 4% average return on sales for all United States manufacturers). Return on total capital employed is still extremely low at 2.2%, but return on equity is approximately 16.5%, far above the average return to stockholders in the United States. Note also that while

Balance Sheet

As of September 30, 1972 and 1973

MARUBENI CORPORATION

ASSETS	Millions of Yen 1973	Millions of Yen 1972	Thousands of U.S. Dollars 1973 ¥265.50=US$1	Thousands of U.S. Dollars 1972 ¥301.10=US$1
Current Assets	¥1,406,406	¥1,004,832	U.S.$5,297,198	U.S.$3,337,204
Cash on Hand & in Banks	182,386	158,188	686,953	525,367
Notes & Bills Receivable	505,692	301,845	1,904,678	1,002,474
Trade Accounts Receivable	468,092	358,576	1,763,058	1,190,887
Securities	1,162	11,411	4,376	37,898
Merchandise in Stock	77,522	56,984	291,985	189,253
Merchandise in Transit	23,367	12,893	88,011	42,820
Advances on Merchandise	106,017	70,738	399,311	234,932
Temporary Payment	1,689	1,709	6,362	5,676
Miscellaneous Accounts Receivable	5,251	7,613	19,778	25,294
Short-Term Loans	3,746	1,884	14,109	6,257
Miscellaneous Deposits	42,065	29,196	158,437	96,964
Prepaid Expenses	10,703	8,906	40,313	29,578
Other Current Assets	207	121	780	402
Allowance for Doubtful Debts	(21,493)	(15,232)	(80,953)	(50,588)
Fixed Assets	341,065	294,989	1,284,614	979,704
Tangible Fixed Assets	52,309	48,617	197,021	161,465
Buildings	9,285	8,693	34,972	28,871
Structures	3,295	3,245	12,410	10,777
Machinery & Equipment	1,617	1,226	6,090	4,072
Vehicles	430	421	1,620	1,398
Furniture & Fixtures	1,431	1,150	5,390	3,819
Land	36,860	33,102	138,866	109,937
Construction in Process	391	780	1,473	2,591
Intangible Fixed Assets	969	870	3,650	2,889
Rights	649	560	2,445	1,860
Prepaid Expenses Amortizable after One Year	320	310	1,205	1,029
Investments	287,787	245,502	1,083,943	815,350
Invested Securities	183,424	161,407	690,862	536,058
Stocks of Subsidiaries	29,576	18,710	111,397	62,139
Investments	635	513	2,392	1,704
Investments in Subsidiaries	3,588	882	13,514	2,929
Long-Term Loans	50,656	38,718	190,795	128,588
Other Investments	19,908	25,272	74,963	83,932
Total Assets	¥1,747,471	¥1,299,821	U.S.$6,581,812	U.S.$4,316,908

EXHIBIT II - 7

	Millions of Yen		Thousands of U.S. Dollars	
	1973	1972	1973 ¥298.50=US$1	1972 ¥301.10=US$1
LIABILITIES				
Current Liabilities	¥1,316,876	¥985,690	U.S.$4,959,985	U.S.$3,273,630
Notes & Bills Payable	514,891	343,186	1,939,328	1,139,774
Import Bills Accepted	185,048	130,692	696,979	434,049
Trade Accounts Payable	176,008	158,251	662,931	525,578
Short-Term Borrowings	307,738	240,620	1,159,081	799,137
Accounts Payable	26,201	15,848	94,919	52,634
Advances Received on Merchandise	61,120	55,687	230,207	184,945
Miscellaneous Deposits Received	27,534	25,584	103,706	84,968
Provision for Taxes	8,500	3,700	32,015	12,288
Other Current Liabilities	10,838	12,122	40,821	40,259
Fixed Liabilities	348,656	249,986	1,313,205	830,243
Long-Term Borrowings	336,706	249,986	1,268,196	830,243
Convertible Debentures	11,950	–	45,009	–
Reserves	27,058	15,591	101,914	51,780
Reserve for Price Fluctuations	2,870	2,400	10,810	7,971
Reserve for Overseas Market Development	3,203	3,973	12,064	13,195
Reserve for Overseas Investment Losses	8,580	3,669	32,318	12,185
Reserve for Foreign Exchange Losses	3,000	1,000	11,299	3,321
Reserve for Special Depreciation	611	705	2,302	2,341
Reserve for Succeeding Old Cost Basis	587	591	2,211	1,963
Reserve for Retirement Allowance	8,127	3,253	30,610	10,804
Liabilities	¥1,692,590	¥1,251,267	U.S.$6,375,104	U.S.$4,155,653
CAPITAL				
Capital Paid-up (Note 2)	¥30,460	¥27,500	U.S.$114,727	U.S.$91,332
Legal Reserves	10,394	12,724	39,149	42,258
Capital Surplus	7,153	9,856	26,942	32,733
Earned Surplus	3,241	2,868	12,207	9,525
Retained Surplus	14,027	8,330	52,832	27,665
General Reserve	8,154	4,412	30,712	14,653
Voluntary Reserve for Retirement Allowance	575	575	2,165	1,909
Unappropriated Surplus	5,298	3,343	19,955	11,103
Capital	54,881	48,554	206,708	161,255
Total Liabilities & Capital	¥1,747,471	¥1,299,821	U.S.$6,581,812	U.S.$4,316,908

Statement of Income and Unappropriated Surplus

Year Ending September 30, 1972 and 1973

MARUBENI CORPORATION
EXHIBIT II - 8

	Millions of Yen		Thousands of U.S. Dollars	
	1973	1972	1973 ¥301.10=US$1	1972 ¥301.10=US$1
Operating Income:				
Net Sales	¥3,986,538	¥3,027,739	U.S.$15,011,443	U.S.$10,055,593
Other Operating Income	3,019	2,639	11,363	8,764
	3,989,557	3,030,378	15,022,806	10,064,357
Operating Expenses:				
Cost of Sales	3,879,335	2,963,094	14,613,431	9,840,897
Selling Administrative & General Expenses	60,118	44,598	226,433	148,117
	3,939,453	3,007,692	14,837,864	9,989,014
Operating Profit	49,102	22,686	184,942	75,343
Non-operating Income (Expense):				
Interest Income	30,381	30,182	114,354	100,239
Dividend Income	6,341	4,377	23,883	14,537
Miscellaneous-Net	4,283	6,539	16,132	21,717
Interest Expense	(54,265)	(44,712)	(204,383)	(148,495)
Provision for Various Reserves	(8,638)	(5,731)	(32,535)	(19,034)
Loss on Conversion of Foreign Currencies—Net	(2,437)	(3,535)	(9,179)	(11,740)
	(24,335)	(12,880)	(91,733)	(42,776)
Income before Income Taxes	24,747	9,806	93,209	32,567
Provision for Income Taxes	15,700	4,700	59,134	15,609
Net Income	9,047	5,106	34,075	16,958
Unappropriated Surplus at October 1, 1971 & 1972 Previously reported	3,343	1,797	11,103	5,375
Add. Gain on Translation of Foreign Currency as Adjusted (see Note 1)	–	–	1,489	593
	3,343	1,797	12,592	5,968
	12,390	6,903	46,667	22,926
Appropriations made during current year:				
Dividends Paid	3,000	3,000	13,051	9,964
Director's Bonus	60	60	301	199
Transfer to Legal Reserve	347	300	1,307	996
Transfer to General Reserve	3,200	200	12,053	664
	7,047	3,560	26,712	11,823
Unappropriated Surplus at Sept. 30, 1972 & 1973	5,343	¥3,343	U.S.$19,955	U.S.$11,103

investments are a relatively small proportion of total assets (16.4%), they are over five times as large as the capital position of the company. The trading company's capability to create credit is shown in the fact that just three accounts, notes bills receivable, trade accounts receivable and advances on merchandise represent over 60% of the company's total assets and exceed the company's capital position by almost a factor of twenty. The figures for Marubeni are representative of the recent performance of the other large Japanese trading companies.

In addition to investments backward into the manufacturing sector, the Japanese trading companies have forward integrated beyond their investments in offices abroad to other investments in warehousing, fabricating facilities and infrastructures to support export growth.

British Trading Companies

British versions of integrated trading companies are nowhere as large or as complex as Japanese examples. With the exception of Unilever Limited's trading company, integration backward into manufacturing or processing is rare. In the case of Unilever, the trading company was formed to distribute the company's own products as well as those of others.

British trading companies have tended to have strong regional orientations, particularly toward countries of the old Commonwealth and have little or no operations in the Americas. The relatively underdeveloped nature of most of the countries in which British trading companies have major revenue sources explains part of their strength in these areas. As mentioned previously, by being strongly involved for decades in these countries, they have built supporting infrastructures for trade, including warehousing and major fabrication facilities, which are very costly to reproduce today. As a result, a determined effort by their suppliers or any other competitive source would be necessary to do better in these regions than the trading companies themselves.

Indeed, forward integration into lighterage and insurance brokerage in addition to warehousing and fabrication is seen by the British traders as where the major profit opportunities are for trading companies today.

Like the Japanese trading companies, the British trading companies are major importers as well as exporters. Today, these companies tend to import into the host countries where they do business only those goods essential to the countries' growth. As these countries became independent after the Second World War, they gave substantial guidance and counsel to government leaders to help get the new nations underway.

The organization of independent British trading companies, such as Inchcape, is geographic rather than product-oriented like the associative, middleman and Japanese type trading companies. The organizations are characterized by extensive decentralized decision-making. As now constituted, the British headquarters are predominantly a management concern with relatively few employees. Head office personnel are organized geographically under several General Managers and focus their many efforts toward the group's interests.

Economic, bookkeeping and country information is gathered, digested and spewed out as appropriate. Quite often, economic and political intelligence is s shared with the British government, bankers and suppliers. The largest companies operate subsidiaries which contact manufacturers in the U.K. when appropriate. The overseas companies are set up as complete entitites with appropriate staffing for whatever activities they are involved in. The largest of the British trading companies today has worldwide sales of less than $500 million.

American Trading Companies

We have not been able to find one example of an independent integrated trading company in the United States involved with manufactured goods. The only examples of such companies in the United States are either

strongly affiliated with large process manufacturers or commodities. The best examples today are the Kaiser Trading Company and Woodward & Dickerson of Philadelphia.

The Kaiser Trading Company is part of the Kaiser Aluminum and Chemicals Company, a wholly-owned subsidiary of Kaiser Industries. The Trading Company only exists to serve the Aluminum and Chemicals Company and no other subsidiary of Kaiser Industries. In fact, there are a number of divisions within the Aluminum and Chemical Company which do not use the trading company for international sales. Top executives of the company have discussed at times starting with a Webb-Pomerene Association to utilize their resources on a broader client base; however, lack of definition in the law has resulted in a negative decision in this regard.

Woodward & Dickerson is a world trader in such basic commodities as fertilizers, animal food ingredients, vegetable oils, cocoa and tobacco products. While it is both an importer and an exporter, about 40 percent of their business is in the form of shipments offshore from the United States--third-country trade. If barter transactions are required, then the company is usually prepared to conclude business on this basis.

The Company has offices, employees, branches, agencies and correspondents in practically every country in the world with major foreign offices in Tokyo, Singapore, Manila, Korea, Vancouver and London. Woodward & Dickerson's current sales are approaching $200 million. Although basic commodity trading is the bulk of the company's business, it has diversified into marketing cement, clinkers, gypsum, other industrial commodities and established construction machinery sales agencies in some locations. The Company has also made considerable equity investments to support export flow including barges, bagging facilities and a tobacco processing factory, although these investments are in no way comparable in scale to those made by the British and Japanese trading companies.

SECTION 3

TRADING COMPANY REQUIREMENTS FOR SUCCESS

We have stated previously that the trading company concept is first and foremost a structural response to resolving problems peculiar to international trade. As such, the concept must compete against alternative means of dealing with these problems such as direct exporting by the manufacturer. In addition, the problems of the marginal or nonexporting small and medium-sized manufacturers must be factored into the requirements picture.

Although the form of a trading company may change to meet the requirements of particular industries or particular markets, in our judgment is is possible to generalize on the requirements needed by a trading company if it is to deal with the unique problems of international trade and to succeed against other structural forms and the variety of foreign competition.

A. An Export Trading Company must have strong ties to manufacturers. It takes time and money to penetrate foreign markets. To be successful the trading company (in fact, any company) must intimately know its markets. The company must identify the end-users of its products, establish the buying practices of those who will purchase its goods, where in the world it should marked based on growth and potential, the strenths and weaknesses of competitors it will face, the nature of tariff and non-tariff barriers likely to be encountered and still other business considerations. In addition, the company must develop a sales approach and promotion material in the appropriate languages, if necessary. Without a lasting tie to a manufacturer it is not economically justifiable to perform these activities.

To compete effectively against other companies, investments in export infrastructure both domestically and in foreign countries is often called for regardless of the location of the investment. In today's markets a great deal of capital is often needed to penetrate a market and

sustain or increase market position once established. Again, if a lasting tie to a supplier is not highly likely, investment cannot be economically justified. Without continued investment into a market, the competitive capability of the trading company quickly reaches a plateau--at a low level of sales, aggressive suppliers have no reasonable alternative except to "go it alone."

Lasting relationships between a trading company and its suppliers are likewise important to the foreign buyer. Particularly in capital goods a buyer is looking for staying power on the part of the company he is purchasing the goods from. He will want service over the life of the product and if he does not feel that his supplier (the trading company) is going to be around or handling the line of goods he is interested in, he will look for alternative sources of supply. The image of dependability is closely related to the tie between manufacturers and traders. Dependability is important to expanding demand for the product or increasing the supplier's share of the foreign market.

A third reason why strong ties to supplying manufacturers are essential to trading companies directly relates to efficiency, operating expenses and effective use of human resources. The more quickly suppliers turn over, the more time trading company management must devote to finding new suppliers. As this can involve considerable time and market research, it is an expensive overhead operation. Minimizing turnover reduces operating expenses and results in more effective use of the salesforce time as there is no need to re-educate buyers on what they sell. In short, reducing turnover of suppliers reduces unit costs and hence can make the product more competitive in the marketplace--or increase the profitability of the trading business.

B. Export Trading Companies must be product specialists. This requirement emerges partly out of the need to create a sustained relationship with a manufacturer. One of the important ways a trading company can keep a supplier is spending as much time marketing the product as the manufacturer could. This means putting at least one man full time on the staff per manufacturer relationship. Any less manpower

than this automatically means the manufacturer can spend more time marketing his product than the trading company must spend time with each product it offers if it is to compete successfully in the marketplace. Regardless of the number of goods in which a company trades, it must be an expert in each. It is not how many products a trading company deals in which counts toward success, but how much capability it has to market each. Without product specialization, the trading company cannot hope to compete against others in the marketplace who are specialists and without competitive success, the company cannot maintain a lasting relationship with its suppliers.

C. Export Trading Companies must have strong foreign sales networks under their control. One of the most important characteristics of a trading company to its suppliers is international business know-how. But this know-how is useless in the absence of results. Results require a detailed understanding of product needs and someone who can respond to those needs by contacting product end-users. Trading companies must be represented by a competent sales force in every country in which it seeks business. Sometimes this representation can be accomplished by utilizing established foreign distributors, but often effective results can only be achieved by establishing a presence of a trading company. The trading company must invest, at a minimum, what its suppliers would invest if they were going directly to the same marketplaces. The ability to use the same office to support the marketing activities of a group of products rather than just one product is one of the real economies unique to trading companies.

D. A trading company must have depth and continuity of management. Management depth is important to both suppliers and buyers of a trading company. Manufacturers are wary of utilizing agents or distributors for international sales when they perceive that no more than one man holds the organization together. The threat of losing their penetration into foreign markets is too high. Perceptions of insufficient depth or continuity by manufacturers also leads to quick terminations of trading company relationships once export volume starts to build. A significant number of small companies interviewed indicated this was one of the major reasons they ended relationships with ETC's.

Perceptions of insufficient depth or continuity of management are also significant obstacles in building export volume from the foreign buyer's end. Buyers are likewise wary of purchasing goods from what they perceive as organizations without substance. Particularly in capital goods, buyers want to feel that they will be able to get service over the life span of the goods. The stronger the distribution system, the more organization he sees, the more confidence a buyer will have in dealing with the trading company.

A number of sources have indicated that the real strength of the Japanese trading companies, outside of their financial clout, is "The Mitsui Man"--the typical line trading officer. This man is probably in his mid-thirties and joined the trading company after college at the age of 22. He is quickly sent, for example, to Brazil for two to three years. He carries memos, documents around the office and sits in on meetings, but largely makes little contribution--except he learns about the company's business in Brazil, trading in general, and Portuguese. He may then return to Japan and work in the accounting or coordination groups and then perhaps in the steel group. By the time the man is 35, he may be semifluent in two or three languages, know the customs in several foreign countries and know the art of export trading inside out. While the circumstances are peculiar to the Japanese trading company, the ranks of the European trading companies are filled with men of similar background. It is the competition which an American trading company must meet.

E. The Trading Company must have the ability to create credit. In the highly competitive world of international trade, the ability to offer credit terms to foreign buyers often means the difference between winning or losing sales. Over the last several decades the ability of exporters to sell for cash with order on a confirmed irrevocable letter of credit basis has been substantially reduced. Part of the reason for this change is other industrial nations are rapidly becoming competitive to the United States in advanced technologies. As export competition becomes more severe, the availability and terms of financing become more decisive. The Ex-Im Bank has documented on several occasions that to

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conclude many export sales it is necessary to extend loan maturities or even simple short-term credit arrangements. Thus, it is increasingly necessary for the exporter to offer terms such as cash on arrival of documents or goods or even open account sales or installment payments spread over a number of years. Some of the funds necessary to offer credit terms can come from banks and other financial intermediaries, but growth demands that much of these funds come from the exporter--the trading company.

If credit is important to buyers of goods, it is also of equal importance to suppliers--particularly small and medium-sized businesses. Frequently, the working capital requirements needed for a large international sale are difficult if not impossible for the small firm to come up with. The extended payment schedules needed to close sales are also obstacles to the small firm. Further, even when credit terms are not lengthy, the time between shipment of goods and receipt of payment may run 180 days or more, straining the small firm further.

In the final analysis it is as important for a trading company to be able to offer credit to its suppliers as its buyers unless the trading company is associative in nature and the firms associating to form the trading company are not capital deficient. This requirement is even more important today than just 20 years ago because of the high costs of penetrating products-markets around the world and it is becoming more important with each passing year.

F. Trading Companies must have sufficient diversity of products and markets. One of the principal characteristics of a trading company is its inherent ability to diversify and hence lower its overall business risk. Each product and each market brings with it not only opportunity but threats--threats are not always parried. If a large competitor wants to buy into a market and pick up costs elsewhere, he will. A strong supplier may be acquired by a company with a sizable international activity and terminate the trading relationship. A strong devaluation could ruin a product's saleability in a country or a reevaluation of currencies could alter radically the competitiveness of specific products against foreign competition.

> The trading company must be able to accept these risks of doing business without undue threat to survival. The only way to lower the overall risk is to have a sufficient number of product/markets in the trading companies' sales "portfolio."

Exhibit II-9 summarizes the requirements of success for trading companies.

EXHIBIT II–9

TRADING COMPANY REQUIREMENTS FOR SUCCESS

A. A Trading Company must have strong ties to manufacturers.

B. Trading Companies must be product specialist.

C. Trading Companies must have strong foreign sales networks under their control.

D. Trading Companies must have depth and continuity of management.

E. Trading Comoanies must have the ability to create credit.

F. Trading Companies must have sufficient diversity of products and markets.

SECTION 4

GENERAL ECONOMIC FACTORS CONTRIBUTING TO THE ABSENCE OF TRADING COMPANIES IN THE UNITED STATES

A rigorous economic analysis of why trading companies never developed in the United States to the extent of those in Europe and Asia is beyond the scope of this study. However, four fundamental factors have been established which have had a strong influence on the absence of such companies in the United States:

1) availability of natural resources;

2) early emergence of the Industrial Revolution in the United States;

3) size of the domestic markets;

4) the Profit Center concept of management.

A. The availability of natural resources has had a profound impact on the pattern of development of the United States. As stated in Section 1, the theory of mercantilism and the concept of the favorable trade balance had a strong impact on Europe, leading to the development of colonial empires and trading companies. The concept of mercantilism is thus closely related to self-sufficiency. None of the European powers of the 16th, 17th and 18th Centuries or Japan for that matter has had the degree of self-sufficiency that the United States had had until recently, primarily because of their lack of the range of natural resources necessary to provide these countries with the standard of living they desired. Correspondingly, exports of goods and services were necessary to pay for these imports. In contrast, the continental United States has had for most of the history of this country an adequate supply of all the natural resources necessary for its development. Self-sufficiency in metals, minerals, and fuel was for decades a fact of life for American industry. Accordingly, the United States Government did not have to take initiatives designed to promote exports as did European and Asian Governments.

B. Early emergence of the industrial revolution in the United States had a far-reaching impact on the need for United States trading companies. Among other benefits, the industrial revolution propelled the United States to the technological forefront of the world's societies. It provided for the early development of the railroads which made transportation of natural resources to production centers around the country feasible and distribution of manufactured goods throughout the country as well. The early emergence of the industrial revolution in the United States had the effect of making the country even less dependent on imports to achieve a desirable standard of living--increasing the degree of self-sufficiency of the country. In contrast the development of the industrial revolution had the opposite effect on Europe and Asia.

In Europe, industrialization called for more imports of raw materials than ever before and hence more exports to pay for them. In Japan, as mentioned previously, survival was an issue, as industrialization of the Western powers had brought with it superior military strength. Japan desperately needed exports to pay for the costs of importing industrial processes necessary for military might. In addition, unlike European nations, Japan lacked the experience of centuries of mercantilism which might have provided her with sufficient capital and know-how to mobilize for international trade. The solution the Japanese Government favored ultimately led to the development of the general trading companies.

C. The size of the domestic market has probably had the greatest impact on the absence of large trading companies in the United States. The two strongest qualities of the trading company concept are its risk pooling nature and its ability to reduce many faceted transaction costs to a minimum. These qualities are far more important to large import transactions and large volumes of export trade than domestic trade where transaction costs (such as shipping, insurance, financing) are relatively small and easily handled in a common culture.

In contrast to every other country, the size of the United States markets for manufactured goods is immense and until recent years has been among the fastest growing in the world. Thus United States manufacturers did not need to search for foreign markets to sustain growth. The strategic

incentive to seek foreign markets was not present. The combination of sufficient natural resources and a high level of industrialization resulted in high per capital income and demand for more and more consumer goods.

European companies on the other hand were faced with limited domestic markets and sustained growth and national prestige depending on economic growth through exports. Trading companies grew up to respond to sales opportunities generated by individuals in the old colonial empire areas and as mechanisms to support a host of products with a single (and less costly) distribution system. In Japan, once established, the trading companies grew steadily. Encouraged and protected by the Japanese Government, the number of commodities in which trading companies dealt rose sharply, the network of foreign offices grew and Western companies and governments were made aware that dealing with the Sogo Shosha was the best way to penetrate into Asian markets.

D. The profit center concept has also played an important role in the absence of trading companies in large United States enterprises. Today, the American business community is comprised of many companies with the same internal elements as a trading company. Many large American companies have manufacturing operations, financial subsidiaries such as credit corporations, own transportation vehicles and even self-insure themselves against loss. Companies like General Motors, Ford, General Electric and Borg-Warner (to name a few) fit this description. Yet none of the largest companies in the United States ever developed into a trading company in the British or Japanese sense. Two reasons seem to emerge as the reasons why not: the relatively small size of export sales for these companies for many years and the profit center concept of management.

Under the profit center concept, the responsibility for the performance of individual business is placed on one man: for example, the utility turbine generator business. This man naturally wants to control all of the decisions which affect his business--at least internally. Early in their development, some companies, like General Electric, formed trading companies to handle the development of foreign business (most were, however, called International Divisions). But the profit center concept worked against them and most internal trading companies of United States firms have failed.

The case of the General Electric Company provides a good example of how the concept failed. At first, the trading company tried to promote foreign sales of all General Electric products; however, with the diversity and cost of products, it took a lot more time and effort to sell some products than others. For example, radios and other electric equipment could be sold easily while sales of electric utility power turbines could take years. As a result, the international trading divisions tended to spend more time on products with definite sales potential, while other products lagged in attention. Transfer prices were established to charge business lines for the time the trading group spent developing sales.

Managers responsible for the profitability of the business lines complained that they did not have real profit authority. There was this "trading company" charge they could not control and often could not see the benefits from. Managers whose lines were not being pushed complained that they were forced to miss out on real potential abroad. When General Electric ended the trading company function, no one was unhappy. In effect, the same "do it yourself" philosophy which runs through small exporters extends all the way through the largest American multinationals--perhaps this philosophy is part of the American pioneer spirit.

The next part of the report will develop more completely, commercial, banking and legal reasons which have constrained the growth of trading companies in the United States.

PART III

CONSTRAINTS TO FORMING TRADING COMPANIES IN THE UNITED STATES TODAY

In the previous section we discussed some general economic factors contributing to the absence of trading companies in the United States. But there are other constraints, legal, market-oriented and financial which futher contribute to their absence by preventing the independent export units in the United States from achieving the requirements necessary to achieve trading company status.

This part of the report explores these constraints, some of which are more important than others, and further explores the nature and character required for an American trading company and what changes are needed to create a viable environment for their existence within the United States.

SECTION 1

LEGAL CONSTRAINTS

Because large trading companies are an uncommon organizational form in this country, it is logical to address the question of whether such organizations are legally possible to create in the United States or if specific legal restrictions impair the viability of the concept. In this section we examine the legal ramifications of the export trading company concept, specifically addressing the ability to create organizations which can meet our requirements for success.

Webb-Pomerene Export Trade Act

A. The Webb-Pomerene Export Trade Act of 1918 permits groups of businesses to export through a single sales agency or "association" by declaring that the Sherman Act should not be construed as declaring illegal an export association "entered into for the sole purpose of engaging

in export trade and actually engaged solely in such export trade or an agreement made or act done in the course of export trade by such association." The act is an exception to our principal antitrust laws which ordinarily prohibit competitors from acting together.

Companies associating under this act are not entirely free of the antitrust laws, however. Earlier this year, the Antitrust Division of the Department of Justice published an "Antitrust Guide for International Operations" commenting on this issue. It states:

> A special antitrust exemption is provided under the Webb-Pomerene Act for acts of a collective export association of American producers, provided that the association does not (i) artificially or intentionally restrain United States domestic trade or affect United States domestic prices, or (ii) restrain the export trade of any United States competitor of the association The Webb-Pomerene Act applies solely to the export of "goods, ware, or merchandise" and, therefore, does not explicitly extend to service and licensing transactions. An association must be limited to domestic firms. (Footnotes deleted.)

1. <u>The Act is in part intended to benefit smaller manufacturers.</u>

The intent of the Act is to promote, encourage and expand export trade on the part of the United States, with particular emphasis on small and medium-sized businesses. During the congressional debates on the proposal, Congressman Edwin Y. Webb stated:

> In order to build up an export trade it is necessary to have the most expert representatives in the foreign trade fields to introduce and thoroughly advertise our American goods. This involves a large expenditure of money before the trade can be established. A number of our larger enterprises are able to do this alone, and for this reason, the proposed law would not greatly benefit these large enterprises, but our smaller manufacturers and merchants would be prohibited from undertaking such an enterprise because of the tremendous costs that it would involve.

2. The fact that the concept under study is intended to benefit smaller manufacturers is important.

Small and medium-sized manufacturers are clearly eligible to participate in Webb-Pomerene Associations. As long as the associations or agreements are developed solely for the purpose of export trade and do not restrain trade within the United States, export trade of other domestic competitors, or affect domestic competition, the activities are permissible. Because of their size, groups of smaller manufacturers are unlikely to engage in activities which would restrain domestic trade. Thus, the Webb-Pomerene Act allows smaller business to organize and act consistent with the criteria for success discussed in Part II-Section 3. The Act allows, for example, strong ties to manufacturers (who may actually own the association), as well as the ability to integrate either horizontally or vertically. The associations may serve as central selling agents for the members, taking orders, negotiating sales, and handling the exports of its members. They may retain certain functions in export trade such as buying members' products and reselling them abroad at terms agreed upon by the members. Methods of selling may be combined, e.g. with members using their established agents for some markets and the association sales office for others.

B. The Webb-Pomerene Act does not provide a legal basis for enforcing the requirements for a successful trading company.

Three issues of some significance to the successful operation of a trading company can be addressed from a legal point of view:

- the ability to require suppliers to operate through the trading company for a prescribed period of time once they agree to initiate a relationship;
- the ability to require suppliers not to export independently in competition with the trading company;
- the ability to get a clear definition of the degree of impact on domestic markets which would constitute a violation of the antitrust laws.

1) It is permissible for a Webb-Pomerene Association to require that members agree not to withdraw from the association or export independently of the association for a "reasonable" period of time.

We have mentioned that it is extremely important for the trading company to create a strong tie to its suppliers. We examined the question of how long it is legal to bind members. While the law states a "reasonable" period a time is permissible, it is not clear what period of time is reasonable. In court cases, periods of ten years or more have been declared unreasonable, while for stable organizations, periods of from one to two years are considered reasonable. It may be possible to bind an intial group of suppliers for five years to a new and hence "unstable" trading effort.

2) Preventing suppliers from selling their products to a competing domestic exporter is a clear restraint of trade and would not be permissible under the Act.

Legal cases have held that preventing a member of a Webb Association from selling his product to another domestic exporter is beyond the antitrust exemption provided by the Act. It is also legally unacceptable for an association to create territorial rights to markets it has developed by requiring that any member's export trade, after withdrawal, be handled by or through the association.

3) The inability to get a clear definition of what export action by an association constitutes a violation of the antitrust laws in a fundamental weakness in the usefulness of the act.

Compared to other trade laws, few cases have been decided as to activities permissible under the Act. For example, there are conflicting legal definitions of what constitutes an excessive degree of concentration. Such uncertainties have certainly affected the decisions of companies considering participating in or forming Webb Associations.

C. The domestic market share of association members in specific industries will have a significant impact on the association's freedom to act.

We were also concerned about the legality of other specific actions, such as offering various government assistance programs to Webb Associations or other trading company concepts in the event that such actions were desirable and appropriate. In order to obtain an indication of possible legal difficulty, a meeting was held with Joel Davidow, head of the Foreign Commerce Department, Antitrust Division of the Department of Justice. His opinion was that such programs are frequently made available to various industrial sectors of the United States economy. As long as a Webb Association or any other trading company concept did not consist of firms who dominated specific domestic markets, then no antitrust considerations appeared to be involved. In general, the attitude held by Justice is the less the share of domestic market share held, the less the chance of any antitrust problems. Since the concept under consideration is specifically oriented to smaller companies, such industry concentration seems impossible.

D. There are a number of organizational weaknesses of Webb-Pomerene Associations.

The Act has appealed to businesses dealing in basic raw materials and commodities. Most associations have been formed to deal in one product or product line. They tend to be products with little or no brand identification, with competition based largely on price alone. Usually, they involve industrial commodities like carbon black and sulfur, raw materials like flour and lumber. Over 50 percent of all the Webb-Pomerene associations ever formed have dealt in food, wood or paper products. Webb Associations are almost entirely horizontally integrated. Companies which sell a product with brand name identifications have had an almost impossible time making a Webb Association work. An exception to this statement appears to be Amatex, which was discussed previously, and which does turnkey projects for manufacturers of textile equipment. However, Amatex views itself as a supplementing sales agent of its members, and therefore has less of a problem with name identification.

In sum, although there are some uncertainties, the statute provides a legal basis for organizing and operating a trading company consistent with the criteria we deem essential to success. An extensive legal review of the Webb-Pomerene Export Trade Act is found in Appendix B.

Antitrust Barriers to Creating Vertically Integrated Trading Organizations

Webb Associations, as noted, are predominately horizontally integrated companies. In addition to examining the legal consequences of organizing horizontally, we felt it was also necessary to consider the legal consequences of organizing under a different concept. We posed the question whether one could create a vertical association of manufacturers, insurers, shippers and others designed to market products exclusively in foreign markets.

A. If a vertical arrangement has no effect at all in the United States, the courts lack jurisdiction.

The answer to the question posed above ran parallel to the analysis of Webb Associations. If the arrangement does not have an impact on the United States markets of the individual members of the trading vehicle, if it does not squeeze competitors out of foreign markets or monopolize the lines of commerce, and if the arrangement does not foreclose the competitors of any of the parties from a segment of the market otherwise open to them, depriving them of a fair opportunity to compete, there are no antitrust consequences.

Obviously, vertical arrangements lend themselves to abuse; however, in practice repetitive contracts between manufacturers and those engaged in transporting and distributing products is the prevailing method of dealing in foreign markets. The arrangement is subject to attack only if it is shown to restrain trade. Assuming that shippers, insurers and others are not prevented or precluded from conducting business with firms outside of the vertical arrangement, an association involving smaller manufacturers is highly unlikely to cause antitrust difficulties. Other forms of vertical organizations involving manufacturers producing related but noncompetitive products would be viewed in a similar manner.

SECTION 2

COMPETITIVE AND MARKET CONSTRAINTS

We have previously described what we consider the requirements of a successful trading company. This section addresses the question of whether there are competitive or market forces which constrain a trading company from operating in a manner needed to succeed in foreign markets.

We specifically consider the United States manufacturer and the market and competitive problems a United States trading company would face starting from scratch. In addition, we discuss what additional characteristics a trading company will have to have in the United States to bring substantial numbers of manufacturers into export trade.

A. Control is the overriding objective for American managers and in exporting this desire will prompt companies to use direct distribution as early as possible. In Part I, Section II we mentioned that the American manager will opt for "going it alone" over other means of marketing his products abroad in order to gain control over activity and profit. This motivation of United States businessmen to control is critical to an understanding of why trading companies have never thrived in the United States.

B. The desire for control to a substantial degree impairs the ability for an American Export Trading Company to possess strong ties to manufacturers. Strong ties to manufacturers are the greatest needs of a trading company. We explained that the great strength of the Japanese trading companies was due to their control over the manufacturing sector and that British trading companies created their ties to the manufacturing sector by "controlling" end-markets. Without strong ties to manufacturers there is no economic justification for a trading company to invest in specific product/market investments to build exports and create a high level of supporting infrastructure. Without such investments the trading company cannot effectively compete against other companies who seek to penetrate the markets. If the trading company is not an effective competitor, the supplying company who depends on that

market for growth will terminate its relationship. To the extent that the manufacturer terminates a trading relationship as soon as volume increases to a breakeven level, the trading company never has the ability to invest in the market and so on. Without strong ties to manufacturers, it is also difficult to remain a product specialist--another requirement of success.

C. Small and medium-sized manufacturers are not greatly interested in putting up the money to form and operate a trading company. We found no interest on the part of manufacturers to buy into a trading company. In fact, we found little interest on the part of manufacturers, exporters and nonexporters alike, to utilize a trading company to execute their international business strategies. Capital limitations are part of the disinterest. However, the possible illiquidity of ownership shares is just as important a consideration. Another contributory factor to the disinterest is the belief that exporting is only the first stage of international business. Foreign direct investment is seen as the ultimate level of international interest and trading is perceived to be a far more basic approach. Nonexporting or marginal exporters generally just don't have the interest in exporting to consider investing in an export trading company.

D. An Export Trading Company concept to be successful must find its place in the early phases of development extending if possible to the point where a small company management will be willing to trade-off control for cost-effectiveness of effort. In the three phases of export development, "Introductory," "Results," and "Investment," the Export Trading Company concept can be expected to help throughout the first and into the second. The tests of whether the concept is worthwhile should be in whether it can stimulate interest and accelerate the introductory process, and whether it can extend its usefulness into the Results Phase, thereby serving small companies for a longer period than is now the case with Export Management Companies.

In addition to the market demands, the Export Trading Company must be able to delay the take-over of the exporting effort by manufacturers to support activities to identify and enlist new exporters. If the objective of the concept is to introduce as many new firms to exporting as possible, the trading company will need sound business underpinnings to absorb expenses incurred in identifying potential suppliers.

E. To substantially expand the number of firms exporting goods, the Export Trading Company will require depth and breadth of skills--and this objective will probably require the Export Trading Company to be "big." To achieve the coverage required to induce significant numbers of small and medium-sized companies to export, the Export Trading Company will have to have people identifying market-producer match-ups, calling on producers, and essentially spending the time necessary to help the company management make their decisions to export. To be convincing and, indeed, to deliver over the long run, the Export Trading Company must have a competence which will equate to an investment in technical and marketing skills both here and abroad.

F. To achieve this scale and competency, the Export Trading Company will need to benefit from the economies of scale achieved by its successful customers: it cannot sustain such a system with large numbers of very small accounts. We have concluded that one of the principal reasons that Export Management Companies have not grown into companies of more significance is that they can never gain momentum. Too many resources are required to develop new start-up customers to replace those lost through success. While the Export Trading Company can never expect to halt the outflow, extending the periods of affiliation should offer a significant opportunity for the Export Trading Company.

G. The Export Trading Company must offer two basic advantages to its customers which will encourage their sustained use: increased marketing competence and lower unit costs. To extend its appeal to customers, the Export Trading Company must do more than fill the company's needs during the Introductory Phase. What the Export Trading Company must be able to do is demonstrate through their ongoing operations that it would be difficult and expensive to duplicate their

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> activities on the customer's behalf. If this can be done, it will alter in a natural way the company's decision-making processes. It will make it less easy for management to believe that through control they could improve the quality and level of exporting efforts being expended on their behalf. These requirements, however, will mean that some substantial investments in infrastructure to support a significant foreign marketing effort will be required. Some means will need to be found to secure the front-end capital necessary for those investments.

From this perspective of the beginning exporter and his needs and problems, two key questions are raised: Is it possible, through the scale and sophistication of a relatively large American Export Trading Company to keep customers longer so as to take advantage of their success? Is the economic benefit derived from serving larger customers sufficient to finance the required marketing capability?

These are real feasibility issues for the Export Trading Company concept. We will provide a further discussion of them and recommendations in Part V.

SECTION 3

FINANCIAL CONSTRAINTS

As stated previously, the ability to offer terms to foreign buyers often means the difference between winning or losing sales. The scope and variety of export financing have grown rapidly since World War II. Until that time exporters had generally relied on working capital loans, short-term advances against documents evidencing shipment of goods and the credit extended to overseas buyers by foreign banks which subsequently borrowed from United States banks with which they had arranged lines of credit. In addition to these financing methods new ones have been developed in recent years, the more important of which are purchases by banks from United States exporters, without recourse, of the obligations of foreign importers and the extending of direct loans by United States banks to foreign importers for the purchase of goods and services from United States suppliers.

A. Today, sales of goods by United States exporters to foreign importers generally are made on the basis of six methods of payment:

1) an export letter of credit opened by order and for account of the foreign buyer in favor of the domestic seller;

2) dollar draft drawn by the seller on the buyer;

3) authority to purchase or authority to pay;

4) cash deposit in advance of shipment;

5) open account; and

6) consignment.

When the credit standing of the buyer is unknown or uncertain, the risk to the seller is greatest and the "cash in advance" method is desirable. On the other hand, when little or no risk to the seller is involved, export sales are likely to be made on an "open account" basis. Generally,

risks are between these two extremes and the greatest volume of exports are handled by either letter of credit or dollar drafts. Exhibit III-1 briefly explains these financial methods.

B. The competitive nature of the credit arrangements arises from the conditions of employment, maturity arrangements and cost of the various methods of financing. Frequently, conditions for letter of credit sales in foreign countries sometimes calling for prepayment of all or part of the principal for periods up to a year. Obviously, the seller who demands letter of credit conditions under these circumstances can easily be in a noncompetitive position. On other occasions foreign buyers may be only able to acquire a bank loan in their own country at very high rates. Thus, the ability of the exporter to finance transactions at his own risk--create credit--can be a significant competitive advantage.

C. In the United States, the ability of a company to create credit is strongly related to the level of its net worth. The amount of money a firm's owners have invested in the business and the sum of its retained earnings--the worth of the firm--is extremely important to credit lenders. Raw materials suppliers and bankers look at this value to judge how safe their stake in a firm is. They are careful about extending their lines of credit, whether that be in the forms of accounts payable or bank loans.

In turn, the level of net worth required for particular businesses is related to the kinds of assets needed to perform necessary functions and tasks. A capital intensive business such as manufacturing of heavy machinery thus requires a greater level of net worth per dollar of assets than a sales organization whose basic requirement is people.

D. In relation to its sales potential, a trading company requires a relatively low net worth. It is not a very expensive proposition to start a trading operation. Figuratively speaking, just a few knowledgeable men, a telex and a small office operation are necessary to start an export sales organization. Hypothetically, this organization can sell an almost limitless amount of goods relative to the net worth necessary for them to operate. While we are not implying that a trading company is in any way such a small or unsophisticated operation, it is by and large a marketing mechanism which requires small levels of net worth relative to its sales capabilities.

EXHIBIT III-1

BASIS OF SALES IN INTERNATIONAL TRADE

Export Letters of Credit

A letter of credit is essentially a declaration by a bank that it will make certain payments on behalf of a specified party under specified conditions. It is called a "letter" because it takes the form of a notification to the party or parties likely to be the recipients of the payments.

The value of the letter of credit to the exporter is that it authorizes him to draw drafts on a bank and by presenting the prescribed supporting documents, to receive funds. The ultimate collection of those funds from the importer is the work of the banking system and no concern of the exporter

Dollar Draft

An export draft is an unconditioned order drawn by the seller on the buyer instructing the latter to pay the amount of the draft either on presentation (sight draft) or at an agreed future time (time draft). Unless a bank "accepts" the draft (agrees to pay it at a stated future date), the total risk of default remains with the seller.

Authority to Purchase or Pay

The authority to purchase is an instrument used primarily by banks in the Far East as a way for their clients to make payments for goods bought abroad. It authorizes the exporter to draw documentary drafts on the buyer or on the buyer's bank. It specifies a bank in the exporter's country where the exporter may negotiate drafts drawn under the authority. Unless the authority specifically states otherwise, the seller's draft is negotiated with recourse – that is, if the buyer fails to pay the draft at maturity, the holder of the draft has recourse to the seller for payment.

A variation of the authority to purchase is the authority to pay. Under an authority to pay, drafts are drawn on the bank designated to negotiate the drafts. Once the drafts have been paid, the beneficiary is no longer liable as drawer.

Cash Deposit in Advance

This method calls for payment in cash, in whole or in part before shipping merchandise. Although this payment arrangement affords the seller the greatest protection, it is disadvantageous to the foreign buyer. In some countries, local exchange control restrictions prohibit such payment.

Open Account

In this kind of transaction, the arrangement between buyer and seller provides for payment at some specified date but without any negotiable instrument evidencing the obligation. Legal procedure to enforce payment in case of default are often very complicated.

Consignment

Under a consignment arrangement, goods are not sold but rather consigned to the foreign importer. The exporter retains title to the goods until they are sold to a third party. As in the case of sales on open account, no tangible obligation to pay is created and it may be different to obtain payment if the importer defaults.

E. The relatively low net worth position of any United States Export Trading Company translates into a relatively small ability to credit, almost regardless of the credit worthiness of the foreign buyer.

On the surface, it would appear that the crucial limiting conditions on the amount of money a trading company could borrow or finance is the credit of the foreign buyer. If the foreign buyer has an excellent credit record, there appears to be little reason for not granting sufficient credit to fund a transaction, no matter how large. In fact, the net worth condition of the trading company is still the limiting factor on the size of the credit commitment attainable by the trading company from a bank if the trading company takes title to the goods. The limitation on credit is a function of two risks that are not covered by the buyers credit:

- Acceptability of the Goods

  If for any reason the foreign buyer refuses to accept the goods once they arrive in his country, the bank will look to the title holder for payment. Thus the net worth of the title holder is the important limiting condition. In the case of dispute, substantial risk is still involved. If the bank is put in a position where it must sell the goods on the open market, it can likely result in it getting only pennies on the dollar value of the goods. While percentage-wise nonacceptability is a rare occurrence, it can be a rather expensive mistake for a bank and because a great percentage of export financing is done by a relatively small number of international banks, these banks are quite cognizant of the threat and deal with it accordingly.

- Warranty Issues

  Malfunctioning of goods after delivery, but before full and sometimes any payment is made is another threat to the banks that the foreign buyers credit worthiness will not cover. While a trading company may service or arrange for service on the goods or have a claim against its suppliers, the threat to the bank still argues against extending more credit than the trading company's net worth position will support.

F. Without a greater capability to create credit than a net worth position would justify, it is our judgment that an American Export Trading Company will not prove feasible. Without the ability to extend credit creation beyond typical net worth criterion, we are convinced that a viable export trading company cannot exist in the United States. There are two major factors which lead us to this conclusion:

- The size of the trading company will be severely limited. The ultimate size will be affected both by its limited ability to finalize sales against foreign competition which have the capability and desire to use credit conditions to strategic advantage and the trading company's limited ability to invest in penetrating markets due to its non-competitiveness in the market place.

- It is our opinion that the ability to create credit is the strongest weapon the trading company can have in delaying manufacturers' decisions to "go it alone." By being able to extend credit terms to foreign buyers an incentive is cerated for manufacturers to utilize trading companies. The combination of this incentive and a strong network of distributors under the control of the trading company should delay the take-over decision of enough firms long enough to create the basis for a viable trading company.

To achieve financial viability an American Export Trading Company must have an economical means of overcoming the acceptability of goods and warranty issues.

G. The ability of an American Export Trading Company to create credit will have to be given support by the United States Government. We believe that the net worth issue cannot be solved without government assistance. While a few banks offer to accept drafts on foreign buyers from American exporters, the level of drafts which may be accepted for each company is, of course, limited and somewhat costly. Such a service would also have to be substantially expanded to serve the needs of thousands of additional manufacturers operationg through export trading companies.

H. We believe that the most practical approach to solving the credit needs of the export trading company is through the availability of guarantee insurance similar to that provided by FCIA and OPIC on drafts which an export trading company draws on foreign buyers. The concept of this recommendation is that if the banking community is protected against losses through insurance on the underlying risks of an international transaction, then the drafts drawn by export trading companies on foreign buyers will be a safe investment and the subsequent market of these export trading company acceptances will open up the export trading company's ability to create credit through conventional banking channels.

Exhibit III-2 illustrates the commercial risks attendant with international trade. With the exception of cancellation of orders before shipment, nonacceptability of goods on arrival and importer default due to warranty issues all these risks can be insured against by either marine insurance or FCIA/OPIC insurance (Exhibit III-3). We believe that a special export trading company policy should be developed to cover the two risks mentioned previously and deductable policies and other operational issues reviewed and changed as appropriate to maximize the applications of such a policy. We firmly believe that such a policy is workable and can be provided at a reasonable cost. The First National Bank of Boston offers to accept drafts on foreign buyers from American exporters for a flat 2% on each collection. Under this acceptance the bank takes the risks of acceptability and warranty in consideration.

I. At this time we see little support for offering the above kinds of insurance to an export trading company within the United States Government. The banking community, however, appears to be supportive. We discussed the concept of extended commercial insurance as a way of creating a viable export trading company with officials of the Export-Import Bank, Treasury Department, FCIA, the Private Export Funding Corporation (PEFCO), and a large group of commercial bankers. We found little support from within the government. Among the principal difficulties is the lack of experience and capability in examining warranty issues and the conviction that exporters must assume some risk for default. Although officials concede that a trading company may require such a unique policy to support its growth, many other companies also desire such coverage and offering it to one group and not to all groups is difficult problem to overcome.

EXHIBIT III–2

COMMERCIAL RISKS IN INTERNATIONAL TRADE

BEFORE SHIPMENT

- Cancellation of Order
- Importer becomes Insolvent

DURING SHIPMENT

- Marine risks, physical loss or damage caused by
  - perils of the sea
  - fire and explosion
  - collision, stranging and sinking
  - jettisons, assailing theives and barratry
  - latent defects of the vessel
  - faults or errors in navigation and/or management of the vessel
  - general average and salvage charges
- On-shore risks, physical loss or damage by acts of nature
  - sprinkler leakages and explosion
  - subsidence of docks and structure

AFTER SHIPMENT

- Importer refuses acceptance
- Importer defaults on payment due to:
  - warranty issues
  - commercial difficulties
- Importer becomes Insolvent

EXHIBIT III-3

EXPORT CREDIT INSURANCE THROUGH THE FOREIGN CREDIT INSURANCE ASSOCIATION

Created in 1961 to provide export credit insurance to United States exporters, the Foreign Credit Insurance Association (FCIA) is a pool of some 50 of the nation's leading insurance companies with combined assets in excess of $27 billion.

Working in cooperation with the Export-Import Bank of the United States, FICA insures United States exporters against commercial and political risks. While FCIA underwrites commercial credit risks, Eximbank covers political risks and reinsures a portion of the commercial risks.

Coverage includes:

- Short-Term Insurance (to 180 days)

  In the short-term field, it issues to exports 1) comprehensive insurance policies normally covering 90 percent of credit losses and 95 percent of political losses, or 2) political-risk only policies covering 90 percent of losses.

  Credit risks include failure of the importer to pay because of insolvency or protracted default. Political risks include currency incovertibility, expropriation, cancellation of import license, or other actions taken by foreign governments that prevent payment by the buyer. Premiums are charged according to the economic and political condition of the importing country and the terms of the credit.

  Generally speaking, FCIA requires an exporter to insure enough of his eligible short-term sales under this program to provide a reasonable spread of risk. Sales on cash and Letter of Credit terms may be excluded.

- Medium-Term Insurance (181 days to five years)

  This insurance is written on a case-by-case basis. The overseas buyer must make a cash payment of at least 10 percent of the invoice amount although 20 percent is preferred and may be required. The remainder is payable in installments and FCIA will insure 90 percent of this "financed portion" on a comprehensive basis, with the shipper carrying the other 10 percent at his own risk. In certain higher-risk markets the exporter may be required to carry a larger share of the financed portion.

  The same coverage is offered for political risk only, at somewhat lower premium rates. The program also provides for advance commitments and preshipment insurance coverage on consignment transactions and sales from consigned or warehoused stocks held abroad.

  It should be noted that under both the short-term and medium-term FICA programs, Eximbank carries 100 percent of the insured political risk; FICA carries 100 percent of the insured political risk. Proceeds both of short-term and medium-term policies are assignable to facilitate borrowing from the customer's commercial bank.

  In certain cases, commercial banks may be the named insured both under short and medium-term FICA policies covering exports of United States products for one or a number of named suppliers.

The overwhelming majority of commercial bankers was supportive of the concept (as there is no risk to them involved) and felt that such a vehicle could substantially expand the volume of United States exports. The appeal of the vehicle is that it requires absolutely no changes in the rules and regulations which currently exist within the banking industry or within the conduct normal to financing international transactions.

J. An indirect financial constraint on the development of Export Trading Companies is the inability to take advantage of profits on freight brokerage.

There is no doubt that the more integrated a trading operation, the greater profitability will be. Profitability will increase as a result of the addition of other profitable activities and will increase as a result of opportunities created by economics of scale. One activity that a trading company could easily perform and would provide an excellent addition to profits are commissions on freight brokerage.

Both manufacturers and the various types of trading vehicles normally go through a freight forwarder to:

- book passage on ships;
- coordinate delivery;
- perform documentation;
- sometimes prepay for shipment.

The freight forwarder received two commissions: one from the shipper, and one from the shipline. An export trading company or manufacturer can elect not to use a freight forwarder and perform the above services themselves; however, if a company takes title to the goods it is the shipper of record and is pervented by Federal Maritime Regulations from getting a commission from the carrier.

1. The standard commission to freight forwarders from shipping lines could yield a significant increase in the profitability of trading companies--causing them to be of

more interest to potential investors. The standard commission to a freight forwarder is 2% of the shipping cost of the goods to be shipped. According to our interviews with major exporters, freight costs themselves average between 15 to 25 percent of merchandise value, but can amount to 70 or 80% of the merchandise value. In general, the lower the value of the goods per pound of weight, the greater the merchandise cost will be. Exhibit III-4 illustrates two cases. In the case of the textiles exporter, profitability is seen to increase by 6%; in the case of the juvenile furniture exporter, his profitability increased by 16%.

EXHIBIT III—4

INCREASED PROFITABILITY THROUGH COMMISSIONS ON FREIGHT BROKERAGE

Case 1:	The Textile Exporter	
	Merchandise value	$100,000
	Shipping Costs (15% of merchandise value)	15,000
	Brokerage commission (2% of 15,000)	300
	Average pretax return on sales (5%)	5,000
	Return with commission on freight brokerage	5,300
	Increase in profitability	6%
Case 2:	The Exporter of Juvenile Furniture	
	Merchandise value	$100,000
	Shipping costs (40% of merchandise value)	40,000
	Brokerage commission (2% of 40,000)	800
	Average pretax return on sales (5%)	5,000
	Return with commission on freight brokerage	5,800
	Increase in profitability	16%

PART IV

THE EXPORT MANAGEMENT COMPANY

Part II of this report discussed one organizational response to world trade utilized by some of the United States major trade competitors. As mentioned previously, this structural export vehicle does not exist in the United States. This has been primarily because of (a) the historical development of United States trade growth, and (b) because of the underlying philosophy and business posture of American enterprises.

As was pointed out, historically the United States was a prime trade target area for its colonizers, rather than a trading nation. It furnished a market for finished European goods and a source for needed raw materials. As the United States grew into a developed country, its business posture turned inward rather than outward. The need for and interest in export trade was minimal due to the enormous unsaturated market potential found within its own continental boundaries. Additionally, developing this domestic market carried fewer of the problems and risks that were inherent in dealing internationally.

Therefore, immense domestic growth opportunity, coupled with (a) the political isolationist posture of the United States during its early history, and (b) the basic independent and entrepreneurial philosophy of American businessmen, left an indelible stamp on both the foreign trade vehicles utilized by American business and on the attitudes American businessmen hold towards exporting.

This section of the report will discuss in detail the characteristics of one of the prime trade vehicles currently utilized in the United States: the Export Management Company (EMC). The characteristics of this export trade, the major forms it takes, the functions it performs, and the problems and potentials it faces as a means of stimulating increased export trade on the part of small and medium-sized manufacturers will be discussed.

The methodology used in substantiating the conclusions that will be made in this section is primarily based on the survey of existing Export Management firms conducted for the United States Department of Commerce.

This methodology included the survey and analysis of a randomly selected sample of Export Management Companies to which a self-administered questionnaire was provided. Appendix B includes this questionnaire and the tally of major results. The sample was drawn from the United States Department of Commerce, Bureau of International Commerce's Directory of United States Export Management Companies, and was augmented by other mail-outs to specific Export Association members. An attempt was made to draw the sample to insure both a diversity in geographic location and of product category handled. A total of 287 questionnaires were mailed out of which 65 were returned due to either the relocation or nonexistence of the firm. Eighty-five questionnaires were returned and analyzed for the purpose of this report.

SECTION I

GENERAL CHARACTERISTICS OF AN EXPORT MANAGEMENT COMPANY AND ITS ROLE IN INTERNATIONAL BUSINESS

A. The Export Management Company is hard to characterize as its functions are not precise. Also, it is one trade vehicle in the spectrum available to manufacturers for exporting exterior to their own organization. As mentioned previously, there are many terms used for independent exporters in the USA. "Export Merchant," "Export Broker," "Combinational Export Manager" or "Export Management Company" (EMC), "Manufacturer's Export Representative" or "Commission Agent," and "Export Distributor" are all terms used to distinguish between various kinds of independent export-trading firms which operate as the exporting arm for United States manufacturers. However, these terms usually refer more to the nature of the services performed or the contractual arrangement with the manufacturer rather than to the character of the export firm itself.

Increasing the complexity in pinpointing the characteristics of an Export Management Company is the fact that one EMC rarely concentrates on only one of these services. It can function primarily as a commission agent for one manufacturer, while it may act as an independent distributor (i.e., purchasing the goods itself and reselling them abroad at a mark-up) for another manufacturer.

In addition, an EMC may concentrate in certain product lines or market areas, or it may be diverse. It may operate using agents ab ad, or its own sales people. The range of organizational arrangements are many as is the differences in the depth of marketing services offered from firm to firm. The findings of the EMC survey in these areas will be discussed in detail later in this report.

B. In general, the Export Management Company is a firm that acts as the exporting arm for a combination of manufacturers, dealing under its own name or the name of the individual manufacturer. It can function as the manufacturer's overseas representatives, receiving a commission on sales, or it can buy and sell products overseas on its own account. For the most part, an Export Management Company is a firm which acts as the export sales department for more than one manufacturer. The EMC may operate in two ways: (1) in its own name, or (2) under the name of the manufacturer, using the manufacturer's letterhead, invoices, etc. as if it were the manufacturer's internal export department.

In addition, it may act as an "independent distributor" purchasing and reselling goods under its own name for a price mark-up, or it may act as a "commission representative," functioning primarily as a marketing middleman for the manufacturer, receiving a sales commission on goods sold, but never taking title of the goods.

The degree to which an EMC takes title to the goods sold and bears the financial risk of the sales generally distinguishes between the two major types of EMC's: Export Commission Representatives or "agents" and the Export Distributor.

Briefly summarized, the Export Commission Representative is a firm that assumes all the duties of export management for the manufacturer except for credit risk. The manufacturer carries the overseas customer's account although the EMC may make credit checks and handle collections. Legally, the EMC may operate in the name of the manufacturer but it is not actually an agent in that it cannot legally commit the manufacturer, and the manufacturer has no legal responsibility over the EMC's actions. Also, the representative's sales are usually subject to approval by the manufacturer. This type of EMC receives remuneration for his work by sales commissions on the goods sold overseas.

The Export Distributor is a firm that buys goods from a manufacturer on its own account and then resells the product abroad at its own risk for an agreed-upon mark-up. In this relationship, the manufacturer deals with the EMC as he would with any other domestic customer while the EMC carries the account of the foreign customer and bears all credit risk.

C. The Export Management Company plays a vital role in stimulating exports from small and medium-sized firms which have no international experience. As mentioned previously, American manufacturers can enter the international marketplace in a number of ways. Often the EMC is a manufacturer's introduction to foreign trade.

As a manufacturer becomes more and more involved in exporting his/her use of an EMC may change. Manufacturers may license or directly invest in one market area where sales volume is high, and use Export Management Companies to develop the new product or market areas it is trying to penetrate.

In addition, the degree to which a manufacturer is involved in direct exporting may vary. One manufacturer may export through an international department or division, utilizing its own sales force abroad and handling all export procedures and mechanisms. Others may only have an export department and use foreign sales agents and distributors abroad. Likewise, the depth of services offered by an Export Management Company itself may vary anywhere from merely handling export documentation to serving as consultants in developing overseas marketing plans and strategies for clients, or actually purchasing goods and exporting them under their own name.

D. However, the long-term role of the Export Management Company in a manufacturer's international export picture is typically tenuous at best--EMC's are most often seen as an "initial step" to exporting. EMC's face the difficult problem of having client "mortality" built in to business success. For the most part, trade mechanisms can be viewed as a continuum of international trade involvement, with the manufacturer moving up the continuum from indirect to direct exporting as both his international business experience and his product sales volume in specific markets increases.

This puts the Export Management Company in the position of being the initial step on the ladder to export involvement in new or hard-to-reach markets, yet losing its client once it has developed the market

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sufficiently to allow it to reap greater benefits. Interviews with both EMC's and manufacturers substantiated that the independent nature of the American businessman eventually causes manufacturers who were achieving exporting success with EMC's to switch to a "go-it-alone" mode of trade.

There was little indication that the manufacturer would not eventually move up the trade involvement continuum. Most EMC's felt that suppliers would eventually drop their services because the manufacturers either wanted (1) more control over their export business, (2) felt they could do the sales job better, or (3) achieve lower per unit costs by cutting out the middleman.

The open-ended responses to the questionnaires also revealed that a major problem for the EMC was preventing its client from utilizing its distributor network once sales success was achieved. The EMC appeared to be constantly put in a dual defensive stance: one, against competition from other traders, and two, against potential competition from its own client.

The specific characteristics of the Export Management Company, the functions and services it performs, the clients and products it handles, its organizational structures and financial contraints will be described in detail in the following section in an effort to establish the constraints that must be overcome if a viable framework for a United States Export Trading Company is to be created.

SECTION 2

SPECIFIC CHARACTERISTICS OF EXPORT MANAGEMENT COMPANIES

A. Functional and Trade Direction Characteristics

1) Most Export Management Companies function primarily as "export distributors," buying goods on their own account and marking them up in foreign markets. The results of the survey of EMC's found that the majority (62%) of EMC's responding acted primarily as "export distributors" rathern than "commission agents." However, a substantial number (31%) indicated that they functioned in both modes of operations.

Only five of the respondents characterized their operations as being oriented to working primarily on commissions. However, this low agent response may be due to the fact that the sample was drawn from a universe of well-established Export Management firms which were registered with the Department of Commerce and were members of trade associations. Many EMC's start their operations as commission agents and move up the spectrum of services with continued growth.

When the responses to the questionnaires were analyzed to determine if the characteristics of EMC's that functioned primarily as "export distributors" rather than in a combination mode of both "distributors/commission agents," it was found that those who functioned primarily as "distributors" exhibited the following tendencies:

- They handled a larger number of product lines that tended to be high technologically in character.
- They had a somewhat broader role in handling the advertising, promotional, pricing and distributing strategies of clients.
- There was little difference in the size of the manufacturers they handled, the average number of such firms, or the average length of the relationship, their organizational structure, or their view of the competitive world.

- They were slightly better capitalized in terms of equity base and the frequency with which owners supported the business with personal guarantees, but had no greater advantage in terms of available external financing.

- They experienced a higher pretax return on sales on average (32% of the distributor/agents indicated having under a 5% return on sales compared to 27% of the distributors).

2) Export Management Companies function primarily as exporters rather than in combination of export and import trade. The survey results showed that most EMC's deal primarily in export trade rather than importing, licensing agreements or other types of trading. Ninety-three percent of the survey respondents indicated that over 75% of their current annual sales volume came from exports. In addition, over 61% of the respondents indicated that exports made up all of their sales volume.

Only 28% of the respondents indicated that they imported and of that 28% the majority (14% indicated that imports contributed less than 10% of their annual revenue. Only 7% indicated that imports contributed over a fourth to their annual revenues.

The use of licensing as a source of revenue was even less. Only 16% responded to dealing in licensing and its contribution to annual revenues never exceeded 10%.

It was interesting to note, however, that many EMC's saw licensing as the exporting revenue area that would experience the most growth by 1980. This fact seems to indicate that EMC's envision following the trend of American business towards direct investment modes of international trade rather than pure export-import trade vehicles.

3. Market Coverage Characteristics

1) Export Management Companies are global in nature; however, the trade patterns vary considerably between firms. Over two-thirds (67%) of all the respondents indicated that they traded in all trade areas which included Europe, Eastern Europe, Africa, Asia (excluding Japan), the Middle East,

Japan, Latin America and Canada. Canada and Eastern Europe were the trade areas receiving the least interest on the part of EMC's. Only 20% and 17% of the respondents indicated that they traded to Canada and Eastern Europe respectively, and the percentage contribution to sales of these areas rarely exceeded 10% of their annual export sales volume.

Africa was also seen as a relatively low trade area. Although 61% of the respondents indicated that they traded in this area, its percentage contribution of their total annual export sales volume rarely exceeded 10%. Japan was also a relatively low trade area. Only 70% of the respondents were in this market and it rarely contributed more than 10% to a firm's sales volume.

Latin America was the primary trade area for the majority of EMC's, followed by Europe, Asia (excluding Japan), the Middle East and Japan, in that order. Eighty-seven percent of the respondents indicated that they traded in Latin America, with that region contributing up to 100% of the annual sales volume of some firms. However, the percentage contribution to sales volume from this region most frequently hovered around the 25 to 50% range.

Eighty percent of the respondents traded in Asia, with this region contributing up to 90% of the sales volume for some firms. However, the percentage contribution for most firms hovered around the 10 to 25% range.

Seventy-nine percent of the respondents traded in the Middle East, with that region contributing up to 90% of the sale volume for some firms, but more frequently in the 25 to 30% range.

2) Most Export Management Companies saw the areas of trade emphasis for the future as remaining basically the same, with a slight reordering of the importance of the less developed countries. The survey responses indicated that most EMC's saw the Middle East as replacing Latin America as the prime area of good export growth in the next five years. Sixty-five percent of the respondents saw this area as having good future potential. Africa was seen as growing in potential while Asia (except Japan) and Europe were seen as declining. Japan, Eastern Europe and Canada continued to be seen as low potential areas.

3) The factors influencing an Export Management Company's trade pattern or the regions of the world in which it is active are related primarily to product characteristics and personal market knowledge rather than formal market opportunity. The prime reasons given as always being factors in the decision on which geographic markets to concentrate in were (1) market match with the product line, (2) knowledge of the market area, (3) in-country business contacts, and (4) availability of a distribution network, in that order of importance. Receptiveness of the local government to United States business, market exclusivity for the product, and the competitive environment from other export traders appeared to play a less important role.

C. Export Control Characteristics

1) Export Management Companies rarely handle all of a supplier's exporting business, and their services are discontinued on the part of the manufacturer after a successful level of sales growth. The pattern on the control which EMC's had over the client's entire export business varied considerably. The most frequently mentioned proportions for the EMC's role in the client's exporting were either under 25% (31% of the respondents) and between 75% and 100% (53% of the respondents).

Direct exporting by the manufacturer was the biggest competitor to an EMC's services. Of the various forms of other international business structures that suppliers used in addition to EMC's (i.e., direct foreign investment, direct exporting, cooperative or "piggyback" exporting, or other EMC's), ten percent of the respondents indicated that most of their suppliers used direct exporting as an additional export mode. This was the only exporting vehicle indicated as being used by most of the suppliers. However, other Export Management Companies and direct foreign investment by the manufacturer were indicated as being used by some clients, in that order of importance.

The primary reasons listed for the loss of a supplier relationship were (1) that manufacturers started their own export operations internally, or (2) that they merged with a company that had an international department. Exporting through another EMC or through a cooperative "piggyback" exporter were occasionally seen as a reason for the loss of the relationship,

but exporting through a foreign trading company, direct investment abroad on the part of the manufacturer or the decision to stop exporting were rarely seen as the reasons for suppliers taking alternative export actions.

The view among EMC's on the point at which sales success caused the loss of a client varied. On the average, the majority (85%) of respondents felt that suppliers would tend to terminate a relationship with an EMC when their export sales exceeded $200,000. However, almost 32% of the respondents felt that suppliers would leave them when sales volumes reached between $200,000 and $500,000: 29% believed that they would terminate at between $500,000 and $1,000,000 in export sales, and 25% felt they would terminate when sales exceeded one million dollars.

However, most EMC's were willing to lower their profit margins in return for longer-term contracts and client stability. Sixty-four percent indicated that they were somewhat or very willing to use this strategy, compared to 36% who indicated that they were somewhat or very reluctant. Only 24% indicated that they were very reluctant.

2) Most Export Management Companies felt that the suppliers beliefs that they could either (1) achieve better sales success themselves, or (2) accomplish the export function at a lower per unit cost, were the prime reasons for suppliers ending their export relationship with EMC's. The responses to the question on why most of the suppliers end an export relationship with a firm produced the following ranking of answers:

1. supplier believes he can achieve greater market penetration;

2. supplier believes he can accomplish the export function less expensively per unit cost;

3. supplier wants to control the foreign market;

4. supplier wants to export in geographic areas your firm does not handle.

Other answers to this question revealed that personal differences in policy between the manufacturer and the EMC, or the lack of sales success for the product line overseas often played a part in the termination of a relationship.

3) Export Management Companies saw increased client service, closer relationships and steady sales performance through market growth, as the major ways that EMC's could fight against the trend for clients to leave once sales volume was high. The respondents to the survey answered the question on how to retain suppliers who had experienced good growth in a wide variety of ways. However, the four steps listed most frequently were (1) developing a closer working relationship with the client, (2) showing continued growth through either geographic expansions or the expansion of the depth of market services offered the client, (3) development of longer-term and stronger contracts to prohibit the supplier from selling in the EMC's market, and (4) joint financial participation, either in terms of the EMC and the manufacturer jointly investing in some market development efforts, or in the passing on of cost reductions achieved by volume to the manufacturer.

In analyzing the wide variety of responses provided by the survey, the underlying thread running through them appeared to be that EMC's had to be able to convince the suppliers that they were performing an invaluable service which relied more on overseas market knowledge and performance than at-home paper processing. They also had to be more willing to work jointly with the manufacturers for their mutual gain, rather than sticking to rigid commission rates or procedures that made them viewed only as a "middleman" who could be replaced once sales volume warranted in-house staff. The manufacturers needed to know that they were not only getting good service and continued sales growth that would be more expensive and less ifficient if done internally, but also that the EMC was actually functioning has their "eyes and ears" overseas rather than merely processing orders.

4) Most Export Management Companies saw the prime role that the government could play in the aiding of the EMC's to maintain long-term relationships with the suppliers as revolving around (1) being educated on exporting and the EMC's role, or (2) legislation to help set industry standards and enforce the exclusivity of contracts. The survey respondents answered the open-ended question on the steps that the United States Government could take to encourage longer relationships between suppliers and EMC's in a wide variety of ways. However, 13 major categories (see Exhibit IV-1) emerged with the primary ones being increased efforts on the

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Exhibit IV-I

AREAS MOST FREQUENTLY MENTION BY RESPONDENTS AS AREAS THE U.S. GOVERNMENT MIGHT PLAY AN IMPORTANT ROLE IN AIDING THE ENCOURAGEMENT OF SUPPLIERS TO USE AND MAINTAIN RELATIONSHIPS WITH EXPORT MANAGEMENT COMPANIES

1. Positive publicity on the image and role of the EMC in exporting.

2. Public education to the manufacturers on both (1) the importance and (2) the realities and complexity of exporting.

3. Legal aid to EMCs in enforcing contracts and market exclusivity.

4. Legal aid in setting standards and uniform codes for EMCs, such a as developing prototype contracts with minimum term requirements "just cause" termination agreements, and cancellation fee clauses.

5. Tax incentives to suppliers for utilizing EMCs and having long term contracts with them.

6. Tax incentives to EMCs for expanding overseas.

7. Financial assistance to EMCs.

8. Aid to lower export prices to compete.

9. Aid to lower transportation costs and taxes.

10. Aid in stopping the unfair trade practices of foreign competitors.

11. Relaxation of antitrust laws which impact on EMCs' ability to integrate.

12. Better U.S. Department of Commerce sales leads and aid overseas.

13. More stability in exporting rules and regulations.

part of the United States Department of Commerce to educate the public to (1) the importance of exporting, (2) the realities and complexities of exporting, and (3) the positive role EMC's could play in developing this export market. It was felt that more positive publicity on the image and role of the EMC was a critical need if the EMC's were to be successful in attracting and keeping marginal or nonexporters as clients.

The second most frequently mentioned concern area for government attention was the need for legal aid to EMC's in setting standards and uniform codes for EMC's or protype contracts with minimum term requirements, just cause termination agreements, or cancellation fees that would enable all EMC's to compete equally and still be able to protect themselves or have some legal basis to prevent suppliers from encroaching on market exclusivity, or arbitrarily cancelling the relationship once a market was developed.

The third most frequently mentioned area of concern involved financial aspects and efforts the government could take to either lower EMC or supplier costs when utilizing an EMC. These comments included such things as tax incentives to EMC's to expand overseas, tax incentives to suppliers for working with an EMC or having a long-term contract, financial assistance to EMC's, reductions in freight rates, transportation taxes, and export prices in order to make United States goods more competitive.

D. Service Characteristics

1) The depth of marketing services currently handled by Export Management Companies tends to be specific, relatively shallow, and oriented more towards a sales function than towards performing the total overseas marketing function for clients. The response to the survey indicated that the functions of most EMC's tend to concentrate on services typical of the export department or sales division of a manufacturer; rather than on services which would be typical of the total marketing function for clients overseas.

The following exhibit shows the responses of respondents to the question on the exporting functions they performed. As can be seen, those functions which are marked as being

performed "frequently" by most of the respondents were those that dealt with specific shipping and sales functions rather than with more comprehensive market research, pla planning and strategy development functions. Those functions receiving high marks as being "frequently" performed for clients were as follows:

- o developing marketing and sales strategy in markets;
- o developing and maintaining contact with customers abroad;
- o establishing pricing policies;
- o arranging for all CIF quotes in response to overseas inquiries;
- o handling all relations with foreign freight forwarders for proper documentation;
- o advising on all export packing and marketing;
- o assuming all responsibility for delivery of goods;
- o arranging for insurance;
- o arranging for servicing of products through overseas distributors.

More comprehensive market planning services such as reports on market conditions, competitive moves, tariff problems or import controls, and new product applications received fewer responses as being "frequently" done by the majority of the respondents. The responses on services that were "rarely" done indicated a leak of both depth in marketing services and integration of export services within EMC's. For example, such things as specific formal market research and assisting suppliers in arranging licensing and joint venture arrangements were rated as rarely being performed. Integration by performing freight forwarding, manufacturing, or servicing products sold abroad themselves, were also rated by the majority of respondents as being rarely done.

The responses to the question on where primary responsibility for the different components of the overseas marketing strategy lay also indicated that EMC's performed a heavier role as the sales arm of the client rather than the marketing arm.

Although all respondents indicated that they contributed to the overseas advertising, promotional, pricing and distribution strategy of a client, they appeared to have more flexibility in the area of promotional and distribution strategy. While 91% of the respondents indicated that they were primarily responsible for the overseas distribution strategy and 75% said they had this prime responsibility in promotional strategy, only 61% of the respondents indicated that they had prime responsibility in developing pricing strategy and only 54% said they had prime responsibility in advertising. In these two areas, the prime responsibility was more frequently shared with the manufacturer, rather than left entirely to the EMC.

E. Client Characteristics

1) Most Export Management Companies handle a small number of suppliers and specialize in a few product lines which tend to be high technology lines and interrelated. The most frequently mentioned number of suppliers being handled by respondents on the average was between 6 and 15 manufacturers. Thirty-seven percent of the respondents indicated handling this number of suppliers on average, compared with 32% who indicated that they handled between 16 and 25 suppliers on average. Only 22% of the respondents indicated handling over 25 suppliers.

Product line concentration on the part of EMC's was shown by the fact that over 77% of the respondents indicated that they handled under 10 product lines or product "families" (i.e., machine tools, electronic components, construction equipment, etc.) and almost 54% handled under five product lines. Only 3% of the respondents handled more than 30 product lines.

In addition, there was a tendency on the part of the EMC's to carry interrelated product lines and high technology products. The survey showed that the majority (68%) of the respondents concentrated their sales representation on such products. The definition of whether a firm dealt in high or low technology

products was based on the characteristics of their major export product line. This product line's position on a continuum of capital intensity was used to categorize the product and thereby the EMC as an either high or low technology product exporter. This capital intensity ratio was defined as the ratio of capital[1] to manufacturer's shipments. Exhibit IV-2 shows the breakdown of the major product categories within the high and low technology classifications.

The factors listed most frequently as entering into the decision on the choice of which product lines to handle were (1) that the line had a high potential in the geographic area where the firm was active, and (2) that the firm had personal expertise in the product line. Low product line competition in the market area did not bear as much importance as a factor in the choice of product lines. Lines were dropped by the EMC most frequently because of either a loss of exclusivity in the market region, or the failure for the product to be competitive. The third most frequent reason given for dropping a particular product line was the failure of product sales to grow.

2) Export Management Companies' clients are small to medium-sized manufacturers for the most part, and although their relationship with a manufacturer can be relatively long-term, it is often only the intial step into exporting. Over 31% of the respondents indicated that all of their suppliers had annual revenues from both domestic and international sales of under $25 million, and 64% indicated that at least 75% of their suppliers fell within this sales range. Suppliers with more than $100 million in annual sales revenues rarely made up more than 10% of the proportion of manufacturers handled by EMC's.

The majority (54%) of the respondents indicated that their average contracts with suppliers were between one and three years in duration, with 13% indicating that their average contract was for one year. However, most EMC's indicated that manufacturers maintained relationships with their firm for a relatively long period of time. Over 40% of the respondents

1 Capital is defined as total assets (i.e., physical as well as financial assets) with investment in government obligations and the securities of other corporation deducted. It is also net of depreciation.

Exhibit IV-2

CAPITAL INTENSITY BY INDUSTRY
USED TO CLASSIFY EXPORT MANAGEMENT
COMPANIES AS HIGH OR LOW TECHNOLOGY EXPORTERS

Ranking, As Measured by the Following Ratio:	Capital* / Sales
High Technology Product Classifications	
Petroleum	3.40
Tobacco	1.13
Electrical Machinery	.98
Chemicals and Allied Products	.90
Non-Electrical Machinery	.88
Primary Medals	.86
Other Trans. Equipment	.86
Motor Vehicle Equipment	.82
Miscellaneous Manufacturing	.75
Low Technology Product Classifications	
Paper and Allied Products	.73
Stone, Clay and Glass	.73
Lumber and Wood Products	.69
Instruments	.69
Printing and Publishing	.66
Leather Products	.61
Rubber and Miscellaneous Plastics	.59
Textile Mill Products	.57
Apparel and Other Fabricated Textiles	.53
Fabricated Metals	.52
Food and Kindred Products	.42
Furniture and Fixtures	.42

* All figures on manufacturers shipments were derived from Statistical Abstract 1972. Capital is defined as total assets (physical as well as financial) less investment in governmental obligations and securities of other corporations. It is stated at book value after deducting reserves for depreciation and other contingencies.

indicated that their average supplier/EMC relationship lasted between 11 and 20 years, and almost 27% indicated them lasting between 7 and 11 years. Only 25% indicated having average relationships of under ten years. This finding was borne out by the fact that the majority of respondents indicated that on average EMC's only lost, courted and added between one and five suppliers in an average year.

The most important sources of leads for EMC's for potential new export suppliers were indicated as being their own investigation, overseas market intelligence and current customers, in that order of importance. The sales leads furnished by the Department of Commerce were generally seem as not being very important. Only 17% of the respondents called them "very important" and almost 37% of them saw them as being "unimportant." Other important sources of leads mentioned by EMC's were trade shows, trade and professional publications, advertising abroad and personal trips abroad.

F. Sales Characteristics

1) Most Export Management Companies have relatively low sales volumes which are only moderately stable in nature. The small size of EMC's is illustrated by the fact that the majority (57%) of the respondents indicated that their current annual export sales volume was under $3 million, and that over 86% of the respondents indicated that their sales volume was under $10 million.

In addition, EMC sales were characterized as being only moderately stable, with 49% of the respondents characterizing their sales as moderately stable, 20% characterizint them as fluctuating, and 9% characterizing them as widely fluctuating. Only 21% of the respondents characterized their sales as stable and stability appeared to play a major part in the EMC's desires to expand their services or market penetration.

2) However, most Export Management Companies experience relatively high average pretax return on sales, but this return appears to vary considerably between firms. The most frequently mentioned average pretax return on sales was under 5%. This return was cited by 34.7% of the respondents. However, 30.7% of the respondents indicated that their average return was between 5% and 10%, and over 14% indicated that their return was either between 10% and 15%, or 15% and 20%. A few respondents indicated experiencing pretax returns of over 25%.

3) Growth of the Export Management Company in terms of sales volume did not appear to impact on the characteristics or depth of marketing services offered by these trade vehicles. When the answers to the questionnaires were analyzed to determine if large EMC's (in terms of sales volume) differed significantly from those which experienced annual sales of under $3 million, very few major differences were discovered. There appeared to be no trend for an EMC to increase the depth and breadth of its marketing services or organization as it grew in size. Organizationally, they differed surprisingly little from small firms, utilizing primarily a home office and distributors rather than sales office expansion abroad. Marketing services also differed surprisingly little from small firms.

However, the following general tendencies were noted of larger EMC's:

- They had a larger equity capital base committed to the business in general ($1 to $5 million).
- They appeared to have longer supplier contracts and relationships.
- They saw the supplier relationship ending most often because the supplier felt he could achieve greater market penetration himself.
- They viewed their competitive position better and were less fearful of competition from small and medium-sized manufacturers.
- They saw the nonavailability of capital and the propensity for United States manufacturers to "go it alone" less of a competitive problem.

C. Organizational Characteristics

1) Organizationally, Export Management Companies operate through small United States sales offices, using a network of exclusive and general distributors primarily, which are supplemented by occasional United States-based salesmen in the field temporarily. The majority (64% of the respondents

indicated that they had under 25 people working for them in their United States home offices. Only 11% of the respondents indicated having between 25 and 75 home office employees and none had a home office in excess of 75 people.

Use of a foreign sales office was indicated by only 40% of the respondents, while only 17% indicated utilizing foreign sales subsidiaries, and only 9.5% had their own salesmen in the field permanently. However, 53% of the respondents indicated sending their own salesmen into the field temporarily. The number of people used in any of these alternate organizational sales structures rarely exceeded ten.

Without a doubt, general and exclusive distributors were the most widely used overseas sales mechanism, in that order of importance. Over 82% of the respondents utilized exclusive distributors. The number of exclusive distributors mentioned as being utilized most frequently was between 11 and 25, but many respondents indicated having up to 250 such distributors. Over 71% of the respondents utilized general distributors, again with the number of such arrangements mentioned most frequently being between 11 and 25. However, many respondents indicated having over 400 such relationships. Resident subagents were utilized less frequently (by only 36% of the respondents) and in less number. The most frequently mentioned number of these arrangements was under ten.

2) Export Management Companies see future growth opportunities as following the same organizational and sales pattern that they currently utilize. Although almost a third of the respondents (30%) indicated that they were "very interested" in opening overseas sales offices, and another third (33%) indicated that they were "somewhat interested," the majority of respondents (68%) picked geographic diversification through foreign agents over the establishment of their own overseas sales offices as the marketing tactic they would perfer to pursue.

The factors seen as representing the greatest hinderences to opening overseas sales offices were (1) high overhead, and (2) insufficient capital, followed in importance by (3) the narrowness of product lines, (4) instability of sales, and (5) lack of manpower, listed in that order.

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The majority (44%) of the respondents indicated that they would need between $500,000 and $1 million in export volume to a particular market before they would want to open a sales office. A significant number (16%) felt sales volume would have to be even higher (between $1 million and $2 million) before such an overseas office would be warranted.

This trend towards expansion of sales through geographic diversification was also borne out by the response to the question concerning existing distribution lines rather than overseas offices where the EMC's expected the majority of their future sales growth to come. Penetrating existing market areas with the same product, but a better distribution system was ranked first, followed by expansion into new geographic market areas with the same product. Diversification through (1) an increased product mix, (2) expanded product mix and geographic areas, or (3) forward or backward integration by moving into complementary ventures such as freight forwarding, insurance, etc. were not seen as having a high priority as means of expansion by respondents.

3) Most Export Management Companies viewed integration into complementary businesses as a highly unlikely future action and the most likely expansionary move as being aimed at either the establishment of a network of overseas offices or the move into licensing and joint venture arrangements. The majority (over 70%) of the respondents saw the construction of overseas warehousing, manufacture of products, or purchase of Freight Forwarders as highly unlikely means of expansions. They also thought it highly unlikely that they would move into pulling together ventures requiring international subcontracting and project management. The prime reasons given for avoiding these expansionary moves were (1) the desire to specialize in marketing (cited by 69% of the respondents) or that (2) the return on investment would be unfavorable (cited by 60% of the respondents).

This likelihood for EMC's to follow the trend of American business towards foreign direct investment (i.e., licensing or joint ventures) rather than more cost efficient means of export consolidation was borne out by the questions on the future direction of trade (i.e., export, import, licensing). Most firms envisioned undertaking more licensing activity

H. Financial Characteristics

1) Most Export Management Companies are thinly capitalized, having a low equity capital base which is frequently supplemented by personal advances or guarantees on the part of owners. The low capitalization of EMC's can be seen by the fact that over 73% of the respondents indicated that they had an equity capital base of under $500,000 committed to the business and almost 28% had under $100,000 committed. In addition, this capital base was highly unstable. Fifty-six percent of the respondents indicated that they either "sometimes" or "regularly" supported the capital in the business with personal advances or guarantees.

Adding to the thinly capitalized picture of EMC's was the fact that the majority of respondents indicated that they had a relatively low amount of external financing available to the business at its periods of peak need. The majority of the respondents (53.5%) indicated that they had between only two and five times equity capital available from external financing sources, and over a third (37%) of the respondents indicated that they had less than two times equity capital available. However, few firms indicated that they used factoring of accounts receivables as a means for generating additional capital. Only 6% of the respondents indicated frequently using this financing method and over 88% indicated that they rarely used it.

2) Most Export Management Companies do not utilize the current government supported financial aid mechanisms available to them. Although EMC's indicated using FCIA more frequently than Ex-Im Bank financing, the majority of the respondents indicated rarely using them. Fifty-six percent of the respondents said they rarely used FCIA and 78% said they rarely used Ex-Im Bank mechanisms. Only 45% of the respondents indicated that they were qualified as a DISC.

I. Ownership Characteristics

1) Export Management Companies tend to be entrepreneurial in nature and are owned by single or majority interest owners. The survey responses showed that the ownership pattern of most EMC's tend to be single or majority interest ownership.

with relatively few firms having a large number of partners, or public ownership. Fifty-five percent of the respondents indicated that the firms were owned by either a single owner or a majority interest owner, and over 24% indicated they were under single ownership. Only 5% had more than five owners in the firm.

In addition, although a great many (47%) indicated that they had the desire to expand into a major world trade force internationally, the majority (53%) indicated that their primary goal was to (a) create a good standard of living for themselves and fellow owners year-to-year or (b) to invest profits to take advantage of growth opportunities while maintaining a balance of comfortable annual payoff, or (c) create an equity position of maximum proportions to be realized within a 10 to 15 year timeframe.

Also, this desire to create a firm that would be a major force in international trade did not appear to be translated itself into a willingness to take those business strategy actions that would allow the firm to grow in this direction. For example, although 47% of the respondents said they had this desire as a goal for their enterprise and although 64% said they were somewhat or very interested in opening overseas sales offices, only 32% indicated that they would likely follow this sales strategy. In addition, diversification through both product mix and geographic area, or through moving into complementary business ventures such as freight forwarding, warehousing, insurance, etc., was seen as a low priority for contributing to future sales growth.

The reason given as being most important in taking a negative attitude towards such diversification into complementary business ventures were as follows: (1) the desire to specialize in marketing (69% of the respondents), (2) unfavorable return on investment in such a move (61% of the respondents), and (3) the lack of desire to make large capital investments (51% of the respondents).

The uncertainty attached to changing operations and the lack of capital available to accomplish such diversification were also listed as important, but to a lesser degree than the three factors just mentioned. Other reasons mentioned by some firms were (1) contentment with their current operations (i.e., these operations had been profitable and stable for 20 years) and (2) the fact that such a move would be hard to

control and was impossible without long-term commitment on the part of the manufacturer (cited by 75% of the respondents), and (3) the price of their goods (cited by 62% of the respondents), (4) company-owned overseas sales networks (cited by 37% of the respondents), and (5) the lower costs of doing business experienced by foreign firms (cited by 36% of the respondents).

2) On the home front, most EMC's saw their own sales expansion efforts hampered primarily by cost factors, foreign government trade restrictions, and competition from foreign export. Although the factors listed as inhibiting the development of the growth of individual EMC's varied considerably, the factors checked most frequently as hindering to a "very great extent" were transportation costs (cited by 38% of the respondents), foreign government restrictions and regulations (cited by 31%), availability of capital (cited by 23%), and competition from foreign export traders (cited by 23%). The availability of low cost rediscounting facility and the propensity of United States manufacturers to "go it alone" were also mentioned frequently as either hindering development to a very great or a considerable extent. (See questionnaire responses in Appendix C.)

SECTION 3

THE VIABILITY OF THE EXPORT MANAGEMENT COMPANY AS A POTENTIAL FRAMEWORK FOR AN AMERICAN TRADING COMPANY

As can be seen from the preceeding section, United States Export Management Companies (EMC's) possess the necessary international trade know-how and marketing mechanisms to form the basis for a United States trading company. However, at present, these trade vehicles do not have the facilities to overcome the competitive and market constraints outlined in Part II, Section 2, which must be overcome if they are to into an American trading company.

These constraints, briefly summarized, are as follows:

- size and stability of sales;
- capitalization needed to support overseas offices and integrated services;
- a worldwide marketing network in order to cultivate (1) new suppliers and (2) new end markets easier and therefore stabilizing both sales volume, trade patterns, and client relationships;
- depth and breadth of marketing competence and an ability to achieve lower per unit cost in order to deter the clients from "going it alone" once they pass the initial entry stage of exporting.

As has been pointed out in the previous descriptive section (Part IV, Section 2) on Export Management Companies, these trade vehicles are severely handicapped in their ability to grow into a viable American trading company because of the following:

- Leadership-wise, EMC's are small and entrepreneurial in nature with no long-term goals to grow past the "middleman" service role to manufacturers. The general business growth philosophy on the part of EMC owners appears to be "business as usual, but more of it," rather than envisioning growth

through diversification by either product line, geographic areas, or integration into complementary companies that could lead to lower per unit costs, and follow the trading company concept.'

- Organizationally, EMC's are largely United States-based, relying on and preferring distributors arrangements overseas rather than their own sales offices. This diminishes the degree of their control in the overseas market and is contrary to the requirements of a successful trading company.

- Financially, EMC's are largely undercapitalized, do not fully utilize current government financial aid mechanisms available to them, and suffer from both an instability and small size of both sales volume and client relationships.

- Competitively, EMC's function primarily as the overseas "sales force" for a client rather than as his international marketing arm. There appears to be little desire on the part of most EMC's to change this role and provide a wide-range of market planning and strategy functions.

In summary, at the current moment, United States Export Management Companies appear to take a myopic and statis view of their role in world trade. They function primarily as product-oriented international traders rather than market-area oriented international businessmen. For the most part, their marketing role has been that of "pushing" a product they are familiar with in markets where they have know-how and contracts, rather than one of reacting to the nonspecific "pull" of international worldwide demand.

This characteristic is substantiated by the fact that the direction of their trade in generally unidimensional (export from the United States) rather than either two-dimensional (export-import to the United States) or multi-dimensional (exporting and importing from a variety of countries), as is characteristic of the large foreign trade companies.

In addition, they appear to have little desire to perform any role greater than a sales role. The depth and breadth of these marketing services are generally shallow and procedurally oriented which could be easily replaced by the manufacturer himself. This view is substantiated by both the non-desire of EMC's to increase the depth of their services by integration or offering more complex and comprehensive marketing services. It is also substantiated by the fact that larger EMC's show little difference in organi-zational or market depth characteristics.

In conclusion, there can be little chance that the EMC's as they are now constituted will move in the direction of a United States trading company unless there is considerable stimulous on the part of the United States Government to make a move in that direction financially or operationally attractive for both EMC's and manufacturers.

Despite these criticisms of the Export Management Company and its ability to serve as a basis of an Export Trading Company, we firmly believe it is an extremely valuable member of the trading community. There is no doubt in our minds that it is currently providing a much needed service to American manufacturers. In the United States today, there is practically no other organized force to bring small and medium-sized manufacturers into international trade.

Furthermore, it is important to stress that the financial resources and means necessary to make the EMC a full fledged trading company do not exist today even if they were predisposed to change the nature of their role with manufacturers.

Finally, our comments on these organizations have necessarily been generalized. From our exposure to a large number of these companies, it is clear that several of the larger EMC's could, perhaps quite easily, transform their role to that of the Export Trading Company we envision and which we shall describe in the next section of the report.

PART V

CONCLUSIONS AND RECOMMENDATIONS

In preceding sections of this report we have discussed the problems and approaches to international trade, the ability of a trading company to solve these problems, the constraints which impede a trading company from solving these problems within the U.S. legal and commercial environment and how these constraints might be overcome. We also explored the nature and capabilities of Export Management Companies, the most common independent export unit in the U.S. This part of the report attempts to distill much of that information in the form of concluding remarks and recommendations.

We first address the issue of the viability of the Export Trading Company concept in the last quarter of the twentieth century. We then present our concept of an American ETC and discuss its nature, characteristics and structure. We further discuss how such a company might be initially funded and finally give our assessment on the feasibility of implementing the concept successfully.

The report ends with our recommendations.

SECTION 1

A. A Trading Company Concept is a viable means of conducting international business in the last quarter of the twentieth century.

A trading company is a particularly viable means of conducting international business today because of its unique potential ability to satisfy the basic needs of many "interested" parties in the international economic community. For the domestic manufacturer, a trade company brings an opportunity for growth he might not otherwise be able to realize at significantly lower risk. For the United States as a whole, a trading company offers the benefits of export sales--a stronger U.S. dollar and lower rates of inflation through a positive contribution to the balance of payments and employment possibilities through capacity expansion that would not

otherwise be possible. The trading company offers foreign buyers U.S. goods which it seeks to satisfy internal needs. For foreign government, a trading company offers the possibility of utilizing its capability to expand exports from itself, a means of limiting foreign economic intrusion vis-a-vis direct investment to areas of specific needs. A trading company also offers its investors a lowered business risk through numerous investments of fixed assets abroad in contrast to firms which expand through addition of manufacturing facilities abroad. The addition of manufacturers facilities abroad, which in many cases must be more than half owned by local interests, complicates both management of the local market development and international business management if the foreign unit is pressured by the host government to export. For buyers and sellers alike, the trading company concept gives an image of total dedication to international trade.

1. Many of the factors which contribute to the viability of the trading company concept detract from the viability of a trading concept which deals in exports only. Such a company would be perceived as exploitive in character by many countries around the world. Such a perception could result in the creation of additional tariff and non-tariff barriers to American goods and makes good relations with host countries difficult to achieve. A trading company which deals in exports only would bring with it the image of 19th century colonialism coming from a country such as the United States. A trading company concentrating exclusively on exports needlessly eliminates the benefits of third-country trade--trade from a country outside of the U.S. to another foreign country, e.g., Mexico to Ireland. Such a trade multiplies the business opportunities possible from foreign offices in a way no other approach to international business can match. A significant volume of third country trade also would bring with it the possibility of barter transactions--taking payment of goods in the form of product. Such a service would be highly valuable to both the trading company and host countries where hard currency reserves are small. It would be valuable to the host country because it does not have to make foreign exchange available for the transaction

and the transaction appears not to affect its balance of trade position. This type of trade benefits the trading company because it makes two sales instead of none--increasing volume and minimizing its unit costs commensurably. In our judgment, two-way, if not three-way trade, must be a policy commitment to make the trading company concept work today and for the foreseeable future.

B. The Trading Company Concept is particularly suited to the needs of small- and medium-sized manufacturers which are presently marginal or non-exporters.

It is our judgment that a trading company approach can solve the problems associated with bringing a large number of small- and medium-sized marginal or non-exporting manufacturers into international trade better than any other approach. The trading company approach minimizes the level of export interest, information and know-how required by manufacturers and almost entirely removes the business risks associated with international trade from them as well.

1. The Trading Company approach minimizes the interest problem.

A trading company approach minimizes the export interest problem in beginning exporting in several ways. It offers manufacturers an immediate strategic opportunity to expand their business. The trading company is, in effect, an additional domestic buyer who neither saturates any domestic demand nor requires a sales effort. The manufacturer thus has the opportunity to raise his sales level and decrease his unit costs of doing business, which could dramatically affect the competitiveness of products domestically. In contrast, going the direct export route offers no such opportunity, but most likely will result in an immediate increase in unit costs until the international sales reach a break-even point. Furthermore, business risks must solely be absorbed by the manufacturer going direct, whereas a trading company may be capable of entirely absorbing the financial and commercial risks attendant with foreign sales.

In addition, the trading company approach requires a minimum diversion or reallocation of resources from its suppliers. Management time and staff support require of the manufacturer is no more than for any other domestic buyer. To the extent that the trading company finances its own purchases, it requires little additional financial adjustment by manufacturers. This last point will be elaborated on shortly. In contrast, "going it alone" requires the smaller business to substantially reallocate its scarce managerial and financial resource. Other kinds of "middleman" trading vehicles also reduce the needed export interest factor, but only to some degree between that needed to go direct, and that required by a trading company.

2. <u>The information and know-how problem is also minimized by a trading company approach.</u>

All the information needed to generate business abroad would be developed by the trading company. It would establish the end-users, buying practices, size and growth potential of products, market structure and competition, tariff and non-tariff barriers and product trends. The role of the manufacturer in these endeavors would be quite small, as opposed to going direct. The trading company, almost by definition, contains all the international know-how to get the job done without any manufacturer involvement.

3. <u>A trading company approach satisfies some basic economic problems confronting the marginal or non-exporter.</u>

To sell a product abroad, it often takes some investment in foreign warehousing, offices abroad, or marketing trips abroad to potential buyers. A product or company with a small level of sales cannot support such an investment, but often a group of products or companies can justify such an investment. By definition, a new exporter has no sales to support foreign investment necessary to induce exports. A trading company concept, however, copes with this problem through a sharing of marketing and infrastructure expenses. It is precisely the start-up problem that trading companies are best structured to solve. It is only when the sales activity could support individual company efforts that the direct export approach is as economically viable as that of the trading company. Obviously, however, the cost of the initial marketing effort must be paid by the products already generating sales. It is, therefore, important to keep the trading relationship with a supplier going for as long as possible.

C. A Japanese Trading Company approach is not a panacea--it is a better device for marketing some products than others.

We have devoted a great deal of space in this report to the Japanese Trading Company--among other reasons, because it is an unavoidable standard for comparison. But not even the supporters of the Sogo Shosha believe that it is the appropriate device to use to market every product. Recall the fact the Japanese trading company is the marketing department for the majority of Japanese firms. Automobiles and consumer electronic products are two areas, however, where there is a great deal of marketing activity outside of the trading companies.

1. A Japanese-style trading company works best dealing in standard goods.

A Japanese Trading Company is an extremely efficient marketing device. Consider a group of American firms such as Borg-Warner, Rockwell International, General Electric, Cargill and DuPont. Next, consider the number of international offices and personnel these firms have around the world. In a Japanese Trading Company the marketing activities of every kind of goods produced by those American companies would be handled from the same office. The volume requirements of such a system demand that the major standard for making a sale is the delivered cost of the goods. The more the purchasing decision strays from the financial aspects of the sale, the less the product is optimally served by a Japanese trading company concept. Basic food commodities, textiles, raw materials, steel, heavy construction and certain industrial goods are typical of the goods the Sogo Shosha sells best. It is capable of generating huge economies of scale in dealing with these products. In general, the higher the technology level, the more the product must be marketed to masses of people, the less applicable the Japanese approach. The more time it takes to make a sale, the more costs the individual sale must absorb, and the more valuable it becomes to have direct contact between the manufacturer and the end-user. The efficiencies attainable by the concept just can't be attained. We do not mean to imply, however, that high technology goods or consumer goods cannot be marketed by trading companies--just that where there are other reasons than cost that determine the sale, different kinds of people and different marketing approaches than those of the Japanese Trading Companies will be required.

SECTION 2

A UNITED STATES EXPORT TRADING CONCEPT

It is our judgment that a trading company concept which is envisioned as a group of manufacturers coming together under its umbrella is not likely to occur without great outside pressure or incentive. All of our work and study of the Japanese and British trading companies, the Webb-Pomerene Associations and the motivation of the American businessman to maintain his independence and "do his own thing" indicates to us that the initiative, drive and capital to form a trading company is not going to come from the manufacturing sector.

THE WEBB-POMERENE ASSOCIATIONS

The history of the use of the Webb-Pomerene Associations is particularly important to our coming to the conclusion above. The rationale for the creation of these associations was to enable smaller manufacturers to come together and share expenses in developing an effective international distribution system--the concept has failed. Although over 260 associations have been organized under the Act since 1918, only 34 are currently operating and only a few of the 260 have maintained their Webb-Pomerene status for any appreciable length of time.

In 1967, the Federal Trade Commission published a detailed, 50-year history of Webb-Pomerene associations which revealed a number of disconcerting facts. According to FTC figures, Webb-Pomerene-assisted exports have averaged around six per cent of total annual United States merchandise exports. But this figure failed to discriminate between exports which association members made on their own and exports which were made with association assistance. According to Willard F. Mueller, former chief economist of the FTC, in testimony before Congress, the figures on Webb-Pomerene-assisted exports have been overstated by at least 50 per cent.

The report further indicated that the typical association has been short lived. Of the 176 associations covered in this report, more than half lasted less than five years, nearly 80 per cent lasted less than 15 years.

An analysis of this report by David Larson of Louisiana State University also disclosed some alarming facts. Taking the group of associations operating in the last five years covered by the report, he found that only six out of 47, or 13 per cent, operated as marketing associations. The remainder of the group organized either to establish common export prices, allocate export business among association members or act as an export broker if they did anything at all except meet. Furthermore, his analysis showed that less than 38 per cent of all the firms belonging to these Webb associations had an asset base of under $5 million, that 70 per cent of the associations had no members that could be considered small firms and not one association was comprised entirely of small firms. Not one of the associations in which the smaller firms participated operated as a marketing organization.

One could argue that the failure of the Webb associations has been a result of a lack of financial incentives--such as a lower tax rate. We do not believe this line of thinking. While we do not believe that most smaller firms are aware of the Webb-Pomerene Act, it is our opinion that the concept's lack of use by small business is simply their lack of interest in such a mechanism to perform the export function.

A Webb association calls for investment. Getting together the initial capital to start such an association would be highly problematical for a small concern. In addition, using any form of indirect distribution is not perceived as the ultimate international marketing structure in the United States, so the investment will be temporary at best. Further, an association requires a somewhat unified approach to marketing. In our experience, a unified approach to marketing would be hard for a group of manufacturers to agree on, no matter how related their product lines are.

THE UMBRELLA CONCEPT

An umbrella concept implies that the manufacturers are the catalysts. We are not convinced that this is possible and, hence, our concept does not envision it. In addition, the concept of the umbrella, as used in the Department of Commerce statement of work, is inaccurate in its references to Japanese and British trading companies. From our explanation of a typical British trading company, there is no way it could be considered as a creation of its manufacturing sector. In Japan,

the trading companies are the only means of international distribution for smaller manufacturers. Yet, the trading company is not part of a corporate framework, but industrial groups which operate closely as a result of a common background and heritage.

A. We believe that the incentive and capital for an American Export Trading Company must come from outside the manufacturing sector and should, thus, have the following six characteristics:

1) is integrated in nature and, hence, is more than simply a trader;

2) deals in imports and third-country trade as well as exports;

3) is substantially diversified on a product and geographic basis and is a medium-size business itself;

4) is a strong financial, as well as marketing, vehicle;

5) acts as an independent international department in its dealings with suppliers; and

6) structured to consist of a head office where business unit management, administrative and other staff activities are performed; a small network of strategically located offices, globally dispersed; and a network of branches, agencies, distributors and correspondents as appropriate to cover individual markets.

1) It is integrated in nature and, hence, more than simply a trader.

Exhibit V-1 is a restatement of the requirements we believe an American trading company must meet to be viable. To fulfill the first three of these requirements, a greater degree of integration than is generally found in Webb-Pomerene associations and middleman export trading units must be present. An American Trading company must be capable of making, and indeed make, equity investments in warehousing, fabrication or packaging facilities and other

EXHIBIT V–1

TRADING COMPANY REQUIREMENTS FOR SUCCESS

A. A Trading Company must have strong ties to manufacturers.

B. Trading Companies must be product specialist.

C. Trading Companies must have strong foreign sales networks under their control.

D. Trading Companies must have depth and continuity of management.

E. Trading Companies must have the ability to create credit.

F. Trading Companies must have sufficient diversity of products and markets.

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infrastructures that can support three-way trade. We believe that this integration is absolutely necessary to delay the supplying manufacturers from terminating their relationships with the trading company once export volume starts to materialize. Integration serves to tie the manufacturer to the trading company longer because it raises the level of investment that must be made by the supplier to do the marketing job as well as the trading company in a particular market and, hence, raises the level of supporting sales where a termination can be economically justified.

Integration also is necessary to strengthen the company's position as a product specialist and give it strong control over a sales network. Integration forward in marketing activities as close to the end user as necessary or practical provides knowlege about specific product/markets which can be reflected in the features and qualities of the goods merchandised. Forward integration also yields stronger control over a foreign sales network, maximizing the company's penetration ability against other competition. Integration gives the trading company concept additional profit opportunities. Also included in the concept would be an ability to earn a commission on freight brokerage activities.

2) <u>The trading company is capable of and permitted to deal in imports and third-country trade as well as exports.</u>

We support the idea that the trading company concept should primarily focus on expanding exports. Earlier in this part of the report, however, we discussed the viability of a totally export-oriented firm and came to the conclusion that such a company was not viable today. We want to reiterate our judgment that, if a trading company is totally relegated to servicing exports, it will fail. We do not believe that such a company would be acceptable to the international economic community today. In addition, such a firm could be wiped out by currency fluctuations if it does not have the flexibility to adapt as necessary. Furthermore, such an orientation eliminates a profit opportunity which will be vital to drawing investments into such companies and eliminates the possibility of lowering total unit costs by spreading the overhead of a network of offices among a far larger number of product/market opportunities.

3) The trading company is substantially diversified on a product and geographic basis and is a medium-size business itself.

The trading company cannot afford to be overly dependent on one supplier, one industry or one country's trade for its survival. Such a policy would not be acceptable to manufacturers who will depend on the trading company if they permit their account volumes to grow significantly and it would not be acceptable to enough investors to draw the kinds of capital necessary to fund the trading effort.

While it is difficult to specify size, we believe that the trading company should contain a minimum of five core business units with at least five supplying manufacturers in each and no manufacturer accounting for more than 10 per cent of sales. Obviously, this is a qualitative judgment. But while the numbers may be judgmental, the rationale which supports them is not. Our interviews and analysis indicate that an organization much smaller than this cannot accomplish the tasks it must do to survive and prosper. Such a composition of businesses and manufacturers:

- will minimize the impact of any firm's termination of relationship with the trading company
- provides the basis of support to get new exporters involved with the trading company
- will spread the business risk among a reasonable, multiple number of units
- will require management depth and capability
- implies a scale of business which is beyond an "emergence phase"

The last point refers to a condition we have observed repeatedly in the United States. A new business is faced constanly with threats to its survival. It takes size as much as time to surmount the problems of this "emergence" stage of business. A trading company is going to be faced with problems and risks more complex than a domestic business. As such, we feel it is of questionable value to develop programs and initiatives toward getting more manufacturers involved in exporting through trading companies without a reasonable chance of the trading company's survival.

Core businesses would be trading operations centering on a group of related products such as machine tools, electronic components or construction equipment. Each core unit should be capable of establishing global marketing strategies independently of the other groups, seeking new exporters to broaden the unit's capabilities and developing an appropriate distribution network. The concept of the business core is to provide a vehicle which completely satisfies the range of requirements of specific end users, thus positioning the company in such a way that its individual suppliers would lose synergestic benefits by terminating the trading company relationship.

4) The trading company is a strong financial vehicle as well as a marketing vehicle.

As mentioned previously, it is our judgment that a viable trading company cannot exist unless it has an expanded capacity to extend credit terms to both its suppliers and its buyers. As a result, the financial management skills required by the trading company will be significantly greater than found in the United States today. The judgment, risks and tools involved would be considerable. The trading company would be expected to know, for example, how the floating rate system will affect its portfolio over a three-month period. It should be able to assess the necessity for hedges, the availability of World Bank or Export-Import Bank assistance on transactions. It must easily handle decisions involving credit on open account, letter of credit, barter, various denominations of currencies, AID types of programs of one country or another, financing for the firm's account or financing without recourse to the firm.

We would like to see the trading company be responsible for creating credit up to ten times its net worth. Such a level is two to three times that currently possible by independent export units in the United States, but only half that of a Japanese trading company. We expect such credit to be supported by a guarantee insurance policy as described previously.

5) Our concept of an ETC acts as an independent international department in its dealings with suppliers.

The ability to create credit is dependent on the trading company's taking title to the goods. The typical relationship between a supplier and the trading company would, hence, be to buy the product from the supplier for its own account and sell it to another party elsewhere in the world. The trading company thus assumes the market risk from the time it accepts delivery of the goods from its suppliers to the time the foreign buyer makes payment. The ability to act as an agent, however, would also be an acceptable form of operation. Typical functions of the trading company would include:

- developing comprehensive marketing and sales strategies;
- closing sales contracts;
- providing or arranging for buyer financing, if desired;
- providing or arranging for pre-export financing, if necessary;
- handling all documentation requirements, insurance and shipping considerations;
- advising suppliers on appropriate export packing and marking;
- assemble or fabricate goods upon arrival overseas, if appropriate;
- assuming the responsibility for delivery of goods;
- arranging or performing warranty and other servicing of the goods;
- assist manufacturers in arranging licensing agreements or joint ventures as desirable.

The relationship between the supplier and the trading company would be based on a contract specifying the products and markets the trading company will be responsible for developing. The contract would give the trading company

exclusive rights to developing those products and markets for a period of two to three years, after which time the contract can be renegotiated. The initial contracted period allows the trading company to invest time and effort into the marketing activity with good hope of a return on this investment. After this period, the financial power and marketing strength of the trading company should be producing results which will satisfy the supplier and encourage him to extend the relationship.

6) The ETC structure would consist of a head office where business unit management, administrative and other staff activities are performed; a small network of strategically located offices, globally dispersed; and a network of branches, agencies, distributors and correspondents as appropriate to cover individual country markets.

It is difficult, if not impossible, to operate a global trading business on a meaningful scale without a global presence. While it is not practical or, perhaps, even useful for a company to have a great number of offices abroad, it is our judgment that without a presence it is difficult to create a business which a supplier cannot surpass in marketing effort after his sales volume reaches about a million dollars--in the absence of a financial tie to the trading company. Obviously, more or less of a sales network will be appropriate for different products and different industries. From our experience and judgment, a minimum of five to ten offices staffed by trading company personnel will be required. While the number is, again, arguable, the important element in the number is the sense of scale we are trying to indicate as appropriate for a viable trading activity.

Managers of the various business units would be expected to travel abroad frequently to maintain total familiarity with offices and foreign buyers as well as frequently visit domestic suppliers.

E. In our judgment, a trading company which meets these characteristics can overcome the problems involved in initiating exports from small- and medium-sized manufacturers.

Furthermore, we believe that such a company could be competitive against a broad range of foreign competition and delay the temptation to "go it alone" on the part of its suppliers long enough to justify the investments in infrastructure necessary to expand trade and support an ongoing marketing effort to find new suppliers. It is our conviction than an organization which does not meet these basic characteristics cannot hope to fulfill the requirements for success in trading. Either the organization will be too small to really stand a chance of substantially expanding trade or it will be incapable of generating growth because of its inherent inability to tie its manufacturers to it for sufficiently long periods to justify necessary investments.

F. Participation in the trading company should be limited by international sales levels.

As the trading company is intended to bring firms into the international business arena and not be a vehicle for use by significant exporters, we believe that some limitation on supplier participation is required. We believe that firms with corporate international sales of $10 million or more represent a reasonable cut-off level. Such a level allows the trading company to keep income-producing suppliers necessary to help underwrite the activities involved in bringing new exporters on board, yet does not permit guaranteed funds to be utilized by enormous organizations who can better afford the risks involved in international trade. A company with $10 million in international sales is not a marginal exporter.

A company of this size might not be asked to leave the trading company if it started at a very small level of sales with it, but perhaps simply made ineligible for trading company guarantees.

G. It may be necessary for an American export trading company as we designed it to be a quasi-public institution.

We were greatly concerned by the attitude taken by the Treasury Department and Export-Import Bank on the guarantee issues associated with the trading company's ability to create credit. These institutions felt that providing this service for one group of institutions alone would be contrary to their operating policies. It is the government's feeling that the exporter must accept some

risk and, with the exception of trading companies, the risks of nonacceptance of goods and warranty issues are small indeed. Therefore, to overcome this problem, it may be necessary for and American ETC to become quasi-public. As a quasi-public institution, the Treasury and the Export-Import Bank would find it much easier to grant special status financial tools.

Quasi-public status would also remove any shadow of anti-trust proceedings being brought against the trading company since it is impossible for the government to sue itself on these grounds.

Further, quasi-public status would be a means of initially financing export trading companies. Our concept is one independent of manufacturers, who we have found have little interest in investing in a trading company. Outside of a few existing independent export units, there are few places to find accumulated capital commited to this concept. Quasi-public status could be a means of getting around this concern by providing government guarantees on initial capital to qualified firms or individuals.

H. Despite our conviction that the ETC concept as we have defined it is a viable means of expanding exports from small- and medium-sized manufacturers who are currently marginal or non-exporters, we are unfortunately skeptical as to the feasibility of implementing the concept in the United States.

There is no doubt in our mind that the ETC we have designed is capable of overcoming the legal, marketing and financial constraints which have impeded the growth of trading companies in the United States. But there are still problems. While we think the concept is or could be made viable, we are not convinced it is feasible. This is a hard truth to come to grips with. A hundred interviews after we began this study, we see three major issues which lead us to this negative posture:

1) The need for manufacturer support: We uncovered virtually no manufacturing support for a trading company concept.

2) The need for management expertise: We are stymied as to where the management expertise necessary to run these companies might come from.

3) The need for government support: A consistent, coherent and supportive United States international economic policy is absolutely necessary to make the concept work and this appears to be nonexistent.

1) The need for manufacturer support: We uncovered virtually no manufacturing support for a trading company concept.

It was not within the scope of this study to fully assess manufacturers' interest in a trading company concept. However, in the course of this study we have talked to dozens of small- and medium-sized manufacturers around the United States. We did not detect even a faint glimmer of interest in the concept and, obviously, it will not work without substantial support from this sector.

The characteristics we have stressed as necessary have been purposely designed to create and sustain that interest; however, we are not convinced that they will sway enough manufacturers. The design needs to be tested.

We do not believe that tax incentives will be any more convincing to non-exporters. We believe the problem is psychological to a large extent. Many small businessmen see their businesses as local or regional. Many small businesses serve territories of just two or three states. Convincing these people that the world is their oyster when they have no business in 45 untouched states is a difficult task. Getting these individuals excited about a trading company is even further down the road.

2) The need for management expertise: We are stymied as to where the management expertise necessary to run these companies might come from.

The Department of Commerce believes that there are at least 20,000 firms which have potentially exportable products not currently exporting. Perhaps 10,000 of these firms have products that could be marketed by an American Trading Company. At 25 suppliers per firm, 400 trading companies would be required. At 50 suppliers per firm, 200 trading companies would be required. Our study indicates that less than 20 per cent of all EMC's handle more than 25 suppliers and practically none of them come close to the structural characteristics we outlined as necessary. Where is the trading company management going to come from?

We do not believe that the typical EMC manager is qualified to lead the trading company we have described. He is too entrepreneurial in character, too interested in selling. He is not the business sort we see necessary to run a series of global business units, a sophisticated marketing unit and a sophisticated financial house as well. Almost beyond all other factors, this one looms large in our negative feeling on the implementation capability of the concept.

3) The need for government support: A consistent, coherent and supportive United States international economic policy is absolutely necessary to make the concept work and it appears to be nonexistent.

The reality of the business world today is vigorous competition between European, Japanese and North American companies that compete on a global basis. To successfully compete in this environment, an American Trading Company designed to support small- and medium-sized manufacturers must have its interests supported by the government, as well as direct assistance when appropriate. The need for financial support is one example. These needs arise because the international marketplace is one where political factors are often as important as economic ones and where government support can spell the difference between participation and nonparticipation. No unilateral activites will make the international marketplace subject to the forces of a free economy. In contrast to other countries--where exports are vital to national well-being--the United States has few programs or policies which promote exports, particularly from smaller manufacturers. The last several years have witnessed an alarming number of setbacks and inconsistencies in the programs that do exist:

- Export-Import Bank policies which favor larger and more profitable loans and, hence, cut back on opportunities for the smaller firm.
- The creation and dismantling of the DISC incentive.
- The widely circulated Office of Management and Budget report on United States export promotion policies and programs which suggested the many direct initiatives taken by the Government are not vital to the nation's well being.

- The creation of Webb-Pomerene associations to exempt United States firms from anti-trust activities in foreign trade and their subsequent curtailment as a result of Justice Department prosecution and lack of clarifying legislation.
- Substantial increases in the cost of participating in Department of Commerce trade shows abroad.
- Inconsistencies in the efforts of government organizations, such as the Small Business Administration, to develop export interest on the part of non-exporters.

The issue here is not so much the value of any export promotion program, but rather the inconsistencies in the actions of the Government. It seems that promising programs are developed and then heavy restrictions in applications limit their usefulness. It is hard for us to believe that the necessary support for an American Trading Company will be sustained for long. For, in addition to the financial support that the concept will entail, it requires that the government agencies make a coordinated effort to create the interest factor on the part of American manufacturers. As this kind of program will require funding approval from OMB and support from Congress to be really successful, we are not optimistic on the outcome.

RECOMMENDATIONS

It is our judgement that there are few significant constraints which would prevent the formation and operation of the ETC concept we have proposed. However, our reservations on the feasibility of implementing still need to be refuted or substantiated.

LEGAL ISSUES

We believe that there are no fundamental legal issues which constrain the Trading Company Concept. The Webb-Pomerence Act certainly permits groups of firms to join together under the umbrella of a trading company if that were appropriate. The cases in which legal problems arose with Webb Associations were ones in which the members controlled a significant share of the domestic market in the goods in which they dealt. We do not believe that small/medium sized companies would have such difficulties. Similarly, there are no legal restrictions on creating vertically integrated companies similar to the Japanese Industrial Groups, but such groups would run into anti-trust difficulties if their domestic market shares were high. Again, this situation is unlikely to occur in a trading company comprised of small and medium sized manufacturers.

COMPETITIVE AND MARKET ISSUES

We have uncovered little in the way of competitive or market constraints impedeing the viability of the trading company concept. Indeed, such companies do exist around the world and are thriving. There is no doubt that competitive ability is influenced by financial strength; however, and with the exception of the Japanese trading companies other trading companies are vulnerable to market penetration by well capitalized manufacturers. Trading companies also have historically competed best in standard products markets where cost is traditionally the most important consideration in making a sale. However, we believe that the success of United States Export Management Companies and other specialized traders shows that the concept can be extended to marketing high technology goods as well, albeit on a smaller scale. The greatest market or competitive restraint of growth is the inability of United States independent export units dealing with manufacturers to create strong and lasting ties with manufacturers.

FINANCIAL ISSUES

We have, however, uncovered significant financial constraints which have in turn impeded the growth of large trading companies in the United States. We are convinced that these obstacles must be overcome and the profitability of the trading business enhanced if the coccept is to be viable. We believe that addressing the financial problem appropriately can result in a tie that can naturally bond manufacturers to a trading company and make economically practical investments necessary to provide export growth. The paradox which arises from our analysis, however, is that it takes volume to warrant investment and you can't afford to invest without volume. Thus, the problem of initial capitalization is a serious one which must also be solved.

An alternative means of resolving the serious financial constraints would be thru companies coming together and forming Webb-Pomerene Associations. As stated previously we do not believe this is likely to occur. Recent conversations with EMC's, however, have produced some information which conflicts with our opinion. One individual's company ran into financial difficulty and investments were made by his suppliers to keep him afloat. We believe it would be useful to examine this possibility at a later date, but we tend to consider it a fluke of nature.

Recommendation 1: CONDUCT A SURVEY TO ESTABLISH THE INTEREST OF MANUFACTURERS IN THE CONCEPT

We believe the first step towards proceeding with the concept must be to assess the interest in using a trading company. Our conversations with manufacturers were quite limited and did not involve testing a particular concept but rather the constraints and problems they faced beginning the export effort and their experience with various trading intermediaries.

The model we have proposed, its features and operational characteristics should be explained to groups of small businessmen around the country and their reactions documented. In addition, manufacturers' disposition to invest capital and how much capital should be established to determine whether the Webb-Association approach has merit. Further, manufacturers' comments on the availability of management should be asked.

To a very real extent, the results of this study should refute or substantiate the feasibility of implementing the concept. If manufacturer support is present, there is every reason to believe a workable ETC could be created and thrive.

Recommendation 2: DEVELOP AN FCIA/EX-IM GUARANTEE INSURANCE POLICY WHICH WOULD GIVE HOLD HARMLESS PROTECTION TO DRAFTS OF SELECTED TRADING INTERMEDIARIES AND PROVIDE A MEANS OF CREATING CREDIT

We have mentioned several times the importance of credit creating capability on the part of an American Trading Company. We believe that this protection could be afforded in the following manner. The trading company carries a master insurance policy covering all risks now covered by FCIA/Ex-Im plus non-acceptability of goods after shipment and importer default due to warranty issues. The value of this policy might be for ten times the company's net worth. To create credit, the trading company

goes to its bank with its draft on the foreign buyer and transfers its rights under its insurance policy to the bank on this specific transaction. Because the insurance coverage is backed by the full faith and credit of the United States Government and all commercial and political risks of default are covered, the bank accepts the draft at very low cost to the trading company and these funds are then credited to its account.

The appropriate fashion for attacking this recommendation would be for the Department of Commerce, the international banking community, traders and other interested parties to approach the Treasury Department and/or the Export-Import Bank and recommend an addition to United States policy in the guarantee area.

A task force comprised of members of these bodies should consider the exact criteria which need to be altered, the appropriate level of deductibles and fees and selection criteria for the policies used. We see no reason why such a policy cannot be inexpensively provided -- certainly less than 1 1/2 percent of the shipment value. If for any reason the coverage costs are above this rate, either the concept should be dismissed or some tax incentive for firms created in order to maintain a competitive cost structure vis-a-vis foreign comprtition.

In general, we believe that the concept is workable without a direct subsidy; however, since the ability to create substantial amounts of credit is crucial, if such a capability cannot be created in one way or another, the concept should be dismissed.

Recommendation 3: TEST THE COMPLETE CONCEPT ON TWO OR THREE OF THE LARGEST EXPORT MANAGEMENT COMPANIES

Our concept of the ETC is one where the initiative, drive and capital come from outside the manufacturing sector. We have also stated that we do not believe that the Export Management Companies (EMC) provide a suitable basis for the concept. A few EMCs, however, have most of the operational characteristics of our model. Rather then create a company from scratch to test the concept, if the first two recommendations are followed and the results are positive, we would recommend trying the full concept in an EMC which has several substantial business cores, over 25 suppliers and a small network of foreign offices. We further recommend that the EMCs chosen to test the

concept have a networth in excess of $1 million to insure adequate initial capitalization.

Some means of performance evaluation should be developed to quantify the concept's impact and the results measured over a two to three year period of time. During this period the concept could be reviewed and altered as necessary.

Recommendation 4: REMOVE THE INABILITY TO PARTICIPATE IN PROFITS FROM FREIGHT BROKERAGE FROM ALL INDEPENDENT EXPORT UNITS

Every attempt should be made to enhance the profitability of the trading business to draw the highest caliber of talent and additional investment into it. This ability to participate in freight brokerage should be given to all EMC's and Webb-Associations today regardless of the feasibility of the ETC concept.

Recommendation 5: ASSIST THE EMC's IN ESTABLISHING STANDARDS AND A UNIFORM CODE OF CONDUCT

The Export Management Companies are in strong need of assistance in the legal area. They particularly need prototype contracts with standard minimum term agreements, just cause termination agreements or cancellation fees to enable these firms to compete equally and still be able to protect themselves. While a national association does exist, it does not have the clout necessary to bring about this reform. The absence of those kinds of standards are causing more dysfunctionality in the industry than is good for the country.

Appendix A

Conduct of the Study

The method used to conduct this study entailed six major tasks. These tasks were as follows:

Task I: Assessment of current and pending legal constraints which would affect the formation and development of an American Export Trading Company.

Task II. Assessment of the critical issues of concern to be pursued during the conduct of the study through interviews with selected key individuals.

Task III: Development of descriptive information:

(a) The size and current operations of Export Management Companies

(b) The desire and capabilities of Export Management Companies to move in the direction of the trading company concept

Task IV: Field interviews with the major Groups currently involved in export trade (i. e., manufacturers, large United States and foreign trading companies, transportation, insurance companies, banks, and government agencies).

Task V: Feedback to selected major EMC's on progress and findings additional input on major issues.

Task VI: Development of model details, recommendations and final report.

The substantive interviews conducted during the study are included at the end of this Appendix.

Task I: Assessment of Legal Impact and Antitrust implications

The Washington law firm of Collier, Shannon, Rill, Edwards and Scott conducted an extensive legislative review of present and pending legislative acts impacting on the viability of the concept of American Trading Company as an export vehicle. This task included a review of 1) anti-trust related legislation such as the Sherman, Clayton, and and Webb-Pomerene Acts; 2) a review of banking regulations and 3) a review of pending congressional legislation. The focus of this preliminary task was on the assessment of the impact that these acts and regulations had on the feasibility of developing a United States equivilant to the current Japanese and British Export Trading Companies from an antitrust stand-point.

Task II: Assessment of Critical Study Issues:

Hay Associates conducted a series of preliminary interviews with selected key Department of Commerce Officials and Export Management Companies in order to develop the critical issues and framework for the project. This task included interviews with eleven Export Management Companies in New York, Chicao, Philadelphia, and Washington, D. C., the core of which were chosen by the Department of Commerce and then supplemented with additional interviews by Hay Associates. These EMC's ranged in size, and experience from a small newly formed firm to a well-established integrated trader whose sales volume exceeded $200 million. The group also included a) commission agents, b) distributors, and c) combination distributor/agent.

Task III: Development of descriptive information on a) the size and current operations of Export Management Companies; b) their views on their major trade constraints and c) their willingness to move in the direction of the ETC concept.

A mail survey was developed and utilized in order to reach a broad number of EMC's and receive their input. This questionnaire was developed to obtain both descriptive (size, sales volume, product lines, etc.) information and information on the perceptions held by EMC owners of future growth opportunities and trade constraints.

The methodology utilized included the survey and analysis of a randomly selected sample of Export Management Companies to which a self-administered questionnaire was provided. Appendix C includes this questionnaire and the tally of major results. The sample was drawn from the United States Department of Commerce, Bureau of International Commerce's Directory of United States Export Management Companies, and was augmented by other mail-outs to specific Export Association members. An attempt was made to draw the sample to insure both a diversity in geographic location and of product category handled. A total of 287 questionnaires were mailed out of which 65 were returned due to either the relocation or nonexistence of the firm. Eighty-five questionnaires were returned and analyzed for the purpose of this report.

The analyses was conducted by first looking at the characteristics of all the responding firms as a whole and then analyzing the responses for differences among:

1) firms who functioned primarily as distributors or those who functioned primarily as both distributors and commission agents

2) small firms with under $3 million in sales and large firms with between $3 and $15 million in sales.

This three step analyses was conducted in an effort to see if the trends among EMC's differed for the variables that would be critical for the development of an American trading company.

A tally of the total responses is in Appendix C and the detail data output will be provided to the Department of Commerce.

Task IV: Field Interviews with Manufacturers and Organizations involved in export trade to determine 1) the needs of export suppliers; 2) the existing business and financial infrastructure in the United States and 3) how these organizations could interface with an American Trading Company.

- Small and Medium-size domestic manufacturers

Interview candidates were selected from a list compiled utilizing the Dun & Bradstreet Million Dollar Directory to locate those firms in:

a) specific geographic market areas, and
b) in industries of specific interest to the study Standard Industrial Classification codes (SIC) were utilized to define these industries.

Standard Industrial Codes (SIC's) were utilized to define:

SIC:	28 Series	Chemicals
	3272	Building Materials
	3292	Building Materials
	3429	Marine Equipment
	35 Series	Machinery in General
	3523	Agricultural Equipment
	354	Industrial Equipment
	3551	Food Processing Equipment
	3561	Pumps
	361	Electrical Components
	3661	Communication Equipment
	3662	Communication Equipment
	367	Electrical Components
	369	Electronics
	3714	Pumps (Hydraulic Fluid)
	381	Instruments
	382	Instruments
	3841	Medical/Surgical Apparatus and Supplies
	3842	Medical/Surgical Apparatus and Supplies

Efforts were made to concentrate the interviews on those firms whose annual sales volume was under $15 million in order to reach a larger number of marginal or nonexporting firms.

Over thirty manufacturers were actually interviewed and approximately three times that amount contacted in an effort to set up interviews. Interviews were conducted in the following major United States cities:

San Francisco
Seattle
Los Angeles
Chicago
Philadelphia
Boston
New York

These interviews focused on the current interest in mechanisms used in exporting and the views of the manufacturers on the viability of a trading company concept and the governments current export development efforts.

- Large export trade vehicles and trading experts

  Interviews we conducted with other export traders who did not fall in the Export Management Company classification. This included interviews with the following:

  - United States trading companies
  - Japanese and British trading companies
  - Webb-Pomerene Association

- Commercial Enterprises

  Interviews were also conducted with those organizations which play a vital role in all export transactions in order to identify the feasibility of, and constraints to, the export trading company concept. Interviews were conducted with the following:

  - banks
  - transportation companies
  - insurance companies

- Government Agencies

  Interviews were conducted with numerous representatives of the nine government agencies impacting on export trade. These agencies included the following:

  - Council on Internation Economic Policy
  - Eximbank
  - FCIA
  - Department of State
  - Department of Justice
  - Department of Treasury
  - Department of Commerce
  - Federal Trade Commission
  - Small Business Administration

Task V: Feedback on study findings

Additional interviews were conducted with some of the larger Export Management Companies and Department of Commerce employees to provide feedback on the progress of the study and receive additional input and suggestions on critical issues.

Task VI: Development of model, recommendations, and report

The findings of the above tasks were utilized and amplified with additional interviews and research to produce the final recommendations in the report.

HAY ASSOCIATES

SUBSTANTIVE INTERVIEWS

Export Management Companies

Harry W. Browne
Vice President
Ferrex International Inc.

Bruce S. Chelberg
President
Getz Brothers

Paul Cherney
President
Cinefot International Corp.

John Eastwood
Manager
Auriema International Corp.

Stanley W. Epstein
President
Anglo American Aviation Co.

Joseph Gorski
President
Trade Ways, Ltd.

Leo F. Hill
President
Vanderburg and Co.

Joel D. Honigberg
President
J.P. Marshall Internationa

George H. McNeeby, III
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Ballagh and Thrall, Inc.

Walter Pfeifer
President
Engineering Equipment & Co.

Peter Rheinhard
President
E.D. Magnus and Associates

Harmon Senzel
President
Heggi and Senzel, Inc.

Aurthur A. Singer
President
Singer Products Co.

C. Wertheimer
President
L&W Exports

HAY ASSOCIATES

OTHER TRADING COMPANIES

Clarence C. Adamy
President
National Association of Food Chains

L. Hugh Ballard
President
AMATEX

J. D. Erickson
President
The Kaiser Trading Company

E. Hiroshima
EVP and Secretary
Marubeni, Inc.

Eugene M. Lang
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Samuel Cabot
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Clayton DeAllie
Owner
Clayton Auto Works

Lawrence P. Finnegan
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Narco Scientific

Robert Hamilton
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Charles D. Hultberg
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E. F. Jochen
Director, Vice President
Secretary and Treasurer
Chevron Chemical Co.

Leonard Kay
Comptroller
Mojonnier Brothers

Peter Kohnstamm
General Manager
H. Kohnstamm and Co.

Ernest Levine
Head of Administration
Admiral Tool and Mfg. Co.

Sli Manchester
President
Boston Industrial Wire Cable Co.

Jack McCaughey
International Vice President
Narco Scientific

Harold J. Monger
President
Processing Gear Co.

Liana Morrow
Export Manager
Taradyne Corporation

Ronald Naples
Director, International Operations
Hunt Manufacturing

Lester Pentak
Director, International Sales
Ecolaire

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Met-Pro Corporation

John J. Rowell
Vice President
Guardian Electric Co.

R. Henry Seelaus
Vice President, International Operations
Yarway Corporation

Anthony Shamahs
President
Frigitemp International Corp.

Jerry Shields
Marketing Manager
Gray Mills Corporation

Julian Sobin
President
Sobin Chemical Co.

James E. Tebay
President
Valmont International

R. B. Vertrees
V. P. - Marketing, Container Group
Fiberboard Corporation

Bill Webster
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APPENDIX B

THE WEBB-POMERENE EXPORT TRADE ACT - LEGISLATIVE HISTORY AND JUDICIAL INTERPRETATIONS

Introduction

This section discusses the background and legislative history of the Webb-Pomerene Act (hereinafter cited as "the Act"), summarizes the provisions of the Act, as interpreted by the Federal Trade Commission and United States courts, and examines how the Act impacts on medium and small domestic businesses which are present or potential members of Webb-Pomerene export trade associations. Special emphasis is given to the inquiry: Why have not more firms created or joined Webb-Pomerene associations in order to initiate or increase their export trade business?

Legislative History and Purpose of the Act

Concern for the exemption of export associations from anti-trust regulation became active around the turn of the century, probably as an outgrowth of the Wilson Tariff Act.[1/] International copper dealers strongly urged the Taft Administration and the House Judiciary Committee to include in the Clayton Act an antitrust exemption for exportation.[2/] When these efforts proved unsuccessful, the National Foreign Trade Council was organized to lobby for

1/ Wilson Tariff Act, 15 U.S.C. §§8-11 (1964).

2/ Hearings on Trust Legislation Before the House Comm. on the Judiciary ___ Cong., ___ Sess., pt. 11, at 433 (1914).

specific legislation.[3/] Passage of such an act was championed by the United States Chamber of Commerce[4/] and backed by President Wilson, Secretary of Commerce Redfield, the Federal Trade Commission, and the American Manufacturers Export Association.

In 1967 Paul Rand Dixon, chairman of the Federal Trade Commission, outlined to the Senate Subcommittee on Antitrust and Monopoly the history and purpose of the Webb-Pomerene Act:

"As one of its first orders of business following administration of the oath of office to the Commissioners on March 15, 1916, the Federal Trade Commission undertook an extensive inquiry into the necessity for cooperation in American export trade under Section 6(h) of its enabling Act.[5/]

3/ Hearings on the Investigation of Concentration of Economic Powers Before the Temporary National Economic Comm., ___ Cong., ___ Sess., pt. 25 at 1313 (1940).

4/ Hearings to Promote Export Trade Before the House Comm. on the Judiciary, ___ Cong., ___ Sess., pt. ___, at 38-39 (1916).

5/ Trade Commission Act, 15 U.S.C. §436(h) (1964) provides:

> (h) To investigate, from time to time, trade conditions in and with foreign countries where associations, combinations, or practices of manufacturers, merchants, or traders, or other conditions, may affect the foreign trade of the United States, and to report to Congress thereon, with such recommendations as it deems advisable (38 Stat. 721; 15 U.S.C.A., §46).

"The Commission's two volume report on "Cooperation in American Export Trade" was presented to the Congress on June 30, 1916. It gave recognition to the importance of American foreign commerce and the need to understand the conditions American exporters might meet in competition for world trade.

"The Commission report made two basic findings:

1. That other nations have marked advantages in foreign trade from superior facilities and more effective organizations.

2. That doubt and fear as to legal restrictions prevent Americans from developing equally effective organizations for overseas business and that foreign trade of American manufacturers and producers, particularly the smaller concerns, suffers in consequence. 6/

"In emphasizing this climate of competition as the touchstone for Congressional passage of a protective law, Senator Atlee Pomerene observed during the course of the debates that:

> ...In the foreign countries today the merchants and manufacturers and businessmen generally are allowed to combine to go out and seek the foreign trade, and they do combine for that purpose. If we are to meet them upon a fair basis of competition, we must place in the hands of our businessmen the same methods which the businessmen of other nations use in seeking foreign trade. 7/

6/ F.T.C., Report on Cooperation in American Export Trade, Vol. 1, at 3 (1916).

7/ 55 Cong. Rec. 7513 (1917).

"One of the principal concerns of the Act's sponsors then was this 'meeting of competition' concept which in the minds of the Act's proponents justified the passage of a law which, though antithetical to the traditional concepts of antitrust enforcement, was nevertheless justified in this arena of foreign competition.

"As already noted, the Commission report concluded that small American producers were especially disadvantaged in international trade. With respect to the small businessman the report observed:

> ... They have felt keenly their disadvantage in attempting to enter foreign markets singlehanded in the face of the powerful, united, and long-established competitors of other nations. They realize that for them export trade must be done largely through the medium of export commission houses and export merchants. But they realize the advantages -- in some cases the necessity -- of their own direct representation and their own foreign organization if they are to build up an enduring trade. At present, cooperation with the other small manufacturers is the best solution to the difficulty before them. 8/

Emphasizing this further, Congressman Edwin Y. Webb stated during the congressional debates:

> In order to build up an export trade it is necessary to have the most expert representatives in the foreign trade fields to introduce and thoroughly advertise our American goods. This involves a large expenditure of money before the trade can be established. A number of our larger enterprises are able to do this alone,

8/ F.T.C., Report on Cooperation in American Export Trade, Vol. 1, at 200 (1916).

> and for this reason the proposed law would not greatly benefit these large enterprises, but our smaller manufacturers and merchants would be prohibited from undertaking such an enterprise because of the tremendous costs that it would involve. 9/

"Read in its entirety, the legislative history reveals three principal purposes for the legislation:

> 1. To promote and increase the export trade of the United States;
>
> 2. To encourage and expand the exports of small business; and
>
> 3. To provide a means of effective competition with foreign cartels or combinations in export markets." 10/

Statutory Provisions of the Act

Definitions. Under Section 1 of the Act, 15 U.S.C. §61 (1964), the words "export trade" are defined to mean "solely trade or commerce in goods, wares, or merchandise exported, or in the course of being exported from the United States or a territory thereof to a foreign nation." This section specifies in particular that "export trade" does not include acts in the course of "production, manufacture, or selling for consumption or for resale, within the United States or any territory thereof of such goods, wares, or merchandise." An "association" under the Act may be any corporation or combination, by

9/ Cong. Rec. 3564 (June 13, 1917).

10/ Hearings Before the Subcomm. on Antitrust and Monopoly of the Senate Comm. on the Judiciary, 90 Cong., 1st Sess., at 132-133 (1967).

contract or otherwise, of two or more persons, partnerships, or corporations." 15 U.S.C. §61 (1964)

Exemption. Sections 2 and 3 of the Act, 15 U.S.C. §§62-63 (1964) declare that the Sherman Act should not be construed as declaring illegal an export association "entered into for the sole purpose of engaging in export trade and actually engaged solely in such export trade or an agreement made or act done in the course of export trade by such association." This exemption, however, is limited by three provisos:

1.) That the association, agreement or act is "not in restraint of the export trade of any domestic competitor of such association", and

2.) That the association, agreement or act is "not in restraint of the export trade of any domestic competitor of such association", and

3.) That such association "does not, either in the United States or elsewhere, enter into any agreement, understanding, or conspiracy, or do any act which artificially or intentionally enhances or depresses prices within the United States of commodities of the class exported by such association, or which substantially lessens competition within the United States or otherwise restrains trade therein."

Jurisdiction. Section 4 of the Act, 15 U.S.C. 164 (1964) amends the Federal Trade Commission Act of 1914, 15 U.S.C. §41-58 (1964). This amendment extends the jurisdiction of the Commission to "unfair methods of competition used in export trade against competitors engaged in export trade, even though the acts constituting such unfair methods are done without the territorial jurisdiction of the United States."

Administration and Enforcement. Section 5 of the Act, 15 U.S.C. §65 (1964), outlines the registration and annual report requirements including certain prescribed information that must be furnished to the Federal Trade Commission by a Webb-Pomerene association. At the present time, the mere filing by an association of appropriate papers is tantamount to registration and annual reports to the Commission usually take the form of business letters. However, the absence of rigorously enforced reporting procedures does not diminish the power of the Commission under Section 5 to 1) investigate alleged violations of law, 2) recommend readjustment of an association's business to comply with law, and 3) refer its findings and recommendations to the Attorney General should an association fail to comply with the Commission's recommendations.

Although the Commission has limited statutory authority to assure that associations confine their activities to the exemptions provided by the Act, provisions authorizing the Commission to make any orders, impose any prohibitions or restricting, or make any binding adjudication with respect to violations are conspicuously absent. The Supreme Court has held that such authority is not vested in the Commission but is reserved to the Department of Justice.[11/] Moreover, the Court declared that the Commission's powers

11/ U.S. Alkali Export Ass'n. v. U.S., 325 U.S. 196 (1949).

conferred by §5 of the Webb-Pomerene Act do not preclude suits brought by the Department of Justice before the Commission has made an investigation or recommendation.[12/]

Administrative & Judicial Interpretation of the Act

From its enactment in 1918 until 1949, the Act was administered by the Commission without the aid of judicial construction, although the Commission issued several recommendations interpreting the Act. In 1924 an association of silver producers made an inquiry concerning the participation of an export association in foreign cartels. The Commission's response, now known as the "Silver Letter", formed the basis of many misconceptions about the actual extent of exemption under the Act from Sherman antitrust laws. The Letter "interpreted the Act as permitting export associations to participate in foreign cartels and as allowing export associations to exist for the sole purpose of fixing prices at which their members must sell abroad (i.e., it was not necessary that the association actually perform a selling function).[13/]

The next significant action by the Commission was its first "recommendation for readjustment of business," which was issued to Pacific Forest Industries. Several such recommendations and a handful of court decisions

12/ Id.

13/ 33 A.B.A. Antitrust L.J. 107 (1967).

have followed. These rulings generally constrict the ambit of antitrust exemption initially believed to have been granted by the Act. The effects of such interpretations, as well as the usefulness of the Act itself, are perhaps reflected in the small number of Webb-Pomerene Associations (26) currently operating under F.T.C. supervision. Although over 260 associations have been organized under the Act since 1918, only a few of them have maintained Webb-Pomerene status for any appreciable length of time.

Two cases have gone furthest in interpreting the Webb Act; U.S. v. United States Alkali Export Association, 325 U.S. 196 and United States v. Minnesota Mining and Manufacturing Co., 92 F. Supp. 947.

In the Alkali case, the government charged the defendants, a Webb-Pomerene association, with restricting the export of alkalis from the United States, prohibiting the import of alkalis from abroad, limiting production of alkalis, restraining domestic competition, and price fixing.[14/]

Noting that "all contracts, combinations, and conspiracies aimed at obstructing the foreign commerce of the United States come within the broad prohibitions of the antitrust laws,[15/] the court further observed:

> Unquestionably the cartelization of the world, if accomplished by the individual corporate defendants separately and not through an association organized under the Webb

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14/ 86 F. Supp. 59, 51 (S.D.N.Y. 1949).

15/ Id. at 66.

> Act, would be a flagrant transgression of the antitrust laws. . . No citation of authority is any longer necessary to support the proposition that a combination of competitors, which by agreement divides the world into exclusive trade areas, and suppresses all competition among the members of the combination, offends the Sherman Act.
>
> . . . Consequently, to hold in this case that defendants, by employing the medium of an export association, may restrain our foreign trade with impunity, uninhibited by the sanctions and proscriptions of the Sherman Act, would be to ignore the plain intent of the statute. 16/

Approving issuance of an injunction to prevent resumption of unlawful activities, the court noted:

> The international agreements between defendants allocating exclusive markets, assigning quotas in sundry markets, fixing prices on an international scale, and selling through joint agents are not those "agreements in the course of export trade" which the Webb Act places beyond the reach of the Sherman Law. 17/

In United States v. Minnesota Mining & Mfg. Co., 18/ the defendants' united forbearance from supplying certain areas with American-made goods, when other foreign companies owned jointly by the defendants could supply those same areas with equivalent foreign-made goods. Condemning this program of export forbearance, the District Court stated:

> Prima facie there could hardly be a more obvious violation of Section 1 of the Sherman Act than for American manufacturers controlling four-fifths of the export trade of an industry to agree not to ship

16/ Id. at 66-67.

17/ Id. at 70.

18/ 92 F. Supp. 947 (D. Mass. 1950)

> to particular areas but to do their business there through jointly-owned foreign factories. It is, in statutory language, a "combination . . . or conspiracy, in restraint of trade or commerce . . . with foreign nations." 19/

The effect of the defendant's joint export forbearance upon their domestic competitors was obvious to the Court which observed the restraint precluded American competitors from "receiving business they might otherwise have received from the markets served by these jointly-owned foreign factories." 20/

Financial considerations, also, attracted the Court's attention. Defendants contended that supplying foreign customers from foreign factories was more profitable and, therefore, "in the interest of American enterprises." 21/ The Court rejected this argument and held (f)inancial advantage is . . . irrelevant where the action . . . taken by a combination . . . restricts American commerce, for Congress, in the Sherman Act, has condemned whatever unreasonably restrains American commerce regardless of how it fattens profits of certain stockholders." 22/

Since a major purpose of the Webb-Pomerene Act was to increase the flow of foreign capital into the United States, the court stated:

> Noting in the statute, nor in its legislative history, nor in the penumbra of its policy justifies or has any bearing upon the right of defendants to join in establishing and financing factories in foreign lands. Export of capital is not export trade. 23/

19/ Id. at 961.

20/ Id.

21/ Id. at 962.

22/ Id.

23/ Id. at 963.

In U.S. v. Concentrated Phosphate Export Ass'n.,[24/] the Supreme Court further clarified what could be considered as "export trade" or "acts in the course of export trade." In that case the question was presented whether the Concentrated Phosphate Export Association (CPEA), organized and operated under the Webb-Pomerene Act, violated Section 1 of the Sherman Act, 15 U.S.C. §1, in connection with its sales of fertilizer to the Republic of Korea under the United States foreign aid program (AID).

The court held that because the purchases by the Republic of Korea were initiated, controlled and financed by the American Government they did not constitute "export trade." While noting congressional intent to grant anti-trust exemptions for the purpose of stimulating export trade, the Court quickly added that the "exemption created was carefully hedged in to avoid substantial injury to domestic interests."[25/]

In that case AID required preference for American procurement, the major world trading nations were not eligible to compete on the contracts involved and procurement was limited essentially to the United States and underdeveloped countries. For these reasons, the Court concluded that "to say that American producers needed an additional stimulus (Webb-Pomerene protection) to be able to compete strains credibility."[26/]

24/ U.S. v. Concentrated Phosphate Export Ass'n., 273 F. Supp. 263 (S.D.N.Y. 1967).

25/ Id. at 206.

26/ Id. at 209.

Hence CPEA's price fixing and sales allocations with regard to nominal purchases by the Republic of Korea were not exempt from Sherman Act prohibitions.

Although few cases have been decided on the application of the Act, additional principles have emerged from F.T.C. "recommendations of readjustment." In summary, a Webb-Pomerene Export Association may not:

> 1. Enter into agreements of any kind with domestic producers who are not members of the association which fix prices, terms of sale, or otherwise restrain the free export of goods of non-member firms. This prohibition includes agreements by an association to sell the products of non-members, thereby fixing the non-member's export prices. 27/
>
> 2. Enter into agreements of any kind whereby exports of domestic non-member producers are deducted from the export quota of the association. 28/
>
> 3. Enter into agreements of any kind which prohibit association members from selling to domestic exporters in competition with the association, or which deduct sales by a member within the United States from the member's export quotas through the association. 29/

27/ Pipe Fittings and Valve Export Ass'n., 45 F.T.A. 917 (1948); Sulphur Export Corp., 43 F.T.C. 820 (1947); Export Screw Ass'n. of U.S., 43 F.T.C. 980 (1947); Phosphate Export Ass'n., 42 F.T.C. 555 (1946); Carbon Blacks Export Inc. 46 F.T.C. 1245 (1949).

28/ Florida Hard Rock Phosphate Export Association, 40 F.T.C. 843 (1945); Sulphur Export Corporation, 43 F.T.C. 820 (1947); Phosphate Export Association, 42 F.T.C. 555 (1946).

29/ Florida Hard Rock Phosphate Export Association, 40 F.T.C. 843 (1945); Pacific Forest Industries, reported in a footnote at 40 F.T.C. 843 (1940); Phosphate Export Association, 42 F.T.C. 555 (1946).

4. Falsely represent that it is the sole export representative of the United States in a given industry. 30/

5. Enter into agreements of any kind with owners or operators of shipping terminals, thereby restricting use of such terminals to only association members. 31/

6. Be involved in acquiring control of any patent or process useful in the production of the goods it markets. 32/

7. Enter into an agreement of any kind which precludes or restricts the right of the association or its members from using a trademark or label in the United States. 33/

8. Enter an agreement of any kind whereby it controls or attempts to control any of the terms or conditions of sales by its members within the United States. 34/

9. Enter an agreement of any kind with any foreign producer or cartel whereby the United States is designated as an exclusive trade area, or imports into the United States are otherwise curtailed or restricted. 35/

10.. Own stock, either directly or indirectly through subsidiaries, in corporations or other producers outside the United States. 36/

30/ Pacific Forest Industries, reported in a footnote in 40 F.T.C. 843 (1940).

31/ Phosphate Export Association, 42 F.T.C. 555 (1946); Florida Hard Rock Export Association, 40 F.T.C. 843 (1945).

32/ Sulphur Export Corporation, 43 F.T.C. 820 (1947).

33/ General Milk Co., Inc., Ltd. 44 F.T.C. 1355 (1947).

34/ Phosphate Export Association, 42 F.T.C. 555 (1946); United States v. United States Alkali Export Association, 86 F. Supp. 59 (S.D.N.Y. 1949).

35/ Export Screw Association of the United States, 43 F.T.C. 980 (1947); Phosphate Export Association, 42 F.T.C. 555 (1946); United States v. United States Alkali Export Association, 86 F. Supp. 59 (S.D.N.Y. 1949).

36/ General Milk Co., Inc., Ltd. 44 F.T.C. 1355 (1947); Export Screw Association of the United States, 43 F.T.C. 980 (1947); United States v. Minnesota Mining & Mfg. Co., 92 F. Supp. 947 (D. Mass. 1950).

11. Enter an agreement of any kind whereby foreign producers are guaranteed the right to sell within a given area a specified tonnage over and above sales in that area by the association. 37/

12. Enter an agreement of any kind which discriminates among its members as to the right of withdrawal, resignation or restricting the right of former members to compete with the association after withdrawal. 38/

13. Conduct office operations jointly with a domestic trade association. 39/

14. Enter an agreement of any kind to "maintain the status quo" in the world market of the industry and to do nothing which would encourage or increase competition in the industry. 40/

15. Require members to accept "unreasonable" restrictive withdrawal rights from the association as a condition of membership. 41/

16. Take into membership anyone who is not a citizen of the United States, nor any foreign purchaser, customer, representative or agent of a foreign company. 42/

37/ Sulphur Export Corp., 43 F.T.C. 820 (1947).

38/ Phosphate Export Ass'n., 42 F.T.C. 555 (1946).

39/ Carbon Black Export, Inc., 46 F.T.C. 1245 (1949).

40/ Sulphur Export Corp., 43 F.T.C. 820 (1947).

41/ United States v. Minnesota Mining & Mfg. Co., 92 F. Supp. 947 (D. Mass 1950).

42/ Phosphate Export Ass'n., 42 F.T.C. 555 (1946).

17. Enter into an agreement of any kind with a foreign company engaged in the manufacture or sale of the same commodity exported by the association to 1) fix prices, 2) give notification of inquiries for bids, 3) allocate individual orders, 4) divide sales territories, or 5) pay compensation to bidders. 43/

In addition to the above restrictions on permissible Webb-Pomerene activities, the Commission advised in 1966 that "while membership in a Webb-Pomerene association by a firm owning foreign establishments is permissible the statutory exemption enjoyed by the association is lost if artificial or intentional enhancement or depression of domestic prices is in any way traceable to the foreign operation of member firms." 44/

Effect of Webb-Pomerene on Export Trade

In summarizing the impact of the Act on export trade, Mr. Wilbur L. Fulgate reported at a 1974 A.B.A. meeting that "the Act has not been a major factor in U.S. foreign trade. However, over the years it has accounted for an average of 5% of such trade and, therefore, it should not be discounted." 45/ In its 1967 Report on the Act, the Commission noted that "in 1962 more than 80 percent of Webb sales involved consumer goods and services and industrial raw materials. Of these, by far the most important were motion picture and

43/ U.S. v. Electrical Apparatus Export Ass'n., Civil Action No. 33275 (S.D.N.Y. 1947), 44 F.T.C. 1421 (1949).

44/ Advisory Opinion Digest No. 91, 70 F.T.C., 18974 (1966).

45/ 43 Antitrust L.J. 547 (1974).

television film packages which by themselves accounted for more than half of all foreign sales reported as Webb-assisted."[46/] The Report pointed out that such associations had not exported to any substantial extent those technically complex and differentiated products produced by capital intensive industries. The conclusion of the Report recognized that "in no major area of the world is the total amount of U.S. exports increased to a significant degree by Webb-Pomerene association activity."[47/]

Mr. Fulgate posits why the Act doesn't have greater impact on capital intensive industries:

> "Perhaps use of the Act may not have been needed in such industries, or perhaps, because such industries involve very large companies, the antitrust risks have been considered too great." 48/

He also recognizes that "the Act does afford a way for cooperative export by small and medium size companies in the same industry who wish to share the risks of a new venture. . . . Today opportunities abound for U.S. companies, new to foreign markets, to have a try at exporting and distributing their goods abroad. A Webb association may well meet their needs."[49/]

46/ Webb-Pomerene Associations: A 50 Year Review, 37 (1967).

47/ Id. at 42.

48/ 43 Antitrust L. J. 548 (1974).

49/ Id. at 548.

However, a writer for Industry Week has opined that "the biggest reason most U.S. firms don't export is: they simply don't know how."[50] He then encourages small and medium business to use government sources, studies, contacts, etc. to expand into the foreign market. In doing so, the vagaries and uncertainies surrounding Webb-Pomerene law may inhibit use of an export trade association.

Perhaps the most accurate explanation why businesses do not use a Webb-Pomerene association is that "the basic marketing strategy of most American manufacturers rests heavily on the concept of product differentiation and the use of brand names. Many manufacaturers have avoided joint exporting because they are unwilling to blend the individual image they have developed over the years with that of their competitors into a common association image."[51]

50/ C. A. Nekvasil, Why Are You Afraid to Export, Industry Week, Sept. 24, 1973.

51/ Joint Exporting Efforts by U.S. Companies May Get Increased Emphasis, Commerce Today, Oct. 1, 1973.

LEGISLATIVE EFFORTS TO AMEND WEBB-POMERENE IN THE LAST FIVE YEARS

A review of the history of congressional efforts to initiate or amend legislation relating to export trading corporations in the last five years indicates that such efforts have focused on three areas:

(1) Broaden provisions of the Webb-Pomerene Act to include services,

(2) Exempt Webb associations from private treble damage actions and exempt individuals from criminal penalties, and

(3) Create greater certainty with respect to the application of anti-trust laws by establishing pre-clearance procedures and giving the FTC sole jurisdiction to administer the law.

No legislation has been enacted into law during this period.

In 1971, Senators Inouye and Magnuson introduced the Export Expansion Act, S. 2754, which would have authorized chartered export associations, allowing the establishment of groups of firms to engage in export activities as long as they operated within the legal confines of a charter approved by the Department of Commerce. The Chairman of the FTC, Miles Kirkpatrick testified in opposition to S. 2754, and suggested that the Export Trade Act of 1918 (the Webb-Pomerene Act), be amended to exempt trade associations from private treble damage actions and individuals from criminal penalties.

In 1972, Senator Inouye and Magnuson introduced a series of bills, S. 4114 through S. 4120. These bills included modifications reflecting the testimony received on S. 2754, and S. 4120 incorporated the FTC's suggestions regarding exemptions from treble damage actions and criminal penalties and

included the export of services as an exempted activity. The other bills introduced in that series, among other things, would have established a Trade Development Corps of trained business personnel to assist the government in programs to make American exports more competitive, authorized regional American merchandise centers offering services such as warehousing, distributing, translating, etc., established a joint export association program permitting the government to enter into cost sharing contracts with private firms, and expanded the kinds of goods which could be imported into foreign trade zones for manufacture and export.

In 1973, Senator Inouye and others introduced S. 1483, which would have amended the Webb-Pomerene Act by including services and excluding treble damage actions and criminal sanctions.

Also in 1973, Senator Inouye and others introduced S. 1486 which would have established a Federal Export Agency within the Department of Commerce to foster the development of export associations or joint export projects, and provided special incentives to small businesses.

S. 1774, introduced in 1973 at the Administration's request, again included the exemption of services under Webb-Pomerene, the changes in anti-trust laws, added a pre-clearance procedure designed to provide greater certainty with respect to application of the anti-trust laws to export trade associations, and gave the FTC exclusive authority to determine whether the activities of registered groups are in conformance with their registration statements.

Senator Inouye and Congressman Thomas Rees introduced identical bills in 1975, S. 1973 and H. R. 9449 respectively. Again, this legislation exempted services under the Export Trade Act. In addition, the legislation established new criteria for eligibility to participate in Webb associations: export sales must be likely to be substantially increased as a result of membership in an association, and not likely to increase significantly without membership, and such individual membership in an association is essential to the functioning of the association.

The Secretary of Commerce in consultation with the Chairman of the FTC would be required to establish within the Commerce Department a program to promote and maximize the formation of associations and use of the provisions of the Act in a manner consistent with the Act and anti-trust laws. Lastly, in an effort to provide greater certainty in the application of the antitrust laws, the FTC and the Attorney General were required to meet periodically to avoid conflicting positions regarding the formation and maintenance of associations.

As of this date, Senator Inouye has indicated willingness to try to move his legislation through the Senate. However, the House Judiciary Committee, claiming a crowded calendar of higher-priority bills, has shown little interest in acting on the legislation.

Laws and Regulations Relating to the Use of Bankers' Acceptances in Export Trade

The Commerce Department contract calls for a review of banking regulations, definitions and credit instruments as they apply to export transactions. The following paragraphs summarize the existing laws and regulations concerning bankers' acceptances, the credit instrument generally used in export transactions. Further research is required as to the practical inhibitions on export transactions inherent in the present system, and the need for changes in the statutes or regulations.

12 CFR 201 sets forth the Fed's regulations concerning extensions of credit by Federal Reserve Banks. Section 201.4(b) authorizes the Fed to discount bankers' acceptances (1) arising out of an importation or exportation or domestic shipment of goods or the storage of readily marketable staples or (2) drawn by a bank in a foreign country or dependency or insular possession of the United States for the purpose of furnishing dollar exchange: Provided, That such acceptance complies with the applicable requirements of Section 13 of the Federal Reserve Act. Section 13 (12 USC 346) authorizes Federal Reserve Banks to discount acceptances having a maturity at the time of discount of not more than 90 days' sight, exclusive of days of grace, and which are indorsed by at least one member bank. Acceptances drawn for agricultural purposes receipts or other such documents may be discounted with maturities up to six months.

Section 201.5(d) limits the amount of credit granted to any one obligor to that amount authorized under 12 USC 84, to 10 percent of paid-in capital

stock plus surplus. The Fed has interpreted its regulations to provide that demand paper is eligible for discount. 12 CFR 201.104. Certain federally insured obligations are eligible as collateral for advances. 12 CFR 201.108. A full guarantee of principle and interest is required. 12 CFR 201.108(c). (Eximbank is included but FCIA is not.)

Under 12 CFR 211.107, participation by banks in acceptance credits is extended to Edge corporations.

Acceptances of agricultural cooperative marketing associations having maturities of up to nine months are eligible for discount. 12 USC 351.

COLLIER, SHANNON, RILL, EDWARDS & SCOTT
WASHINGTON, D. C. 20007

MEMORANDUM

18 January 1977

TO: JAMES CASSANO AND CRAIG JOHNSON
HAY ASSOCIATES

FROM: SKIP HARTQUIST AND RICHARD FRANK

RE: WEBB-POMERENE EXPORT TRADE COMPANIES -- LEGALITY OF RESTRICTIVE WITHDRAWAL AGREEMENTS

Question -- Whether an export trading corporation, established pursuant to the terms of the Webb-Pomerene Export Trade Act, may require individual members, as a condition of membership, to agree not to withdraw from the group or at least not to export independently in competition with the Export Trade Corporation for a period of five years?

The legislative history of the Webb-Pomerene Export Trade Act ("Webb Act") indicates that Congress was greatly concerned with the inability of small and medium sized American manufacturers to effectively compete in foreign markets. Paul Rand Dixon, former chairman of the Federal Trade Commission described the three principal purposes of the Act as follows:

> "1. To promote and increase the export trade of the United States;
>
> 2. To encourage and expand the exports of small businesses; and
>
> 3. To provide a means of effective competition with foreign cartels or combinations in export markets." 1/

1/ Hearings Before the Subcommittee on Antitrust and Monopoly of the Senate Committee on the Judiciary, 90 Cong., 1st Sess., at 132-133 (1967).

Senator Atlee Pomerene, one of the Act's sponsors observed during the course of the debates that:

> . . . In the foreign countries today the merchants and manufacturers and businessmen generally are allowed to combine to go out and seek the foreign trade, and they do combine for that purpose. If we are to meet them upon a fair basis of competition, we must place in the hands of our businessmen the same methods which the businessmen of other nations use in seeking foreign trade. 2/

A principal concern of the Act's sponsors was this "meeting of competition" concept which in their minds justified passage of the law which, though antithetical to traditional concepts of antitrust law, was nevertheless justified in the international arena.

Sections 2 and 3 of the Act, 15 U.S.C. section 62-63 (1964) declare that the Sherman Act should not be construed as declaring illegal an export association "entered into for the sole purpose of engaging in export trade and actually engaged in solely in such export trade or an agreement made or act done in the course of export trade by such association." This exemption, however, is limited by three provisos:

1. That the association agreement or act "is not in restraint of trade within the United States."

2. That the association, agreement or act is "not in restraint of the export trade of any domestic competitor of such association", and

3. That such association "does not, either in the United States or elsewhere, enter into any agreement, understanding, or conspiracy, or do any act which artificially or intentionally enhances or depresses prices within the United States of commodities of the class exported by

2/ 55 Cong. Rec. 7515 (1917).

> such association, or which substantially lessens competition within the United States or otherwise restrains trade therein."

Few cases have been decided on the application of the Act.[3/] The courts and the Commission have, however, confronted the question of whether a Webb-Pomerene Export Association may require members to accept restrictive withdrawal agreements as a condition of membership.

In Phosphate Export Association, 42 F.T.C. 555 (1946) the Association adopted a resolution whereby each member bound itself to retain membership for at least ten years. If any member found it necessary to resign, such resignation would not become effective unless and until such member entered into an agreement with the Association providing that all sales by it or for its account of phosphate rock for export to Europe should continue to be handled by the Association with the same quota as that existing prior to resignation. In holding the Resolution might possibly violate the Sherman Act, the Commission concluded:

> This resolution placed a restriction around the right of a member to withdraw from the Association, and contemplated that in the event of the resignation of any member, except O. & C. and Swift, PEA should continue to handle the exports to Europe of such ex-member. While certain restrictions on the right of immediate withdrawal from an assocation may be necessary and justifiable, it is not considered that a restriction which might run for a period of 10 years, as in this situation, is reasonable. The provision requiring an ex-member to market its European

3/ The leading cases construing the Act are: U.S. Alkali Export Ass'n v. United States Court, 325 U.S. 196 (1949); United States v. Minnesota Mining and Manufacturing Co., 92 F. Supp. 947 (D. Mass. 1950); United States v. Concentrated Phosphate Export Ass'n., 273 F. Supp. 263 (S.D. N.Y. 1967); additional principals have emerged from F.T.C. "recommendations of readjustment."

exports through PEA raises the question as to whether or not an Association may, by agreement, handle the export trade of a competing nonmember producer. Such an arrangement necessarily means that the Association and the nonmember by agreement fix the prices, terms and conditions upon which the nonmember's sales are made in export trade. While such an arrangement as among the members may be said to be valid under the terms of the Webb- Pomerene Act, it is not considered that associations may deal with nonmembers in this manner without entering into unlawful agreements and thus violating the Sherman Act, which prohibits contracts in restraint of foreign commerce, except such contracts as may be entered into by members of a Webb law association organized and acting under the provisions of that law. (Emphasis supplied.) Phosphate Export Ass'n, supra at 837-8.

In its Recommendations for the Readjustment of the Business of PEA[4/] the Commission suggested:

3. That Phosphate Export Association rescind and cancel any and every intermember bylaw, rule, contract, or agreement discriminating as between members in their right to withdraw or resign from the Association, or restricting or limiting the right of withdrawal or resignation of any member by requiring that such member's export trade, after such resignation or withdrawal, must be handled by or through the Association.

4. That Phosphate Export Association in the future cease and desist from selling, handling, marketing or disposing of Florida pebble land phosphate for the account of or belonging to any producer who is not a regularly admitted and recognized member of the Association.

4/ Section 5 of the Webb-Pomerene Export Trade Act (15 U.S.C. section 65 (1973)) grants the Federal Trade Commission the power to investigate possible violations of the antitrust laws committed by Webb-Pomerene Export Associations and "if it shall conclude that the law has been violated, it may make to such association recommendations for the readjustment of its business . . . If such association fails to comply with the recommendations of the Federal Trade Commission, said Commission shall refer its finding and recommendations to the Attorney General of the United States for such action thereon as may be deemed proper."

Even though the Commission concluded that the PEA resolution probably violated the Sherman Act, it did suggest that "certain restrictions on the right of immediate withdrawal . . . may be necessary and justifiable." What type of restrictions would be considered necessary and justifiable was left unanswered.

In United States v. Minnesota Mining and Mfg. Co., supra, members of a Webb-Pomerene Export Company entered into an agreement in 1929 providing that a party to the agreement desiring to withdraw prior to December 31, 1934 could do so by giving one years notice and agreeing not to compete with the Export Company until after December 31, 1956. After December 31, 1954 a party could withdraw by giving two years notice. On June 1, 1944 the Export Agreement was amended to extend these dates to December 31, 1964 and December 31, 1966 respectively. The Government argued the terms of the Export Agreement violated both section 1 and section 2 of the Sherman Act. It was the Government's view that it was unlawful for four-fifths of the American export trade to combine to export exclusively through one corporation from which they could not withdraw at will.

In analyzing the Governments claims, the court reasoned:

> If the Government's contentions are sound, they must rest on the basis that these terms of the Export Agreement and the conduct which they expressly prescribe are what are not called per se violations of the Sherman Act. For there is no other evidence for finding as a fact that defendants designed or used the Agreement or the Export Company with the purpose of effect of monopolizing commerce in violation of section 2 or restraining commerce in violation of

section 1. 3/ United States v. Minnesota Mining and Mfg. Co., supra at 963.

In Minnesota Mining and Mfg. Co., Judge Wyznaski points out that every successful export company inevitably affects adversely the foreign commerce of those not in the joint action, but "[T]he Webb-Pomerene Act is an expression of Congressional will that such a restraint shall be permitted." Id. Judge Wyzanski held most aspects of the Export Agreement in Minnesota Mining and Mfg. to fall within the purpose and scope of the Act:

> Yet it is said that the arrangement at bar goes far beyond an ordinary Webb-Pomerene corporation. But surely the 1918 Congressional policy of promoting export corporations contemplated many of the features at which the 1950 Department of Justice looks askance. The recruitment of four-fifths of an industry into one export unit was foreseen by Congress, 53 Cong. Rec. 13538; 55 Cong. Rec. 3583-3584. The assignment of stock in an export association according to quotas, if not foreseen, has at least been silently acquiesced in. Federal Trade Commission Annual Report for 1939 at p. 149; TNEC Mono. No. 6, pp. 141, 288. There may have been no similar Congressional prevision or approval of the firm commitments of members to use the unit as their exclusive foreign outlet, the refusal of the unit to handle the exports of American competitors, the determination of what quotas and at what prices each member should supply products to the unit, the fixing of re-sale prices at which the unit's foreign distributors should sell and the limitation of distributors to handling products of the members. Nonetheless, these are all such normal features of any joint enterprise and usually so essential to its stability and to preventing its members from taking individual selfish advantage of the knowledge and opportunities that have come to them as a group that, absent special circumstances revealing their unfairness or oppressive character in a particular setting, they are not outside the license granted by the Webb-Pomerene Act. (Emphasis supplied.)

3/ This analysis suggests that even if the terms of an agreement are found not be constitute per se violations, if the purpose or effect is to monopolize or restrain commerce, Sherman Act violations can be established.

With regard to the manufacturer's agreement not to withdraw from the group or at least not to export independently at any time before 1966, the court found the period "unreasonably long and [not] supported as a device necessary to achieve stability." Id. Concluding that the provision must be replaced by a reasonable withdrawal allowance, the court held:

> Taking into account the length of time the Export Company has already functioned and the changed situation which the decree in this case will effectuate, this Court determines that hereafter a reasonable provision would be one which allowed a member to withdraw within 2 years of the effective date of the decree of this Court or at any time thereafter upon giving 1 year's written notice. Id. at 966.

Thus in the two cases where the issue of restrictive withdrawal provisions has been examined, lengthy withdrawal requirements have been held violative of the Sherman Act. 6/ In Minnesota Mining and Mfg., a period of one to two years was raised as a reasonable alternative. In both Phosphate Export and Minnesota Mining and Mfg., however, the export companies had been operating for a number of years and had presumaly achieved stability. Accordingly, it appears that the Commission and the court would find a five-year membership requirement reasonable during the developmental stages of an Export Company. Once some degree of stability is achieved, the period should be reduced to one to two years.

There does not appear to be any antitrust violation where each manufacturer agrees not to sell its products independently in competition with the Export Company. The court in Minnesota Mining and Mfg. specifically held that:

6/ In Phosphate Export Ass'n supra, the Commission only suggested that the resolution violated the Sherman Act.

> "firm commitments of the members to use the unit as their exclusive foreign outlet "[is a]" normal feature of any joint enterprise and usually so essential to its stability . . . that absent special circumstances revealing their unfairness or oppressive character in a particular setting, they are not outside the license granted by the Webb-Pomerene Act." United States v. Minnesota Mining and Mfg. supra at 95.

It is unlawful, however, to enter into agreements of any kind which prohibit association members from selling to domestic exporters in competition with the association. In Pacific Forest Industries, reported in a footnote at 40 F.T.C. 843 (1940) the Commission made the following recommendation for the readjustment of the association's business:

> "1. That Pacific Forest Industries shall not by its by-laws, contracts with other members, or associate members, or otherwise, prohibit its members from selling plywood directly to American exporters."

See also Phosphate Export Association supra; United States v. United States Alkali Export Association, 96 F. Supp. 59 (S.D. N.Y. 1949) (where the Commission suggested that it would be unlawful to enter into an agreement of any kind whereby the Association attempts to control any of the terms or conditions of sale by its members with the United States.)

CONCLUSION

It is permissable for members to agree not to withdraw from the Export Company or at least not to export independently so long as the period of time is reasonable. Prior cases indicate that a period of one to two years would clearly be acceptable and that a period of ten to twenty years would not. Further, it appears that a newly created Export Company will be accorded greater flexibility concerning withdrawal requirements so that it can achieve stability. Any agreement not to sell within the United States, including to competing exporters, would violate the Sherman Act.

APPENDIX C

The following Questionnaire was used in analyzing the characteristics of Export Management Companies, their views on future trade problems and potentials, and their strategy for future growth.

The percentage of total respondents checking each answer is provided for those interested in more detailed information than provided by the analysis in Part IV.

APPENDIX C

DIB 4066P
OMB 41-576084

UNITED STATES DEPARTMENT OF COMMERCE

Survey of Export Management Companies on the Export Trading Company Concept

© HAY ASSOCIATES 1977
1845 Walnut Street Philadelphia, PA 19103

1. Please list your major product lines and the percentage they contribute to your annual sales volume?

(The responses showed that 68% of the respondents concentrated their efforts on High Technology products. See Appendix for definition of High Technology classification.)

2. How many product lines or product "families" (i.e., machine tools, electronic components, construction equipment, etc.) do you handle in total?

One major one	11.8%	Under 30	19.7%
Under 5	42.1%	Under 50	1.3%
Under 10	23.7%	Over 50	1.3%

3. On the average, what would best describe your export operations?

Respondents

.07% act primarily as an export agent working on commission

62% act primarily as an export distributor, buying goods on own account and marking them up in foreign markets

31% act substantially in both of the above

4. What percentage of your annual revenue currently comes from the following categories? How do you think this will change in the next five (5) years?

The responses showed that most EMC's function primarily as exporters.

5. The following is a list of exporting functions. Please mark the ones you provide for your clients.

	Frequently	Occasionally	Rarely
Informal periodic reports on market conditions	33.8%	48.6%	17.6%
Periodic reports on competitive moves	39.2	40.5	20.3
Periodic reports on new product applications	26.8	43.7	29.6
Special formal research	7.5	28.4	64.2
Training and instructing foreign sales network in applications of the product	60.9	39.1	
Developing and maintaining contact with major customers abroad	97.5	2.5	
Consolidating orders to the company from several overseas customers	35.1	28.4	36.5
Keeping clients aware of impending import controls, tariff increases, or other adverse developments in foreign markets	35.2	49.3	15.5
Assisting suppliers to arrange for licensing or joint manufacturing efforts in markets where borders are being closed to imports of the product	12.0	36.0	52.0
Developing marketing and sales strategy in markets	84.6	14.1	1.3
Establishing pricing policy	87.2	9.0	3.8
Translating brochures, manuals and other documents at export manager's expense	39.2	29.7	31.1
Translating brochures, manuals and other documents at manufacturer's expense	13.0	24.6	62.3
Arranging for all C.I.F. quotes in response to inquiries from abroad	98.7	1.3	
Arrangint for physical movement of goods from factory or from port of exit to foreign customers	94.9	2.6	2.6
Handling all relations with foreign freight forwarders for proper documentation	91.0	3.8	5.1

	Frequently	Occasionally	Rarely
Perform your own freight forwarding	24.6%	15.9%	59.4%
Advising on, or arranging for, all export packing and marketing	86.1	10.1	3.8
Consolidating shipments overseas with products of other manufacturers for lower freight costs	41.9	27.0	31.1
Purchasing and warehousing goods in your own name	37.3	29.3	33.3
Assume all responsibility for delivery of goods	88.6	5.1	6.3
Manufacturing of goods yourself for export	10.5	7.0	82.5
Arranging for insurance	89.7	7.7	2.6
Acting as insurance agent on a commission basis	11.3	3.8	84.9
Arranging the servicing of products through overseas distributors	77.3	12.0	10.7
Arranging the servicing of products by your firm	20.6	25.4	54.0
Arranging the servicing of products by manufacturer	19.4	41.8	38.8

6. In thinking about your clients, on the average, who is primarily responsible for establishing the overseas marketing strategy in each country in the following areas?

	Manufacturer	You	Shared by You and Manufacturer
Advertising Strategy	3.8%	53.8%	42.3%
Promotional Strategy	3.9	75.3	20.8
Pricing Strategy	2.6	62.8	34.6
Distributing Strategy	2.6	90.9	6.5

7. How many manufacturers or suppliers do you handle on the average? between 5 & 25

8. On average, how much of each supplier's export business do you handle?

Under 25%	31.4%
Under 50%	5.7%
Under 75%	10.0%
Under 100%	52.9%

9. The following is a list of other international business structures your suppliers may be using in addition to your own services. What proportion of your suppliers use each of the following?

	Most Use	Some Use	Few Use
Direct foreign investment	0%	26.7%	73.3%
Direct exporting by the firm	10.3%	38.2%	51.5%
Other export management companies	0%	32.8%	67.2%
Cooperative (piggyback) exporters	0%	8.5%	91.5%

10. What is your current export sales volume? If applicable, include in your export sales volume sales generated by licensing agreements your Company has arranged for supplier.

Under $3 million	57.5%
$3 – $5 million	16.3%
$5 – $10 million	12.5%
$10 – $20 million	10.0%
$20 – $50 million	3.8%
Over $50 million	0%

11. How do your sales compare with what they were in 1970?

declined since 1970	5.2%
about the same	11.7%
up 50 – 100% since 1970	33.8%
up 100 – 300% since 1970	29.9%
up over 300% since 1970	19.5%

12. Ignoring the effect of inflation, what would you expect your sales level to be by 1980?

about the same as today	11.4%
up 50 – 100% from today's level	67.1%
up 100 – 300% from today's level	15.2%
up over 300% from today's level	6.3%

13. How cyclical are your sales? This is, how would you describe your sales trends over the past ten years?

fluctuating widely	3.9%
fluctuating	20.3%
moderately stable	49.4%
stable	21.5%

14. Using annual revenues from both domestic and international sales as an indication of size, could you estimate what percentage of your suppliers fall within the following categories?

The majority of the respondents indicated that the bulk of their clients had under $25 million in both domestic and international sales volume.

15. Could you please indicate the importance, in terms of percentage contribution to sales, that the following market areas play in your annual sales volume?

	Rank Order of Market Regions by Sales Importance.
Latin America	1
Europe	2
Asia (except Japan)	3
Middle East	4
Japan	5
Africa	6
Canada	7
Eastern Europe	8

16. What do you feel your potential for export growth is in each of these markets in the next five years?

	Good	Average	Poor
Europe	37.8%	40.5%	21.6%
Eastern Europe	14.9	17.9	67.2
Africa	38.9	36.1	25.0
Middle East	65.3	26.7	8.0
Asia (except Japan)	38.7	53.3	8.0
Japan	30.3	32.0	36.8
Latin America	48.7	40.8	10.5
Canada	15.6	31.1	53.3

17. Could you specify the importance that the following factors have on deciding the geographic markets in which you concentrate your sales efforts:

	Always	Sometimes	Never
Available distribution network	60.0%	32.0%	8.0%
Knowledge of market area	73.1	25.6	1.3
In-country business contacts	67.9	26.9	5.1
Receptiveness of local government to U.S. business	28.8	50.7	20.5
Market match with product line	76.7	21.9	1.4
Market exclusively for product	41.2	45.6	13.2
Competitive environment from other export traders	29.3	56.0	14.7
Competitive environment from manufacturers	36.6	53.5	9.9

18. Please estimate the number of suppliers you have added, lost, or sought in a typical, average year using the past five years as a base period.

	Number of Suppliers
New suppliers added	between 1 & 5
Current suppliers lost	" " " "
New suppliers courted or sought	

19. How important are each of the following sources in providing you with leads on potential new export suppliers?

	Very Important	Some Importance	Unimportant
Current customers	41.3%	37.5%	21.3%
Department of Commerce	17.7	45.6	36.7
Professional colleagues	14.7	46.7	38.7
Own investigation	91.1	8.9	
Overseas market intelligence	54.5	32.5	13.0

20. What is the duration of your supplier contracts on average?

between 1 to 3 years

21. What is the average length of time a supplier maintains a relationship with your firm?

between 1 to 10 years

22. When suppliers cease to export through your firm, what export actions do they take?

	Frequently	Occasionally	Rarely
Stops exporting	4.7%	31.3%	64.1%
Merges with another firm with international department	15.4	63.1	21.5
Starts own export activity	57.1	30.0	12.9
Invests in manufacturing capability abroad	4.8	38.1	57.1
Exports through cooperative (piggyback) exporter	12.7	87.3	
Exports through another export management company	6.2	49.2	44.6
Exports through a foreign trading company	6.9	24.1	69.0

23. What do you think the reasons are for most of your suppliers ending an exporting relationship with your firm? (Please rank by order of occurrence, placing a "1" beside the reason most often occurring, a "2" beside the next most frequent, and so forth.)

Supplier believes he can achieve greater market penetration 1

Supplier believes he can accomplish the export function less expensively per unit cost 2

Supplier wants to control the foreign market 3

Supplier wants to export in geographic areas your firm does not handle 4

24. On average, at what level of export sales volume does a supplier tend to terminate his relationship with you?

Under $100,000 7%	$100,000-$200,000 7%
$200,000-$500,000 32%	$500,000-$1 million 29%

One $1 million
25%

25. What specific programs or steps do you think it would take to retain a supplier who has experienced good export growth within your firm? List up to 4 suggestions.

1. developing better/closer client relationship.
2. showing continuous sales growth
3. development of stronger exclusive contents
4. joint participation with manufacturer

26. Are there any steps the U.S. Government could take to encourage longer relationships between suppliers and EMC's?

1) public education exporting & role of EMC

2) legal aid in settling standards

3) financial aid to EMC's & clients

27. How willing are you to lower your profit margins in return for longer-term contracts?

20.0% Very willing 12.0% Somewhat reluctant
44.0% Somewhat willing 24.0% Very reluctant

28. Realizing that you face different competitors in different markets, on balance, how would you rank the following as competitors? Give ratings of 1 to 7, with "1" being the greatest overall competition.

	Rank
Foreign small and medium size manufacturers	1
Multinational corporation	2
Large foreign general trading companies	3
U.S. small and medium size manufacturer	4
Other U.S. export management companies	5
Other foreign export management companies	6
Cooperative ("Piggyback") exporters	7

29. It is frequently said that U.S. exporters cannot trade on an equal basis with foreign exporters. To what extent do you agree with this statement?

30.3% Strongly agree 21.1% Somewhat disagree
39.5% Somewhat agree 9.2% Strongly disagree

30. To the extent that you see foreign exporters at an advantage, which of the following factors do you feel are important in giving them a competitive edge over U.S. exporters?

	Very Important	Somewhat Important	Not Very Important
Knowledge of market area	31.0%	39.4%	29.0%
Company owned overseas sales network	36.8	42.6	20.6
Home-government support in financing	91.7	5.6	2.8
Home-government support in marketing	75.4	17.4	7.2
Favorable availability to offer credit	84.9	15.1	
Their lower costs of doing business	36.2	37.7	26.1
Legal advantages	10.6	31.8	57.6
Price of their goods	62.0	31.0	7.0
Quality of their goods	11.9	38.8	49.3

31. What do you feel the competitive position of U.S. exporters in general will be in five years?

- ☐ the same 33.3%
- ☐ better 29.2%
- ☐ worse 37.5%

32. To what extent do you feel that the following are factors which have inhibited the development of your company? (Circle your choice)

	To a Very Great Extent	To a Considerable Extent	To a Moderate Extent	To a Limited Extent	To a Very Little Extent
Availability of capital	23.2%	11.6%	21.7%	18.8%	24.6%
Cost of capital	17.1	8.6	20.0	22.9	31.4
Availability of low cost rediscounting facility	10.3	22.1	16.2	22.1	29.4
Credit risks	20.0	18.6	25.7	20.0	15.7
Supplier turnover	1.5	17.6	20.6	22.1	38.2
U.S. government restrictions/ regulations	14.5	7.2	11.6	36.2	30.4
Foreign govern restrictions/ regulations	30.7%	29.3%	22.7%	5.3%	12.0%
Competition from foreign export traders	22.7	25.3	33.3	9.3	9.3
Competition from U.S. export traders	5.4	18.9	45.9	17.6	12.2
Propensity of U.S. manufacturers to "go it alone"	6.8	24.3	28.4	21.6	18.9
Cumbersome trade documentation/ traditions	1.4	6.9	25.0	38.9	27.8
Transportation costs	37.8	29.7	14.9	10.8	6.8
Finding, training and holding qualified staff	5.4	16.2	28.4	17.6	32.4
Difficulty in locating new suppliers	9.5	13.5	37.8	27.0	12.2
Difficulty in dealing with suppliers	9.5	18.9	24.3	16.2	31.1
Developing adequate foreign distribution systems	6.8	20.3	31.1	21.6	20.3
Inability to enter or enforce an agreement of any kind with foreign agents to control terms or condition of sales to the U.S.	4.8	4.8	15.9	27.0	47.6
Inability to enter or enforce an agreement with foreign agents whereby the U.S. is designated as an exclusive trade area	4.9	8.2	4.9	23.0	59.0
Inability to enter or enforce agreements designating exclusive trade areas for your foreign distributors in their own countries	2.9	10.1	15.9	21.7	49.3

33. How often do you presently use or have used in recent years the following to assist with your financial requirements?

	Rarely	Occasionally	Frequently
FCIA	56.1%	18.2%	25.8%
Eximbank	77.6	17.2	5.2
Factoring	88.5	5.8	5.8

34. Are you qualified as a DISC?

☐ Yes 45.3% ☐ No 54.7%

35. Please describe your current exporting operations in terms of the number of individuals who work for you or represent you in each category.

The average EMC operates through a small (under 25 people) U.S. sales office, using a network of exclusive and general distributors supplemented by occasional trips abroad on the part of U.S. staff.

36. From a purely business standpoint, which marketing tactic would you prefer?

32.1% establish your own overseas sales offices

67.9% geographic diversification through foreign agents

37. How much do the following represent factors that hinder your opening overseas sales offices?

	Very Little	Somewhat	A Considerable Amount
High overhead	11.1%	19.4%	69.4%
Unstable sales	27.5	40.6	31.9
Narrow product line	29.4	45.6	25.0
Manpower availability	36.8	38.2	25.0
Insufficient capital	27.9	29.4	42.6

38. How interested are you in opening overseas sales offices?

Very	31%
Somewhat	33%
Little	36%

39. How much volume would you need in a market before you would want to open a sales office?

The majority indicated between $500,000 & $1 million in sales in the market.

40. Could you rank (with "1" being first choice) the importance of the following factors in causing you to choose particular product lines?

Line has high potential in geographic areas where the firm is currently active	1
Personal expertise in the product line	2
Line has high potential in new geographic areas where the firm desires to expand	3
Staff knowledge of product	4
Low competition in the product line	5

41. Rank (with "1" being the first choice) the importance of the following factors in causing you to drop a product line in a market?

Lose exclusivity in a market region	1
Failure to be competitive with similar products	2
Product sales don't grow	3
Manufacturer fails to fulfill orders	4
Manufacturer's decision to stop exporting	5

42. Where do you expect the majority of your future sales growth to come from? Rank in order, with "1" being the most likely.

Penetrate existing market areas with current products, but wider and better distribution system.	1
Expand geographically into new market areas with current products.	2
Diversify product mix in current geographic areas.	3
Diversify both product mix and geographic areas.	4
Diversify the firm into complementary ventures such as freight forwarding, insurance, etc.	5

43. Do you do any of the following in your present operations? In the future, would you seriously consider doing any as a means of expanding your business?

	Number of Respondents Doing	Percentage Indicating Future Incentives: Unlikely	Perhaps	Likely
Establishment of network of parent overseas offices	17	48.5%	27.9%	23.5%
Construction of overseas warehousing	8	72.6	17.8	9.6
Manufacture of products	7	70.3	17.6	12.2
If legalized, purchase of freight forwarder	1	73.0	14.9	12.2
Seek license arrangements or joint ventures for clients	21	26.8	43.7	29.6
Invest in overseas ventures	11	48.5	42.6	8.8
Assist in equipping operating ventures	5	53.7	26.9	19.4
Make long-term commitments to market for and sell the products of these ventures	10	47.8	33.3	18.8
Pull together ventures requiring international subcontracting and project management	3	59.2	23.7	17.1

44. For those operations above that you would be unlikely to undertake, how important are the following factors in causing you to take a negative attitude or decision?

	Important	Somewhat Important	Not Important
Want to specialize in marketing	69.4%	20.8%	9.7%
Uncertainly attached to changing operations	41.4	37.1	21.4
Lack of capital to accomplish this	40.3	31.3	28.4
No desire to make large capital investments	50.7	29.0	20.3
Return on investment would be unfavorable	60.6%	27.3%	12.1%

45. As the Chief Executive and perhaps majority owner of your enterprise, the goals and future of the enterprise are a reflection of your own goals and aspirations. What would best describe your own goals relative to the future of your business?

12.7% Create a good standard of living for yourself and your fellow owners year-to-year.

29.1% Create equity for yourself and family by investment of "profits" to take advantage of growth opportunities while maintaining a balance with a "comfortable" annual payout.

10.9% Create equity position of maximum proportions to be realized at some future time, say beyond 10-15 years.

47.3% Create a firm that will be a major force in international trade which will be influential in the development of exports in the future.

46. Please indicate the ownership pattern of your firm as follows:

24.3% Single owner

31.1% One owner with more than 51%

39.2% Less than five interests own total

2.7% Five to ten owners

1.4% More than ten owners

1.4% Public ownership

47. Approximately how large an equity capital base is committed to the business?

27.8% Under $100,000

45.6% $100,000 to $500,000

15.2% $500,000 to $1 million

10.1% $1 million to $5 million

1.3% $5 million to $10 million

0% Over $10 million

48. Do you support the capital in the business with personal advances or guarantees?

32.1% Never

11.5% Rarely

33.3% Sometimes

23.1% Regularly

49. Approximately how much external financing is available to your business at periods of peak need?

Less two times equity capital	36.6%
2 – 5 times equity capital	53.5%
5 – 8 times equity capital	4.2%
Over 8 times	5.6%

50. Please indicate your average pretax return on sales.

Under 5%	34.7%	15% – 20%	14.7%
5% – 10%	30.7%	20% – 25%	2.7%
10% – 15%	14.7%	Over 25%	2.7%

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September 17, 1979

Mr. Max I. Stucker
Arthur Anderson & Co.
69 West Washington Street
Chicago, Illinois 60602
U. S. A.

Dear Mr. Stucker,

In accordance with your request as per your telex dated September 5, 1979, we present in the accompanying Appendix relevant information on the Korean general trading company system, particularly those relating to Korean trading companies operating abroad. Based on the enclosed detailed information, we present hereunder our general comments to your specific questions:

1. How successful have these companies been in their effort to develop foreign markets?

   The rates of increases in export operations of these companies in 1976, 1977 and 1978 which are 102%, 93.5% and 22.4%, respectively, indicate a tremendous boost to the government's export drive especially in 1976 and 1977. The lower rate of increase in 1978 seems to indicate a more realistic rate of growth considering the present worldwide economic crisis.

2. What are the major operating features of these companies and in what ways has the government let its support to these private traders?

   Pages 1 to 2 of the Appendix describes the general features of the Korean general trading company system, its major policies and operating requirements. The major policies of the government offers advantages in terms of continued government financial support, relaxation of government restrictions, and a more efficient administration of export transactions.

Do these companies offer any special inducements such as attractive export financing, discounts, priority shipping, etc.?

The special inducements extended by the government to general trading companies can reasonably justify a more attractive export financing and a faster processing of export shipments.

Does the government offer any special inducements to the companies such as reduced taxes?

The Major inducements of the government for the operation of general trading companies are listed on page 3 to 4 of the Appendix.

We hope the accompanying information would adequately meet your request. Please write us if you need any additional information.

Very truly yours,

Shin. Kum & Co.

RELEVANT INFORMATION ON THE KOREAN GENERAL TRADING COMPANY SYSTEM

A. General Background

In 1975, the Korean Government introduced the general trading company system with the main objectives of avoiding certain weaknesses described hereunder encountered in carrying out the export program and ensuring the continued rapid growth of exports.

1. Inability of the small exporters to undertake specialized international marketing

2. Uneconomical small volumes in units of export by the individual exporters

3. Ineffective performance of direct exports by small manufacturers

4. Instability of the financial position of individual exporters

5. Ineffectiveness of the Government's supports

The major policies of the new system are primarily as following:

1. To induce the individual small exporters to form into a larger unit - general trading company and, if possible, separate the manufacturers from direct exporters.

2. To assist the general trading companies to specialize in international marketing

3. To support them with the necessary financial and administrative benefits.

4. to relax the rigid regulations on their overseas operations

B. Operating Requirements

The government prescribed a set of requirements which each company should meet to be able to continue operations as a general trading company:

The key points of the requirements involve each company's financial position, total export amount and export amount by item, and number of overseas branches and agents. The details of the requirements which have undergone revisions from 1975 to 1979 are as follows:

	1975	1977	1979
1. Paid in Capital should be over	U$ 2 million	U$ 4 million	NA
2. Total exports should be over	50 million	150 million	2% of the total Korean export of the previous year
3. Number of items exported, each item involving over U$1 million, should be over	7	10	5
4. Number of countries products were exported to, each country involving over U$1 million, should be over	10	20	NA
5. Number of overseas branch	10	20 *	20 *
6. Capital stock should be open to the public for sale	NA	Required	Required
7. Export to strategic areas should be over	NA	1. Actual export Middle East: 15% Middle and South America: 3% Africa : 3% 2. Branches and agents: 2 branches or agents in each of the above areas.	NA

* Although there are more than 2 branches and agents each in the U. S. and Japan, there are counted only as 2 branches and agents.

C. Existing General Trading Companies

Eleven (11) companies were designated as general trading companies in 1975 and 1976 and 13 companies in 1977 and 1978. During 1979, 12 of these general trading companies have continued operations. Table 1 of this Appendix presents pertinent information for each of these 12 companies. All 12 are leading privately owned companies each having over 20 overseas branches and many local affiliated companies, except for Korea Trading International Inc. (KTI), KTI was specially established by the Korean Traders Association for the purpose of exporting products made by many small and medium manufacturers. It is exempted from the requirements mentioned earlier and is designated to operate as a general trading company as part of the government's export strategy.

The total number of overseas branches and agents has increased from 142 in 1975 to 302 in 1979 around all the world, of which about 25% are in Asia, 19% in Middle East, 18% in Europe, 17% in North America, 9% in Middle Europe and South America and 11% in Africa.

D. Status of Export Operations

The total export of general trading companies amounted to US$832 million in 1975, which was 16.4% of the total Korea exports. It, thereafter, increased by 102%, 93.5% and 22.4% for 1976, 1977 and 1978 respectively 1978 exports reached US$3,985 million, 31.3% of the total Korea exports.

About 25% of the total export of the general trading companies are for Asia including Japan, 38% for North America and 29% for Europe and Middle East areas.

Table 2 of this Appendix shows the export amounts of the general trading companies, including Yulsan Industrial Co., Ltd. which discontinued operations in 1979.

E. Inducement of the Government

The general trading companies have developed so far with the active support of the Government in various aspects. The major inducements from the Government are as follows:

1. Trade administration

   - o Preferential support in international bidding competition for over 500 thousand dollars
   - o Relaxation of regulations on the importation of raw materials

2. Financial aspects

   - o Preferential support of export financing over the individual exporters
   - o Financing for the stock of finished goods

3. Exchange regulations

   - o Increasing the foreign exchange limit of overseas branches and agents
   - o Relaxation of regulations relative to foreign exchange transactions of overseas branches and agents.

4. Tax Benefits

   There are no special inducements in tax aspects specifically for the general trading companies. They enjoy the same tax benefits which are generally given to individual exporters as follows:

   - o Deferment of taxation on allowance for loss from export, overseas market exploitation and price decrease of exportable goods
   - o Treatment of accelerated depreciation as a deductible expense
   - o Application of zero Value Added Tax rate for the exported goods.
   - o Refund of custom duties on the imported raw materials used for exported goods.

Table 1
List of Korean General Trading Companies (GTC)
as at December 31, 1978
(Amounts in Thousands of U. S. Dollars)

Name of Company	Address	Name of President	Capital Stock	Total Amount of Export 1977	Total Amount of Export 1978	No. of Overseas Br. (Local Affiliated Companies)	Branches or Local Companies in U.S.A.	Major Items
Korea Trading International Inc.	Seoheung Bldg. 68, Kyonji-dong, Chong-ro-ku, Seoul Telex K27434	Mr. Bum Sik O	$ 3,093	$ 24,463	$ 31,313	6	New York Office	P. U. Bag, Cuttlefish, Stuffed Toy, Necklace, etc.
ICC Corporation	520-1, Boop-dong, Buk-ku, Busan Telex K27251, K26548	Mr. Dong Hwan Cho	$13,773	$328,205	$472,277	23 (17)	New York Branch L. A. Branch Chicago Branch Highcity Branch	Footwears, Iron & Steel Products, Machinery, Electronics, Textile & Garments, Construction Materials, Sports & Leisure Goods, etc.
Kumho & Co., Inc.	Samsung Bldg., 50, 1 ka, Uljiro, Chung-ku, Seoul Telex K27321	Mr. Sung Yong Park	$10,309	$204,140	$256,012	20 (11)	Kumho U.S.A. Inc. Kumho N.Y. Inc. Chicago Office	Tire, Iron & Steel Products, Cement, Machinery, Electronics, Toys , Textile & Garments, etc.
Dae Woo Industrial Co., Ltd.	Daewoo Center, 286, Yang-dong, Chung-ku, Seoul Telex K23341-5	Mr. Woo Choong Kim	$84,124	$501,238	$703,808	48 (24)	New York Branch L. A. Branch Chicago Branch Daewoo Int'l (America) Corp. Daewoo Int'l Corp. SF Branch	Textile & Garments, Footwears, Bags, Sports & Leisure Goods, Iron & Steel Products, Machinery & Parts, Vechiles & Tire, Rail-cars, Ships, Electronics, etc.
Bando Sangsa Co., Ltd.	Lucky Bldg. 282, Yang-dong, Chung-Ku, Seoul Telex BANDO K27266 K27470	Mr. Cha Doo Koo	$ 8,247	$211,737	$323,624	23 (16)	Bando Sangsa New York Inc. Bando Sangsa L. A. Inc. Chicago Office	Garments, Food Stuffs, Metal & Machinery, Chemicals, Electric & Electronic Goods, Sporting Goods Stationery, Sundry Goods.
Sam Sung Co., Ltd.	250, 2-ka Taepyung-ro Chung-ku, Seoul Telex K2257 K28565	Mr. Se Chang Song	$24,742	$506,931	$433,394	32 (24)	New York Office Huston Office L. A. Office Chicago Office	Industrial Machinery & Plants Electric & Electronic Goods Transportation Equipments, Iron & Steel Products, Chemicals, Garments, Food Stuffs, Sundry Goods
Samha Co., Ltd.	KAL Bldg., 51, Sogong-dong, Chung-ku, Seoul Telex SAMHA K2288	Mr. Young Joo Kim	$11,340	$212,900	$261,603	21 (14)	Samhwa New York Co., Ltd. Samhwa New York Inc. Samhwa LA Co., Ltd.	Shoes, Garments, Bags, Electric & Electronic Goods, Machinery, Steel Products, Chemicals, Food Stuffs, PVC Products

Sun Kyong Ltd.	5-3, 2-ka, Namdaemoon-ro, Chung-ku, Seoul Telex SUKYONG K24851 K24852 K24853	Mr. Suck Won Yu	$15,464	$246.734	$283,370	23 (8)	Sunkyong Int'l Inc. L. A. Branch Miami Branch Chicago Branch	Polyester Fabrics, Shirts, Blouse, Dress, Suit, Jackets; Ginseng Products, Bags, Wig Products, Farm & Marine Products, Electric & Electronic Appliances
Ssangyong Corporation	Ssang Yong Bldg. 24-1, 2-ka, Ju-dong, Chung-ku, Seoul Telex TWINDRA K28214, 28442, 24270	Mr. Yong Hai Wo	$ 6,186	$175,519	$264,463	22 (10)	New York Office L. A. Office	Portland Cement, Raw Silk, Sweater Machinery, Machine Parts, Steel Products, Transformer, Electric Motor
Hanil Synthetic Fiber Ind., Co., Ltd.	222, Yangduk-dong, Masan city, Gyungbuk-province Telex HANILCO K24284, 26460	Mr. Jong Won Kim	$41,561	$158,302	$183,276	26 (5)	New York Branch L. A. Branch	Acryl Fiber, Sweater, Textile, Garments, Toys, Carpet
Hyundai Corporation	485-1, Sinsa-dong, Gangsu-ku, Seoul Telex K24119 HDSNGSA K23101 HDCORP K23175-7 HDCORP	Mr. Hee Yung Chung	$16,495	$319,802	$259,653	31 (25)	New York Office Miami Office L. A. Office Houston Office Chicago Office Dallas Office	Ships, Plant, Automobile, Container, Railway Carriage, Steel Products, Chemicals, Yacht, Heavy Electric Equipments, Garments
Hyosung Corporation	Dongsung Bldg. 17-7, 4-ka, Namdaemun-ro, Chung-ku, Seoul Telex KYOSTAR K23121-5	Mr. Choong Seon Lee	$10,309	$119,443	$337,808	27 (14)	New York Branch L. A. Branch Seattle Branch	Tire & Cube, Iron & Steel Products, Electric & Electronic Products, Chemicals, General Machinery, Plants & Industrial Machinery, Yarn & Fibric, Garments, Tire Cord Fabric, Leather Products, Vessel & Yacht, Wet Battery

Note: One company, Yulsan Industrial Co., Ltd., was designated as a general trading company in 1977. The company however, failed to meet the requirements in 1979. Hence, the designation as a GTC was cancelled in 1979.

APPENDIX

Table 2
Export by Individual Comapny
(in Million U. S. Dollars)

	1975	1976	1977	1978
Korea Trading International Inc.	$ 11.9	$ 18.1	$ 24.5	$ 31.3
ICC Coproration	63.7	197.1	328.2	472.3
Kumho & Co., Inc.	32.3	98.9	204.1	256.0
Dae Woo Industrial Co., Ltd.	161.0	301.3	501.2	705.8
Bando Sangsa Co., Ltd.	31.1	134.4	211.7	329.6
Sam Sung Co., Ltd.	223.2	355.0	506.9	439.4
Samhwa Co., Ltd.	27.9	105.3	212.9	260.6
Sun Kyung Ltd.	55.8	114.1	246.7	283.4
Ssang Yong Corporation	125.4	140.9	175.5	264.5
Hanil Synthetic Fiber Ind. Co., Ltd.	66.2	104.3	158.3	188.3
Hyundai Corporation	-	-	319.8	259.7
Hyosung Corporation	34.1	112.7	199.4	337.8
Yulsan Industrial Co., Ltd.	-	-	165.8	156.0
Total	$ 832.6	$1,682.1	$ 3,255.0	$ 3,984.7
Increase Rate to the Previous Years	-	102.0%	93.5%	22.4%
% of the Total Export	16.4%	21.8%	32.4%	31.3%
Total Korea Export	$5,081.0	$7,715.1	$10,046.5	$12,710.6

September 24, 1979

The Honorable Adlai E. Stevenson
Chairman, Subcommittee on
International Finance
Committee on Banking, Housing,
and Urban Affairs
United States Senate
Washington, D. C. 20510

re: September 1979 Hearings by the
Subcommittee on International
Finance on S.864, S.1499, and S.1563.

Dear Senator Stevenson:

The Electronic Industries Association (EIA) requests that this letter be made part of the record on these hearings. We applaud the spirit that lies behind the introduction of the several bills under consideration by the Subcommittee. The U.S. antitrust laws have, in our judgment, inhibited and do inhibit the development of U.S.-based international trading organizations that are appropriate both to the diversity and potential for expansion in this country's foreign trade and to the benefit of our national economy.

We have several constructive suggestions which, if incorporated into the proposed legislation, would provide mechanisms for successful joint venture into the world marketplace by U.S. manufacturers of high-technology products. While departing from the long era of constraint, the bills do not yet provide enough relaxation to attract new-to-export electronic companies to enlist, nor to offer already-successful exporters of electronics a mechanism for realizing more or larger transactions overseas.

The export performance of the U.S. electronic industries is testimony enough to EIA's interest in and our members' commitment to the exportation of American goods: some 25 percent or $13.3 billion of U.S. electronics production is exported from this country. That these volumes could be further increased through improvements in U.S. legal institutions, we have no doubt.

S.864, The Export Trade Association Act of 1979
and
S.1499, The Export Trade Activities Act

By their nature, the markets for electronic products render Webb-Pomerene associations unattractive to manufacturers in the electronic industries. The antitrust relief proposed in S.864 and S.1499 would accomplish little in changing this long-standing perception. Hence, while EIA applauds these bills as a manifestation of Congressional desire to remove nationally damaging and unnecessary restraints on U.S. exporters, we feel it incumbent upon us to state our judgment that these bills would — if legislated — improve only marginally the international marketing capabilities of U.S. electronic producers.

ELECTRONIC INDUSTRIES ASSOCIATION • 2001 EYE STREET, N.W. WASHINGTON, D.C. 20006 • (202) 457-4900
TWX: 710-822-0148

S.1663, The Export Trading Company Act of 1979

In previous testimony before the Subcommittee, EIA has pointed to the competitive effectiveness of Japanese trading companies in penetrating world-wide markets for our products. While this bill's proposed antitrust exemptions and relief from taxation are commendable, other provisions mitigate strongly against the establishment or effectiveness of U.S. export trading companies. By way of constructive suggestions, we wish to signal as candidate for remedial amendment these features of the present bill:

- By requiring that the benefits which the bill would confer be granted solely on the basis of the export of goods and export-related activities, the proposed legislation ignores the reality that substantial exporting firms must also of necessity frequently become significant importers.

  The import/export trade balances of such firms will necessarily vary from year-to-year, from country-to-country, and according to changes in demand for individual items constituting the firm's product mix. This is especially the case where the trading company must, in order to sell export goods, agree to accepting offsets or other quid pro quo imposed by the importing country.

- The strictures against manufacturing on the part of an eligible export trading company or any member of its controlling group will almost certainly prevent a building upon the experience, skills and resources of this country's already-successful and -aggressive exporters: manufacturing companies themselves.

- The stricture which appears, inter alia through Title I — so as to require that not less than 75 percent of the total value of goods and services be represented by U.S. Content — simply reinforces the disincentives where it does not render impossible the participation of major U.S. exporters in such trading companies.

- The limitations on ownership and the divestiture requirements set forth in Sec. 102(c) of the bill are compounding disincentives to the establishment of trading companies of size or growth potential. Almost certainly, the thrust of these provisions is to lead to the setting up of such companies at levels of small capitalization and/or undercapitalization.

  The track record for such ventures is not inspiriting, particularly when the founding parties cannot be related to manufacturers.

- The reliance upon limited financing by the Export-Import Bank would, we fear, be illusory. The merest review of the comparative financial strength of representative Japanese trading companies in competitive goods will, we suggest, demonstrate our point. Trading companies require for success highly-leveraged financial operations based upon diversified and changing utilization of the many varieties of borrowing and lending instruments.

> The stringent limits on total resources to which Eximbank is subject, when coupled to the limitations contained in the bill, would cause such trading companies to turn necessarily to the money markets of the private sector. Unfortunately, however, with the antecedents and credit-worthiness of such trading companies in doubt, the private markets would likely be unwilling to provide the requisite funds at reasonable cost.

We remind your Subcommittee that ten percent of all U.S. exports is in the form of electronic products. Even more, in the form of systems built into equipment of other classification, is exported as Aircraft, Machine Tools, and the like. These, the high-technology products, are among this economy's most exportable...in years of feast as well as famine abroad. An export development mechanism would do well as to include, not exclude, the makers of products proved exportable.

• • •

In conclusion, EIA hopes that these three bills mark the beginning of a sustained effort by Congress to relax antitrust constraints in the interest of substantial export expansion. They arrive at a first plateau beyond which can now be discerned a pattern of reasonable remedies: effectively assisting U.S. firms in competing overseas while still maintaining the spirit of competitiveness called for under these laws.

To legislate at this plateau would, however, deflect concern for this country's necessary export expansion into an unwarranted and mistaken complacency.

Sincerely yours,

Peter F. McCloskey
President

STATEMENT OF JACK VALENTI

PRESIDENT OF

MOTION PICTURE EXPORT ASSOCIATION OF AMERICA, INC.

BEFORE THE

SUBCOMMITTEE ON INTERNATIONAL FINANCE

SENATE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

on

S. 864

The Export Trade Association Act of 1979

September 17, 1979

I am submitting this statement for the hearings record in my capacity as President of the Motion Picture Export Association of America, Inc., a Webb-Pomerene Act association whose members constitute the major exporters of motion pictures and television films from the United States to foreign countries. (A list of these companies is attached to this statement).

The Association supports S. 864, the Export Trade Association Act of 1979. The member companies' experience in the export of their products benefitting as they do under existing export trade legislation, clearly demonstrates the actual and potential value of such legislation to exporters generally. In the thirty-five years of the existence of this trade association, the member

companies have steadily increased the value of their exports and now return to the United States a net surplus each year of six hundred million dollars in our balance of payments. It is our considered judgement such a return would not have been possible without existing legislation. Any expansion of the present law to include additional exporters will inevitably help both the United States balance of payments situation and the revenue potential of those exporters. We heartily endorse S. 864 for that reason.

While we fully understand the reasons that caused Congress to vest the basic jurisdiction over export trade associations in the Federal Trade Commission, we believe that the Department of Commerce would be a preferred agency to promote a further creation and existence of export trade associations.

Under S. 864 the Federal Trade Commission would not be prevented from fulfilling its general functions under current law, but its activities in respect to export trade would be restricted to its time-honored antitrust functions. We think it is both logical and appropriate that the Commerce Department, which has the basic responsibility for the promotion of exports, be charged with the initial encouragement and supervision of export trade associations.

Last year an extensive review of export trade associations was undertaken by a Presidential Commission for the Review of Antitrust policies and was studied in detail by an Advisory Panel of business leaders. The Motion Picture Export Association and other export association members presented their views on the vital need for export trade associations at a time when the United States is bleeding from trade deficits that least year were up to the $30 billion mark. We not only elaborated on our experiences and the benefits we derive from current law, but pointed out that many exporters could derive this necessary benefit.

The Business Advisiory Panel members, some of whom did not favor the existing law, felt that there was substantial merit to our position and recommended that the antitrust immunity of export trade association should be expanded rather than contracted. This recommendation was adopted by the Presidential Commission in its final report in January 1979 and is embodied in one of the principal provisions of S. 864. For this reason, if for no other, this legislation is worthy of support. When we consider the enormity of the needs of the United States for an increase in export trade, the pending bill is a matter of urgent priority.

Although we wholeheartedly endorse the basic concepts embodied in S. 864, we believe, however, that it can be improved in two respects:

1. The bill does not specifically state that the existing body of legal and administrative interpretations of the bill will continue to apply to the law as expanded by this proposed modification. The existing interpretations provide a degree of certainty and clarity in making business judgments. These interpretations should be retained to enable a continuation of confidence in the dictates and mandates of the export trade association legislation.

2. Section 13 of the bill calls for a seven year study to examine the effect of the operation of this legislation on domestic competition and on the U.S. trade deficit. It also provides that a Presidential Task Force shall recommend within that period to either continue, revise, or terminate the Webb-Pomerence Act. We urge that the seven year period should be extended to ten years.

> The reason for an extension is based on our experience that it takes five years of operating under the Act to fully explore its value. This means that only those associations formed within the first two years will have acquired the requisite knowledge to properly evaluate the benefits derived. It is likely to take more than two years for a sufficient number of associations to have commenced operations to provide the data for a meaningful study. We believe ten years would better accomplish this purpose. Notwithstanding our comments on this point, we feel very strongly that only after a study such as is envisioned in Section 13 of the bill can a proper determination be made regarding the continuance or discontinuance of further modification of this legislation and existing associations should be afforded an opportunity to present their views.

Therefore, we would hope that the Committee would include language in the bill that will improve the bill in the two respects we have suggested above.

Finally, we wish to refer to the one observation of the Business Advisory Panel which we consider significant. Export trade association legislation, whether existing or proposed in the bill under consideration, may not be everyone's cup of tea, but for those who utilize it, and for others who potentially could find it helpful, it is an important and immensely useful instrument of export trading in a world of foreign cartels and foreign government monopolies.

MEMBERS

OF THE

MOTION PICTURE EXPORT ASSOCIATION OF AMERICA, INC.

Allied Artists International Corporation

Avco Embassy Pictures Overseas Corporation

Buene Vista International, Inc.

Columbia Pictures International Corporation

Metro-Goldwyn-Mayer, Inc.

Paramount Pictures Corporation

Twentieth Century-Fox International Corporation

United Artists Corporation

Universal International Films, Inc.

Warner Bros. International, a division of Warner Bros., Inc.

NATIONAL CONSTRUCTORS ASSOCIATION

SUBMISSION FOR THE RECORD
SUBCOMMITTEE ON INTERNATIONAL FINANCE
COMMITTEE ON BANKING, HOUSING & URBAN AFFAIRS
UNITED STATES SENATE

September 20, 1979

FORMATION OF U.S. EXPORT TRADE ASSOCIATIONS

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

The National Constructors Association respectfully submits this statement on behalf of the nation's engineering and construction industry involved in overseas work.

The National Constructors Association is composed of fifty of the largest American firms engaged in international engineering and construction activities. Many of our members are involved in the export of technology and technical data in the form of engineering designs and construction plans for large-scale industrial facilities in such fields as power generation, oil refining, chemical processes, and steel production. Part of our work includes the specification and often the purchasing of machinery, apparatus, and equipment required for those facilities.

The National Constructors Association speaks on behalf of its members who are performing foreign work and who are, in many ways, the pathfinders for follow-on U.S. markets in developing countries. In many cases, NCA members are the first in those nations to develop an industrial infrastructure.

Engineering and construction projects overseas make up a significant proportion of total U.S. exports. In recent years we have accounted for between $15 and $18 billion in overseas contract work with additional sales of at least $4.5 billion in manufactured goods that supply our overseas projects. That makes us second only to the export of defense equipment in contributing to the U.S. trade balance.

This activity probably accounts for well over one million jobs in our domestic economy.

However, the share of U.S. exports is in sharp decline. The National Constructors Association estimates that between 1976 and 1978, the U.S. slipped from first to fourth place in world construction. Of $86 billion in Middle East construction awards between 1975 and 1978, only about 10% went to U.S. contractors. That is compared to 51% awarded to Western European firms and 27% to Far Eastern firms. These figures do not represent an isolated trend. They represent our experience in all major foreign markets.

The declining strength of the U.S. export industry could not come at a worse time. In 1971, the U.S. posted its first trade deficit in more than 50 years. The $2.2 billion deficit in 1971 was a warning of problems to come. In 1977 and again in 1978 the U.S. posted annual trade deficits averaging in excess of $30 billion. We are running at an even higher rate for 1979. Our cumulative trade deficit over a period of thirty-six consecutive months is $100 billion.

Although the U.S. engineering-construction industry can no longer claim to have the tremendous lead in advanced technologies that we once had, we still have, by some estimates, about 40% of the world's engineering and construction capacity. We should be in an excellent position to compete successfully in world markets. Our capabilities are as diversified and advanced as exist anywhere in the world. In short, on our own merits, we should be claiming a much larger share of world markets than we are. The markets are there. The interest is there.

Yet out competitive position continues to slip. And the reasons for it come down in large part to policies and regulations imposed on us by the U.S. government.

U. S. exporters face more federal controls, conditions, and restrictions than do companies of any other industrialized country in the world. At a time when other nations are encouraging their export industries through their financing, tax, and promotion policies, the United States is subjecting its exports to tighter regulation, scrutiny, and control. It should come as no surprise that nations such as Germany and Japan, with a much greater reliance on foreign energy imports than the U.S., are experiencing far less problems with trade and payment balances than we are. The relative strengths of their currencies can be considered in the comparison as well.

The President showed signs of recognizing the seriousness of this problem last September in his export policy statement. In calling for a reduction of domestic barriers to export, he mandated a "greater sensitivity to the importance

of exports" in administering federal laws and policies. This crucial and timely attitude toward international business implies a restructuring of national goals and priorities that not only reduces current domestic barriers to expanded U.S. trade but also promotes and encourages that trade.

Mr. Chairman, we recognize and deeply appreciate the work your subcommittee has performed during the course of hearings on the Export Administration Act. We have expressed our strong support for the goals and legislative initiatives outlined in the Subcommittee Report on U.S. Export Policy, and applaud your personal efforts on behalf of an equitable and rational U.S. government stance toward international business.

Our members agree that the solution must include changes in the availability of adequate export financing, changes in the irregular, unpredictable, and therefore restrictive export licensing process, changes in the often arbitrary withholding of exports as a foreign policy tool, changes in certain tax policies, and changes in the extraterritorial application of U.S. environmental standards.

All those changes and others we have not mentioned would recognize the new realities of the international marketplace. The reality is that exports and the ability to compete worldwide have become a primary goal and effort of the governments of our foreign competitors. That we as a nation are suffering because of our own government's refusal to recognize these new realities is clear in the trade figures that have been cited before this subcommittee time and time again.

One of the areas where we as an industry are failing to realize our potential abroad lies in the application of U.S. antitrust laws to U.S. engineering and

and construction firms in overseas markets. Those laws prohibit our firms from combining or pooling their resources on an ongoing basis to search out and bid large projects worldwide. The Webb-Pomerene amendment to the Export Trade Act of 1918 originally called attention to the problem by providing certain limited exemptions to the Sherman Antitrust Act for American firms engaging in export trade--provided that such action did not affect domestic trade or prices.

American industry has changed dramatically since then, and the past 60 years have seen the development of technologies and services undreamed of at the time Webb-Pomerene was enacted. Today's markets demand infrastructure and industrial capabilities far beyond the "goods, wares, and merchandise" covered by the Act. The magnitude and cost of providing services for the burgeoning markets of the oil-rich developing countries and lesser developed countries capable of obtaining international financing-institution backing preclude even the largest engineering and construction firms from attempting a "do-it-yourself" approach. The more reasonable approach would be joint venturing among those firms most qualified to form the "package" capable of performing the work needed by the client.

However, U.S. antitrust laws have not been amended to reflect this fact. As a result, industry uncertainty as to the law's application has forced American business to seek prior approval from the Justice Department before combining resources for international projects. Such advance clearance is costly in terms of resources, and effectively prohibits ongoing and follow-up ventures. The Act's exclusion of services, which have become a major part of U.S. export business, constitutes an additional barrier to joint international ventures.

At the same time, our competitors in these markets have formed consortia with explicit government approval and even government participation.

As examples of the above, we request the Committee to consider the following:

Korea: Perhaps the best overseas competitor in the engineering and construction field, Korea has established, with government help and supervision, the Korean Overseas Contractors Association (KOCA). KOCA is comprised of 122 affiliated companies actively soliciting overseas work. Out of the ranks of KOCA members has evolved the Korean Overseas Construction Corporation (KOCC) which is a private corporation formed by 36 top Korean contractors. The method of operation: KOCC will bid on larger, more complex (and, consequently, more costly) projects. Following award of the contract to KOCC, the Corporation assigns, or subcontracts, the work involved to one or more of its members, retaining 1% of the proceeds of the job to continue its marketing and foreign bidding activities.

Phillipines: A country who has learned much more from the Koreans than we have, the Government of the Phillipines has established the Filipino Contractors International Corporation which is charged with designating which of its 23 member companies will undertake a given job overseas. A June, 1977, proclamation by President Marcos, which opened the door for such an association, mentioned, among other things, the need to "avoid ruinous competition between (Filipino) contractors" for foreign markets.

Canada: The Canadian Government actively supports a quasi-government program known as Program for Export Market Development (PEMD). One of the five PEMD

components, PEMD E, helps firms compete in export markets through the formation of consortia.

Italy: Since the early 1970's, the Italian Instituto Nazionale per il Commercio Estero (ICE) has been encouraging joint export associations which allow private contractors to join together into associations in order to spread the costs of marketing and bidding foreign projects among several firms.

Netherlands: Following the May, 1977, elections in the Netherlands, the Minister of Economic Affairs proposed a series of initiatives to promote exports. One of the most highly discussed areas for support is the subject of "turn-key" projects overseas which incorporate Dutch banks, consultants and contractors.

Other examples of the same type of government-sponsored consortia approach to the bidding of large overseas projects abound. We will not bore the Committee with examples from Japan, Inc. or France, Inc., or any other of our major trading competitors. Suffice it to say that the worldwide acceptance of the need to compete in the international marketplace has been recognized by the governments of those nations with whom we are attempting to compete.

We urge the Committee to seriously consider the current state of our trade imbalance and accept the reasoning of the engineering and construction industry that competition for world markets does not exist in a vacuum. For our industry to contribute positively to the trade deficit, we must be able to meet the competition.

The National Constructors Association supports the value of a competitive, free enterprise system envisioned by existing antitrust legislation, and recognizes

the original intent of the Webb-Pomerene Act in providing certain exemptions to those provisions for international ventures. The nature of international competition has changed substantially since Webb-Pomerene's passage, however, and the full development of our export potential is essential if American business is to survive abroad. It is the NCA's position that in order to meet this competition, a mechanism allowing U.S. engineers and contractors to combine without threat of domestic antitrust action must be provided. This can be realized in part by clarification of Webb-Pomerene's antitrust implications and the expansion of provisions to specifically include technology-related items and services.

Such legislation, as part of a broad spectrum of government policy actions in support of expanded U.S. exports, can provide a basis whereby the United States can fully develop its tremendous export potential and reclaim the economic and social benefits that we as a national are capable of realizing.

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PACE

PACIFIC AGRICULTURAL COOPERATIVE FOR EXPORT, INC.

Mailing Address:
465 California Street, Suite 414
San Francisco, California 94104
Telephone: (415) 391-2370

September 11, 1979

Hon. Adlai Stevenson, Chairman
International Finance Subcommittee
Senate Banking Committee
Dirksen Senate Office Building, Room 5300
Washington, D.C. 20510

Dear Senator Stevenson,

Pacific Agricultural Cooperative for Export, Inc. wishes to file a statement regarding Senate Bill 864, and has duly received permission to file from Committee Counsel Robert W. Russell, Esquire.

STATEMENT:

Pacific Agricultural Cooperative for Export, Inc. (PACE) is a California cooperative corporation registered with the Federal Trade Commission and qualified as a Webb-Pomerene Association under the Webb-Pomerene Law (sections 61-65 of Title 15 of the United States Code). PACE was established in 1972.

The goal of PACE is to assist and promote the export of the raw or processed agricultural, food, or other products of its members; all PACE activities are directed to this goal.

PACE has been successful in achieving its goals primarily due to its ability to operate as a Webb-Pomerene Association.

Pacific Agricultural Cooperative for Export, Inc. generally supports S. 864 for the following reasons:

1. It promotes the export trade of the United States which is vital to our economy.

2. The bill enlarges the scope of Webb-Pomerene to include additional activities permitting United States companies to compete with foreign competitors in foreign markets.

3. The bill tends to clarify the requirements for Webb-Pomerene Association qualification.

4. S.864 encourages the establishment of an increased number of Webb-Pomerene Associations.

We would appreciate your keeping us informed as to the progress and any modifications of S.864.

Thank you.

Sincerely yours,

J. Murray Fox

J. Murray Fox
Executive Secretary

JMF/lsa
cc: All PACE Members

October 4, 1979

Phosphate Rock Export Association

STATEMENT ON EXPORT TRADE EXPANSION BY THE
PHOSPHATE ROCK EXPORT ASSOCIATION BEFORE
THE SENATE SUBCOMMITTEE ON INTERNATIONAL FINANCE

I. INTRODUCTION

The Phosphate Rock Export Association ("Phosrock") welcomes this opportunity to comment on legislation designed to expand United States export trade. Chairman Stevenson and the Subcommittee are to be commended for recognizing the continuing need to confront the questions how to stimulate United States export trade; what to do about this country's persistent trade deficit; and how to improve the export competitiveness of United States business.

Inquiry into these subjects inevitably involves an assessment of the Export Trade Act of 1918 (commonly known as the Webb-Pomerene Act) and elicits expressions of polar views concerning the effectiveness, wisdom and, indeed, morality of affording a qualified antitrust exemption to American companies doing business abroad. Those seeking repeal of the Webb-Pomerene Act, deeming it to unnecessarily offend notions of antitrust, square off against those desiring to revamp the Act to make it better suited to produce its intended results of fostering and protecting American export trade.

As an Association that has operated under the aegis of the Webb-Pomerene Act for nine years while pursuing foreign markets for phosphate rock on behalf of its member companies, Phosrock strongly supports the continued validity of the Act's

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purpose. Furthermore, Phosrock believes that its activities exemplify the salutary functions that can be performed by Webb associations as an invaluable aid to American companies that compete in foreign markets.

Notwithstanding the fact that it has operated quite successfully as a Webb-Pomerene association, Phosrock recognizes that new legislative action could have the virtues of resolving some long-standing uncertainties under the Act and of signaling congressional disapproval of the anti-Act bias at times exhibited by enforcement officials. Phosrock urges, however, that any new articulation of United States export expansion policy or any efforts to supersede provisions of the Webb-Pomerene Act must provide a degree of flexibility necessary to treat the great variety of circumstances faced by American companies as they undertake to increase their export activities.

The following considerations strongly indicate that legislation at least consistent with the spirit of the Webb-Pomerene Act should be forthcoming:

- the American dollar sorely needs the strong support that favorable balance of payments can bring;

- the American economy needs the positive boost in jobs that increased exportation will produce;

- American exporters increasingly confront strong competition from foreign entities that are government-owned or subsidized; and

- American exporters often are distinctly handicapped when dealing with many customers in the export market who enjoy the strong support of or participation with their governments.

Opportunities for America to increase its export trade are well at hand. New markets like the People's Republic of China offer great potential but will require persistent and diligent efforts. Moreover, all United States firms need the strong and effective support of their government if the goal of increased exportation is to be achieved.

II. THE WEBB-POMERENE ACT

Passed in 1918, the Webb-Pomerene Act 1/ provides a limited exemption from the antitrust laws 2/ for acts done by and through "associations" engaged solely in "export trade." 3/

1/ 15 U.S.C. §§ 61-66.

2/ Section 2 of the Act (15 U.S.C. 62) removes prescribed export activities from application of the Sherman Act. However, Section 4 of the Act (15 U.S.C. 64) provides specifically that the Federal Trade Commission Act's prohibition against "Unfair Methods of Competition" shall apply to export trade.

3/ The Act defines "export trade" as:

> solely trade or commerce in goods, wares, or merchandise exported, or in the course of being exported from the United States or any territory thereof to any foreign nation

but not including

> the production, manufacture, or selling for consumption or resale, within the United States or any territory thereof of such goods, wares, or merchandise, or any act in the course of such production, manufacture, or selling for consumption or for resale

The statutory exemption for certain joint export trade activities was recommended by the Federal Trade Commission (FTC) in order to permit United States companies to compete against foreign cartels and deal effectively with government-owned, controlled or supported foreign customers. The underlying FTC report, based on an extensive two-year study, had concluded that:

> In seeking business abroad, American producers must meet aggressive competition from powerful foreign combinations. . . . In various markets American manufacturers and producers must deal with highly effective combinations of foreign buyers. . . . These combinations naturally make individual American producers bid against each other. . . . If Americans are to enter markets of the world on more equal terms with their organized competitors and their organized customers, and if small American producers and manufacurers are to engage in export trade on profitable terms, they must be free to unite their efforts. 4/

The keynote of the Webb-Pomerene Act lay in its permitting a cooperative effort by American competitors in the pursuit of their common goal of winning foreign customers from foreign rivals. Congress recognized the advantages of united activity that could reduce the costs of exportation, increase the export market shares of American firms, and -- if the joint activity should result in higher returns from foreign sales -- foster the health of the American economy.

4/ FTC Report on Cooperation in American Export Trade (1915).

While the Act provides that the activities immune from the Sherman Act must relate solely to export trade, without any artificial or intentional effects on domestic markets or on the export trade of domestic competitors 5/, it does not set out requirements or standards for, or limits on, the structure or operating procedures of Webb-Pomerene associations. The principal agency charged with enforcement of the Act, the FTC, has said in this regard that "the test of legality lies in result in most instances rather than in the form or method pursued." 6/

5/ Section 2 of the Act (15 U.S.C. 62) provides that nothing in the Sherman Act

> shall be construed as declaring to be illegal an association entered into for the sole purpose of engaging in export trade and actually engaged solely in such export trade, or an agreement made or act done in the course of export trade by such association, provided such association, agreement, or act is not in restraint of trade within the United States, and is not in restraint of the export trade of any domestic competitor of such association; and provided further, that such association does not, either in the United States or elsewhere, enter into any agreement, understanding, or conspiracy, or do any act which artificially or intentionally enhances or depresses prices within the United States of commodities of the class exported by such association, or which substantially lessens competition within the United States or otherwise restraints trade therein.

6/ See Report, Webb-Pomerene Associations: A 50-Year Review (1968).

The result-oriented approach toward a definition of permissible joint conduct does not provide the degree of certainty that would be preferable for the ordering of commercial affairs. This aspect of the Act, coupled with apparent hostility toward it on the part of the antitrust enforcement agencies, has tended to discourage use of Webb-Pomerene associations by American companies. Nevertheless, uncertainties over the scope of the Act's exemption and concern that creating or joining an association might give rise to legal complications should not overshadow the important cost savings and valuable marketing information that can be gained through a properly organized and operated association.

Phosrock's members have benefited from their ability to pool resources and share risks. Lower distribution costs, the ability to respond to unforeseen market opportunities, prompt collection of accounts receivable and penetration of new markets are all results of Phosrock's activities. Phosrock's customers have benefited from having a reasonable and reliable supplier. Having various suppliers that mine different grades of phosphate rock and being able to use a number of shipping facilities, the Association is equipped to meet customer needs in a flexible and reliable manner. The record demonstrates that this Webb-Pomerene association has been a valuable competitive tool in selling phosphate rock in various world markets. Phosrock believes that a broader utilization by American business of Webb-Pomerene associations could significantly expand United States export trade.

III. PHOSPHATE ROCK EXPORT ASSOCIATION

Phosrock was formed in 1970 when it registered with the United States Federal Trade Commission as required by Section 5 of the Webb-Pomerene Act. 7/ It is a Delaware non-stock corporation. Phosrock's articles of incorporation, by-laws and membership agreement are on file at the Federal Trade Commission. The members of Phosrock are:

Agrico Chemical Company
American Cyanamid Company
International Minerals & Chemical Corporation
Occidental Chemical Company
W. R. Grace & Co.

Membership in Phosrock is open to any person, firm or corporation engaged in the United States in mining phosphate rock. 8/

After an initial interim period of establishment of policies, location of offices and procurement of staff. Phosrock became a full-functioning association in 1972. Its purpose was and is to expand export trade and commerce in phosphate rock by assisting the phosphate rock export activities of its members. The utilization of Webb-Pomerene associations by United States sellers of mined products was one of the specific

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7/ 15 U.S.C. 65.

8/ Major phosphate rock miners in the United States include: Agrico Chemical Co., American Cyanamid Co., Beker Industries, Borden Chemical Co., Farmland Industries, Gardinier, W. R. Grace & Co., International Minerals & Chemical Corp., Kerr-McGee, Mobil, Occidental Chemical, Simplot Co., Swift & Co., Texasgulf and U.S.S. Agrichemicals. Many other companies have substantial reserves. In addition, many smaller concerns have always been a factor in the market, particularly during periods of increased demand when entry seems attractive.

objectives in the enactment of the Webb-Pomerene Act. 9/ The FTC report which formed the basis of the Webb-Pomerene legislation summarized the bill's purposes and rationale when it stated that cooperation among domestic producers is imperative:

> To avoid needless expense in distribution, to meet formidable foreign buying organizations, to insure reasonable export prices and to prevent the profitless exhaustion of our national resources 10/

Phosrock is engaged in all aspects of export sales activity in phosphate rock as a non-exclusive agent of its members. Its responsibilities include market research and analysis, technical assistance, solicitation, negotiation and conclusion of export sales contracts, traffic coordination, invoicing, order processing, and collection and distribution of the proceeds of sale. Phosrock is headquartered in Tampa, Florida and has representative offices in Paris, France; Sao Paulo, Brazil and Tokyo, Japan.

The Association is engaged solely in "export trade." The certificate of incorporation of the Association states that Phosrock:

9/ Virtually every major industrial nation, and European Economic Community itself, encourages or permits the establishment and operation of export associations under exemptions from their respective antitrust laws similar to the Webb-Pomerene Act. The Treaty of Rome which establishes Common Market competition policy contains no explicit "foreign commerce" element like the Sherman Act but rather regulates only trade between member states. It has been specifically held not to apply to concerted action directed outside the Common Market. See Export Cartels (OECD 1974). Moreover, the Philippines and Brazil have each discussed the establishment, respectively, of coconut oil and coffee export sales cartels.

10/ (Underscoring added.) 55 Cong. Rec. 3577.

> shall engage solely in export trade, as the term "export trade" is defined in the Act of Congress entitled "an Act to promote export trade, and for other purposes," approved April 10, 1918, commonly known as the "Webb-Pomerene Act," and any Acts amendatory thereof or supplementary thereto, and such export trade shall be solely trade and commerce in phosphate rock which is for export or is to be exported or is in the course of being exported from the United States to any foreign nation.

The Association makes no sales for U.S. domestic consumption and/or use nor has any involvement in or takes any other action in U.S. domestic commerce. As such, Phosrock has nothing to do with the determination of the price of phosphate rock sold for consumption and/or use in the United States.

Moreover, Phosrock does not control the amount of phosphate rock available for export, for sale in the U.S., or even the amount to be exported by its Members. Under the Association's Membership Agreement, each Member, acting individually, determines the amount of phosphate rock which it wishes to sell each year through the Association (as that Member's agent). Each Member, in addition, retains the unfettered right to sell phosphate rock on terms and conditions which the Member individually determines, to any U.S. domestic person for whatever purpose, including exportation. 11/ Finally, Phosrock has no involvement

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11/ In addition, subject to availability and mutual agreement on terms and conditions, Phosrock will sell and has sold phosphate rock to U.S. domestic persons for exportation.

in export sales by a Member company to any affiliated company abroad. 12/

Phosphate rock is a mined raw material used in various phosphorus derivative industries, particularly in the manufacture of complex phosphatic fertilizers. Generally speaking, it is a fungible commodity the principal varient being the content or extent of the fertilizing element (P205). Various grades of phosphate rock contain differing concentrations of this element and, in the industry, have been differentiated by references to the percentage of the P205 content or the BPL units (bone phosphate of lime or tricalcium phosphate). 13/ Known phosphate rock deposits are scattered throughout the world, but are principally located in Morocco, Algeria, Tunisia, Spanish Sahara, Jordan, Israel, Togo, Senegal, South Africa, certain South Pacific islands, the Soviet Union and the United States. World phosphate resources (from all locations) total roughly 67,000 million metric tons. 14/

Major resource areas (million metric tons) are as follows:

12/ The term "affiliated company" is defined in Phosrock's Membership Agreement to be a corporation in which a member has a 20% ownership interest.

13/ See, generally, Fertilizer Technology and Use (2d ed. 1971).

14/ "Phosphate" Mineral Commodity Profiles 3 (1979 ed. U.S. Dept. of Interior); see, generally, Phosphate Rock and Fertilizers In the World (OECD 1972).

Location	Reserves	Total Resources
Morocco	18,000	40,000
United States	2,200	8,000
South Africa	3,000	7,000
U.S.S.R.	1,400	3,400
Western Sahara	400	1,600
Australia		2,000

Of course, Morocco has access to certain Spanish Sahara resources which can only serve to increase its dominant position in the world market.

Virtually all phosphate rock miners in the world, besides those operating in the United States, are government owned or controlled. Included in this number are:

Morocco
Algeria
Egypt
Senegal
Tunisia
Jordan
Israel
Syria
China
Vietnam
Australia
Ocean Islands
U.S.S.R.
Brazil
Mexico

Naturally, all have the strong political and financial support of these governments. 15/ Morocco, for example, derives over one-third of its gross national product from the export sale of phosphate rock.

15/ See, Walters & Monseu, "State-owned Business Abroad: New Competitive Threat," Harvard Business Review, March-April 1979, p. 160.

Further, many actual and potential customers of Phosrock are foreign governments or companies that are totally or substantially owned or controlled by their governments. Included in this number are customers in the following countries:

Australia	Bangladesh
Indonesia	Philippines
China	Taiwan
Portugal	Mexico
Romania	Austria
Czechoslovakia	Poland
Bulgaria	France (certain customers)
Venezuela	Italy
Pakistan	Brazil (certain customers)
India	Colombia
Sri Lanka	Costa Rica
Korea	Ecuador
El Salvador	Finland

The potential problems of dealing with these foreign sovereigns are many. For example, India several years ago advised its American suppliers, who did not belong to a Webb-Pomerene association for that product, that it would not honor any of the contracts India had executed with the American firms and would not accept any shipments of product until the suppliers released this customer from its contracts and lowered their price to a figure stipulated by the customer. Because the American firms could not take joint action to prevent such pressure tactics, India was able to pit one supplier against the other until it managed to get one supplier to go along. Once the resistance was broken, all the remaining American firms fell into line in order to avoid losing substantial tonnage. However, millions of dollars of export revenue were lost as well.

Finally, even when an export customer is privately owned, it may, like in Japan, have a long-standing relationship

of support and cooperation with its government. Moreover, the government may use its often considerable leverage to influence selection of a phosphate rock supplier in order to foster some other national interest. France, for example, has repeatedly urged the few remaining privately-owned French fertilizer companies to favor Morocco as a supplier in order to attempt to satisfy certain bilateral commitments between those two countries.

Clearly, situations of this kind reflect the important advantages to be gained for American industry through the use of Webb-Pomerene associations. The promising market emerging in Asia, now that China has abandoned its isolationist policies, provides a graphic illustration of the benefits such joint action can provide.

IV. THE CHINA CHALLENGE

Formerly committed to economic independence, China's leadership has lately recognized that its modernization and industrialization goals will require a major infusion of foreign resources, equipment and technology. China, thus, is seeking business arrangements to expand its foreign trade and commerce. China's dramatic swing toward intercourse with the West has been met with interest and enthusiasm from businesses and traders throughout the rest of the world. China's population and territorial size and largely undeveloped and unmechanized status

make modernization an immense task. 16/ The role to be played by traders of the developed world is also awesome; questions of how to enter and develop the China market are without easy answers.

The challenges presented to companies desirous of trading with China provide an excellent illustration of the current importance of enabling American business to resort to joint export activity that is not only condoned but encouraged by a positive United States export policy. A major characteristic of a Webb-Pomerene association is that it facilitates the legitimate sharing of expenses, risks and resources by companies otherwise less capable or less likely to enter a market because of its complexity or cost. China's more than 800 million people, the problems of not only feeding but finding work for this immense population, the needs created by China's determination to move swiftly from an agrarian economy with a predominantly manual labor force to an industrialized and mechanized state, and the virtual absence of a system of law that corresponds to Western precedent all make China a complex market that will require substantial start-up costs.

In short, current trade opportunities for overseas contracts with China present alluring prospects, yet all the competitive problems associated with export activities are

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16/ One commentator has written that "China's economic realties include an agricultural sector so backward that it employs 70 percent of the labor force and 'modern' industries that are 10 to 30 years out of date." Louis Kaar, "China's Narrow Door to the West," Fortune, p. 63, March 26, 1979.

exacerbated in the situation presented by this "new frontier" for American exporters. The advantages for American companies in banding together for joint exportation may prove particularly valuable in this context.

The course of developing trade with China may involve uncertainties and difficulties resulting from China's political history and her pronounced cultural differences from the United States as well as unique commercial challenges presented by a potential customer of this character and power. These problems could be somewhat alleviated for American exporters if firms engaging in the same line of business could form selling organizations together and share the costs and risks of creating and serving markets in China.

Although there is no doubt that China's leadership today is fully committed to modernizing the country as quickly as possible, 17/ China's political history engenders a degree of uncertainty as to whether and for how long this present course will continue. In a recent survey of China, Financial Times reporter David Housego remarked that

> China's record since independence bodes ill for continuing stability in the future. There is probably no other sizeable nation in the world that has seen such upheavals in the last 30 years. 18/

17/ At the fifth People's National Congress held in February 1978, Chairman Hua Guofeng announced officially the concept of the "four modernizations," which calls for rapid modernization of industry, agriculture, national defense, and science and technology to accelerate the growth of the national economy.

18/ "Welcome Partner in the World," China Survey, Financial Times, p. 1, Aug. 20, 1979.

Vice Premier Deng Xiaoping, apparently the main force behind China's decision to embrace the international community and seek recognition as a world power, has been only recently returned to power after a fluctuating political career. Deng is said to have formed an uneasy alliance with his long-standing rival, Chairman Hua Guofeng, who himself acceded to power in 1976. The radicals who prevailed during the Cultural Revolution and supported the "Gang of Four" have been politically defeated, but continue to hold positions in both the Chinese government and the Chinese Communist Party. These forces oppose Deng's pragmatic policies and the economic and legal reforms he has spearheaded. For nearly 20 years prior to the demise of the Gang of Four in 1976, a formal system of laws was considered to be undesirable as unduly confining of the government.

China's lack of a legal structure that corresponds to the complex legal system familiar to Americans creates further uncertainty for American exporters. Although after the creation of the People's Republic of China in 1949, China experimented briefly with a system of laws styled after the Soviets', negotiation and reconciliation have long been the essential tools for dispute resolution in that country. 19/ The Chinese have a traditional distrust of law and litigation and prefer to rely upon principles of mutual trust and mutual benefit. 20/

19/ "Trade and Tariff Legislation," China Trade, 23 (Spring 1979).

20/. According to an ancient Chinese fable, law was the creation of barbarians; civilized people should be governed by moral precepts rather than externally promulgated rules that unworthy people can twist or evade. This attitude may be slowly changing. See Conner, "China Revamps Economic Policy," The National Law Journal p. 20, Aug. 27, 1979.

A prominent Chinese lawyer has emphasized China's concern to preserve its sovereignty and legal tradition while making those concessions required to encourage increased dealings with Western businesspeople. 21/ She has sought to allay the fears of foreign businesses that they may be treated unfairly if China imposes its own customs by explaining:

> They fail to realize that the people in China are seriously attempting to apply the principle of equality and mutual benefit. They are very idealistic people. Many of them are first generation revolutionaries who have devoted their whole lives to the cause of revolution. They want to uphold certain principles. And one of these is the principle of equality and mutual benefit in dealing with foreign friends. 22/

China's leadership has recognized, nonetheless, that a new system of law will be essential to inspire the confidence of foreign businesspeople necessary for facilitating China's economic development. China is hurriedly drafting new legislation to define the legal relationships arising from economic cooperation by foreign traders and investors. 23/ A new law

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21/ Ms. Liu Yiu-Chu, who was interviewed by China Trader, n.18 supra, is a senior partner in the firm Liu, Chau and Lam with an excellent reputation among Western companies as a consultant on Chinese trade.

22/ China Trader, n.18 supra, at 35.

23/ China Trader, n.18 supra, reports that:

> The new laws will be the first commercial laws codified in China since the founding of the People's Republic

(Footnote continued on next page)

on joint ventures adopted by the National People's Congress on July 1, 1979 provides for government protection of foreign enterprises, investment and profit obtained by agreements approved by the Chinese government. 24/ Other laws governing commercial transactions are expected to cover buying and selling contracts, foreign investment and compensation trade, taxation, and a system of tariffs. Although the Chinese have a trademark law, there is at present no legislative protection for patents, copyrights or other industrial property rights. 25/ Moreover, an officer of an international insurance company, the American International Group (AIG), whose relations with China

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23/ (Cont'd from previous page)

close to 30 years ago. Regulations now in effect in the country are based on commercial law in effect before 1949 which has since become custom and on the principle of equality and mutual benefit.

According to Ms. Liu they will reflect China's legal tradition and will take into account latest western practices. She says that any suggestion that China is going to import western law or any mention of the westernization of China's law was suspect.

24/ "Trade Agreement Facilitates Joint Ventures", The Legal Times, p. 12, August 6, 1979.

25/ A China-U.S. trade agreement formally executed on July 7, 1979 requires China to provide patent protection at least equal to that found in the Paris Convention for Protection of Industrial Property and copyright protection not less than that provided in the Universal Copyright Convention.

date from 1975, has observed:

> . . . even if new laws are drafted, foreigners seeking to do business in China should probably expect to have to rely principally on the terms of their contract, the result of perhaps very long negotiations, to define and to clarify the expectation of both sides. AIG has had too much experience in the Far East, in China and elsewhere, for us to believe that the faith which Americans often profess to place in the rule of law will be replicated in the Orient. 26/

In a related vein, uncertainties for American companies wishing to do business with China flow from the vastly different premises of our societies. It will be difficult to translate knowledge of the Chinese mentality -- its apparent stoicism, its notions that profit and success are undesirable that seem to be the cause for extremely low productivity -- into effective marketing strategies. It is clear that market penetration and development will require a long and patient effort that could, in the end, yield very little. Sharing the risks of such an undertaking has obvious merit. Due to the closed nature of Chinese society, a supplier cannot simply enter the market to respond to the demand it perceives. It must rely, to some extent, on very imprecise information.

The emphasis placed by the Chinese upon building business relationships on the basis of mutual trust, together with the lack of a fabric of concrete rules for contract inter-

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26/ M.R. Greenberg, "How to Pierce the Bamboo Curtain," The National Law Journal, p. 30, May 21, 1979.

pretation and enforcement, thrusts especially great importance upon the process of reaching agreement with the Chinese purchaser. According to conventional wisdom, it is almost impossible for a potential exporter to sell in China without an official invitation to do so. 27/ Securing such an invitation is a lengthy process for large and small firms alike. Initial contact is usually achieved by submitting a carefully detailed proposal to the specific Chinese trading corporation charged with responsibility for the commodity in question. 28/ A casual inquiry respecting Chinese requirements or needs is not feasible. The American exporter must make a concrete proposal, one that would be well served by an accompanying suggestion for a technical exchange and provision for commitment of time by technical experts. Obviously, such a serious and full-scale commitment merely to gain the attention of potential purchasers entails high start-up costs.

China's vast territory and the undeveloped state of its transportation facilities and hotel accommodations assure the fact that shipping and distribution efforts will be expensive. 29/ Another less obvious but expensive aspect of export trade with

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27/ Id.; see also Doing Business with China 6 (ed. U.S. Dept. of Commerce 1979).

28/ A discussion of the fact that in China all foreign trade is in the exclusive domain of the Government follows at p. 22.

29/ As of five years ago, only about three quarters of China's communes could be reached by motor vehicle.

China is proving to be the length of time required to ultimately come to terms with Chinese purchasers. Nailing down a major contract can consume several months of tenacious bargaining. 30/ The Chinese tend to deal with American and other foreign exporters from a position of strength since the Government makes all purchases on behalf of Chinese end-users. Observers have noted that the Chinese are masterful at playing countries against each other to obtain the best deals. 31/

China's bargaining strength, derived from the fact that the Government is the single buyer in the market, may be somewhat counterbalanced if American firms can band together to present a united front as sellers. For example, the Chinese tend to rely upon a very short standard contract for all transactions involving small values or standard products. 32/ Chinese purchasing officials can and should be pressed into amending these sketchy contracts due to the fact that the Chinese apply strict constructionist tenets in the interpretation of written agreements. Exporters who jointly present a proposal for the sale of a substantial quantity of goods or services have far greater leverage for seeking revisions of the standard Chinese contract than exporters who bargain individually.

30/ Doing Business With China 6 (ed. U.S. Dept. of Commerce 1979).

31/ Id. at 13. See also "China's Narrow Door to the West," Fortune p. 63, March 26, 1979.

32/ Doing Business with China, n. 30 supra, at 13.

As has been implied, the amount of time and effort necessary to close an agreement with the Chinese is attributable not only to the tough and refined negotiating techniques of the Chinese but also to the fact that China's foreign trade is conducted as a government monopoly by the Ministry of Foreign Trade. The State is always the customer, regardless of the identity of the actual end-user.

Operations of the Ministry of Foreign Trade are conducted through a network of state trading corporations. Phosphate rock and other fertilizer material, for example, are purchased by the China National Chemicals Import and Export Corporation (Sinochem). Although the foreign trading corporations make the ultimate purchasing decisions on behalf of Chinese end-users, these decisions are dictated in turn by the relatively inflexible (and largely unpublicized) requirements of China's planned economy. 33/

Although the trading corporations are the entities charged with the formal decision-making in the Chinese bureaucracy, many other bureaucratic units may become involved in the process. For example, Phosrock officials conducted extended discussions with Sinochem earlier this year on a visit to China designed to promote U.S. phosphate rock. Two sessions were

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33/ In addition to China's Five- and Ten-Year Plans that set forth general goals, China's annual economic plan sets more specific targets and production levels. Domestic resources are always exhausted first before seeking foreign supplies. See Doing Business With China, supra n. 30, at 2.

scheduled per day, six days a week. In addition to the Sinochem officials, representatives attended from a number of other organizations including the China National Chemical Construction Corporation, the All China Chemicals Association, the Chinese Project Institute of Chemical Industry, the Ministry of Agriculture, the Chinese Academy of Agri-Science, the All China Federation of Supply and Marketing Cooperatives, the China National Institute of Agricultural Science and the China National Technical Import Corporation. It was particularly beneficial to be able to draw on the shared resources and expertise of Phosrock's members to respond to the plethora of detailed questions asked and interests represented at these meetings.

The chief effect of the complicated bureaucracy in China that interposes a state corporation between producers and Chinese end-users is that American exporters are once removed from accurate information on market characteristics or demand. This makes the process of selling in the China market more complex than sales to private corporations.

Moreover, American firms will have to confront foreign policy considerations in dealing with the Chinese government. Although American relations with China were only normalized this year, other countries have conducted business with China for generations. The fact that China's Third World relationships may prove important to her purchasing decisions is of particular

concern to Phosrock since many of its competitors are governments from so-called developing countries. During Phosrock's recent discussions with Sinochem, Chinese officials indicated that China had been importing phosphate rock from Morocco, Jordan, Syria and Algeria. These officials emphasized that China, in her dealings with the United States, desires to make new friends but also to honor its old.

All of these factors suggest the benefits to be gained from sharing the risks of uncertainty concerning how the Chinese will behave next, how agreements will be interpreted and how customer needs can be developed. These are all risks that might well be unacceptably high to each exporter acting independently. Further, firms in the same line of business can share facilities; pool their expertise and rely upon joint advertising, marketing, and distribution to reduce their overhead. Finally, concerted action will further enable American companies to bid for orders at a single price put forward by a single negotiating team, thereby frustrating the Chinese tendency to divide and conquer.

V. CONCLUSION

The foregoing discussion outlines Phosrock's experiences and the benefits it derives from present law and summarizes the important and continuing American interests which the Webb-Pomerene Act promotes. Based on the view that a properly organized and operated association can make a positive contribution to expansion of American export trade, Phosrock strongly urges that the Subcommittee reject legislative proposals which could diminish the utility of the Act.

Nevertheless, there are several issues that require prompt legislative attention. Since passage of the Act, there have been few decisions or proceedings construing its rather general provisions. 34/ These cases treated a variety of issues

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34/ United States v. Concentrated Phosphate Export Association, 393 U.S. 199 (1968), rev.'g 273 F. Supp. 263 (S.D. N.Y. 1967): on remand 1979 Trade Cas ¶ 72,719 (S.D.N.Y. 1969); United States v. United States Alkali Export Association, 325 U.S. 196 (1945) aff'g. 58 F. Supp. 785 (S.D.N.Y. 1944 on remand 86 F. Supp. 59 (S.D.N.Y. 1979); United States v. Anthracite Export Association, 1970 Trade Cas ¶ 73,348 (M.D. Pa. 1970); United States v. California Rice Exporters, Cr. 32879 (N.D. Cal. 1952); United States v. Minnesota Mining & Manufacturing Corp., 92 F. Supp. 947 (D. Mass. 1950); United States v. Electrical Apparatus Export Association, 1946-47 Trade Cas ¶ 57,546 (S.D.N.Y. 1947); Carbon Black Export, Inc. 46 F.T.C. 1245 (1949); General Milk Co., 44 F.T.C. 1355 (1947); Sulfur Export Corp., 43 F.T.C. 820 (1947); Export Screw Ass'n, 43 F.T.C. 980 (1947); Phosphate Export Ass'n, 42 F.T.C. 555 (1946); Flordia Hard Rock Phosphate Export Ass'n, 42 F.T.C. 843 (1945); Pacific Forest Industries, 40 F.T.C. 843 (1940). See Larson, "An Economic Analysis of the Webb-Pomerene Act," 13 J.L. & Econ. 461 (1970); Simmons, "Webb-Pomerene Act and Antitrust Policy," 1963 Wis. L. Rev. 426 (1963); Note, "The Webb-Pomerene Act: Some New Developments in a Quiescent History," 37 Geo. Wash. L. Rev. 341 (1968); see also Brewster, Antitrust and American Business Abroad (1958); Fugate, Foreign Commerce and the Antitrust Laws (2d ed. 1973); Diamond, "The Webb-Pomerene Act and Export Trade Associations," 44 Colum. L. Rev. 805 (1944); Comment, "Export Combinations and the Antitrust Laws: The Delemma of the Webb-Pomerene Act," 17 U. Chi. L. Rev. 654 (1950).

including international cartel agreements, domestic price-fixing, restraints on members' exports and use of foreign factories, effects on import trade, limitations on barters and exchanges and exclusion of services from the Act's immunity. Although these decisions help to define the scope of the limited immunity provided by the Act, the absence of clear-cut and definitive statements of permissible joint conduct coupled with the continued hostility of the Department of Justice have had a negative effect on utilization of the Act by American firms. 35/ The reluctance to risk legal problems has been recognized repeatedly as a major cause for the relatively small number of Webb-Pomerene associations. Assistant Secretary of Commerce Frank A. Weil recently testified:

> We think that the fundamental problem, one of the fundamental problems faced today in world trade relates to the fact that many American businesses -- rightly or wrongly -- perceive a threat from the U.S. government in the form of the Justice Department for their activities overseas in getting together to compete with the consortia that they find in competition abroad.
>
> And perhaps the simplest way to put it is that we in the Department of Commerce are not suggesting for one instant a relaxation of our commitment to firm principles of competion and antitrust law. On the other hand, we think that it is possible for the U.S. government to send a more positive signal in terms of those things which are

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35/ The Department of Justice has repeatedly urged repeal of the Act. See, e.g. Shenefield, Antitrust and Trade Regulations Report (BNA) No. 875, AA-3 (August 3, 1978); Turner, Internationl Aspects of Antitrust, Hearings before the Subcommittee on Antitrust and Monopoly of the Senate Judiciary Committee, 90th Cong., 1st Sess. 124(1967).

> permissible to the business community so as to encourage them to take permissible actions as they compete in the world. 36/

Secretary of Commerce John Conners said more than 10 years earlier that "uncertainty about the exemption provided is a deterrent and companies are fearful that joining an association may give rise to legal problems." 37/ The General Accounting Office and the Federal Trade Commission have reached the same conclusion. 38/ As the GAO said in 1973:

> it seems desirable to create a more favorable climate for increased exports while recognizing that care must be exercised to minimize their possibly adverse impact in the domestic marketplace . . .[W]e believe the critical U.S. export situation demands a positive approach -- encouraging the formation and operation of Webb-Pomerene associations -- so that the full potential of the Webb-Pomerene Act in promoting exports can be realized . . . Because of uncertainty over possible antitrust implications, clarifying the provisions of the Webb-Pomerene Act would help create an environment in which U.S. firms might more readily join together...39/

36/ Weil, Hearing before the President's Commission on Reform of the Antitrust Laws and Procedures, July 27, 1978 at p.89-90.

37/ See McQuade, International Aspects of Antitrust, Hearings before the Subcommittee on Antitrust & Monopoly of the Senate Judiciary Committee, 90th Cong., 1st Sess. 179 (1967).

38/ General Accounting Office, "Clarifying Webb-Pomerene Act Needed To Help Increase U.S. Exports," Report to the Congress (1973); Kirkpatrick, Export Expansion Act of 1971 Hearing before the Subcommittee on Antitrust & Monopoly of the Senate Judiciary Committee, 92nd Cong. 2d Sess. 244 (1972).

39/ General Accounting Office Report, n. 38 supra at 16-18. The continued existence of this uncertainty is demonstrated by comparison of the testimony given by the Antitrust Division and the Federal Trade Commission at the hearings before

(Footnote continued on next page)

These uncertainties and the anti-Webb-Pomerene Act bias of the Department of Justice must be resolved if export associations are

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(Footnote 39 continued)

this Subcommittee on September 18 and 19. The Antitrust Division said:

> The significance of the Webb Act obviously is closely related to the issue of the antitrust legality of joint exporting activities. Our position is one which we have held and disseminated for many years, and I want to emphasize it strongly. In general, American businesses do not require antitrust exemption or clearance to engage in joint exporting ventures or any other joint activity the sole purpose of which is to sell goods or services for consumption abroad.
>
> A myriad of normal joint export activities can be and are constantly being carried on by groups of American companies without fear of antitrust prosecution. To be actionable, joint activity must have a substantial and foreseeable effect on United States domestic or foreign commerce. Joint activity intended to impact outside the territory of the U.S. and carried on so as not to affect competition between the parties in the United States is unlikely to raise any question under American antitrust law. Accordingly, it has been the consistent position of the Department of Justice that the antitrust exemption found in the Webb-Pomerene Act of 1918 is unnecessary to provide protection for export trade associations since the normal activities undertaken by such associations have as their exclusive focus markets abroad.

On the other hand, the FTC testified:

> The Export Trade Act, also known as the Webb-Pomerene Act, was adopted in 1918 during a period of resurgent interest in foreign trade. The basic purpose of the Act is to increase exports by granting antitrust immunity to domestic competititors for joint

(Footnote continued on next page)

going to realize the potential Congress intended when it passed the Export Trade Act in 1918.

The suggestion that business advisory procedures be substituted for the Webb-Pomerene Act is a clear step backward with respect to realization of these goals. The adoption of a more liberal policy for providing antitrust guidance through business advisory opinions might be feasible in certain situations such as a one-time joint venture to construct a power plant or license patents and/or technology. This procedure, however, is not a practical or sensible way to motivate effective exportation or to handle the myriad of legal and business problems that arise from joint selling on a long-term basis. A pattern of continuing selling is a prerequisite to the development of foreign markets of any real significance. 40/

There is no legitimate basis to conclude that a liberalized business review program would be utilized by potential exporters. Rightly or wrongly, many in American business perceive the Antitrust Divison as an adversary. The Department

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(Footnote 39 continued)

> activities in export trade that might otherwise be illegal. For example, the Webb-Pomerene Act allows firms that are competitors in domestic markets to jointly fix export prices and allocate foreign markets -- activities that could in some circumstances violate the antitrust laws in the absence of an exemption.

This conflict supports the continued need for an unambiguous exemption for joint exportation.

40/ Appendix A compares the operation of the Webb-Pomerene program with liberalized business review procedures.

of Justice has offered nothing to overcome concerns about its bias and the necessity for submitting large amounts of sensitive information to obtain the business review.

Moreover, a business review program fails to offer the protections the exporter needs. The business review letter affords only limited relief from the antitrust laws. The Antitrust Division reserves the right, at any time, to withdraw its clearance upon its own belief that circumstances warrant such action. In any event, the antitrust clearance only binds the Antitrust Division. Treble damage claims, by either an aggrieved customer or competitor, can be asserted even after conduct has been approved by the Antitrust Division. While a liberalized business review procedure might ease some of the concerns of American business about the uncertain application of the antitrust laws to conduct in foreign commerce, it cannot provide even the degree of protection that is currently provided by the Webb-Pomerene Act.

Phosrock believes that some suggestions deserve serious consideration by the Subcommittee. First, in our view, a significant reason for under utilization of the Act is the absence of a clear enforcement structure. Section 5 of the Webb-Pomerene Act provides a useful framework for such administration, but it has not operated for many years. Regulation should be centralized in the place that possesses the interest and expertise to ensure that the purposes of the Act are fulfilled. Second, uncertainty regarding permissible conduct will continue as long as the immunity conferred is stated in general terms. It is not enough to say that the Webb-Pomerene Act should be amended to

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eliminate exposure to treble damages and criminal litigation. Existing associations have that protection today -- but only for conduct in "export trade". An important and useful purpose would be served by stating with great specificity the kind of conduct that is beyond legal challenge. 41/ The Subcommittee could quite profitably focus on the specific conduct permitted to be undertaken jointly. Indeed, as the Subcommittee recognized in its Report on U.S. Export Trade Policy:

> Export activities are subject to uncoordinated and sometimes conflicting demands from different government agencies. In the face of competition from countries like Japan and Germany which achieve considerable coordination in these matters, the inability of the U.S. to promote cooperative export expansion efforts and synchronize export policies is a serious disadvantage.
>
> Legislative efforts to enable U.S. exporters to compete with foreign banks and cartels in overseas markets date back over sixty years. The Webb Pomerene Act (1918) exempts the formation and operation of Export Trade Associations from some prohibitions of the Sherman and Clayton Acts, but its provisions have been singularly underutilized. Only 28 such Associations exist today, account for less than 3% of U.S. exports.
>
> The principal reason for the Act's failure is its vagueness. Because no definitive standards are prescribed for permissible activities. Webb associations have repeatedly been challenged by the Justice Department. Facing the likelihood of an antitrust investigation and with no clear idea of permissible activities and possible benefits under the Act, firms have been reluctant to form Export Trade Associations. 42/

41/ See, e.g. United States v. Minnesota Mining & Mfg. Co., 92 F. Supp. 947 (D. Mass. 1950).

42/ U.S. Export Trade Policy, A Report of the Subcommittee on International Finance of the Senate Committee on Banking, Housing and Urban Affairs, 96th Cong., 1st Sess. 18 (1979).

Finally, detailed investigation of the trading company concept proposed in Senate bill S.1663 is worthwhile. As has been indicated, Phosrock believes that its operations under the Webb-Pomerene Act have made a positive contribution to U.S. export trade. The question remains, nevertheless, whether American firms are reaching their maximum potential to promote and stimulate foreign commerce. The focus of the Webb-Pomerene Act is relatively narrow: it provides for limited antitrust immunity to permit joint foreign sales. Although Phosrock does not suggest that the Webb-Pomerene Act be weakened in any way, exploration of complementary legislation like S.1663 can reveal whether additional kinds of joint export activities should be encouraged. The Japanese sogo shosha well illustrates the substantial contribution to foreign trade promotion that can be made by trading companies. These firms are engaged in financing, resource development, planning, marketing, research, construction and distribution, either in the capacity of intermediaries or as joint venture partners. They have had a phenomenal record of success. While important issues remain to be explored concerning the scope and consequences of trading company action, the inquiries may well be fruitful.

In conclusion, Phosrock supports the efforts of Chairman Stevenson and the Subcommittee to expand American export trade. This goal of promoting American competitive interests abroad must receive prompt attention if we are to solve the economic problems we now face.

APPENDIX A

COMPARISION OF THE OPERATION OF THE WEBB-POMERENE ACT AND THE PROPOSED LIBERALIZED BUSINESS REVIEW PROGRAM

WEBB-POMERENE	BUSINESS REVIEW
Statutory Basis and Certainty to the Businessman	
(1) "Moreover, in the Webb-Pomerene Act, ch. 50, 40 Stat. 516, as amended, 15 U.S.C. § 61 et seq., Congress has provided a narrow and carefully limited exception for export activity that would otherwise violate the antitrust laws. See United States v. Concentrated Phosphate Export Assn., 393 U.S. 199. A judicial rule excluding all non-Americans as plaintiffs in treble damage cases would hardly be consistent with the precisely limited exception Congress has established to the general applicability of the antitrust laws to foreign commerce." Pfizer v. Government of India, 98 S. Ct.584, 588 n.12 (1978).	(1) There is no statute authorizing opinions - hence, a dispensation granted by one Assistant Attorney General may or may not be approved by a subsequent Administration. The businessman is thus subjected to the vicissitudes of future interpretations of the law.
Scope of Antitrust Immunity	
(2) In the course of conducting the business of a Webb association (qualified under the Act) the association may determine, as a prerequisite to making a sale, the price at which it will sell, and such a determination is not illegal under the antitrust laws. United States v. Minnesota Mining & Mfg. Co., 92 F. Supp. 947 (D. Mass. 1950).	(2) The Department of Justice has no power to prevent a foreign buyer from asserting a claim against American companies engaged in joint marketing to that customer.

Efficiency of Administration

(3) In the organizational papers filed with the FTC (and subject to Commission review and approval) qualifications for membership are established; hence, there is an orderly and legal means of determining who is a member and the relationship between the members is delineated. Thus, at any particular time, a determination can be made as to who is within the immunity and who is not. Moreover, the Congress had the foresight in enacting the Webb Act to establish an orderly means to deal with other problems which may arise in the operation of the association -- i.e., the adjustment hearing procedure. 1/

(3) By contrast, there are no statutory guidelines by which to resolve questions as to which companies may jointly apply for an opinion or who may subsequently join in an ongoing cooperative venture. For example, suppose A and B apply for dispensation to jointly sell in Pakistan. C wishes to join with them in the application to Justice but A and B are opposed. How is this conflict resolved? Alternatively, suppose A and B get the dispensation and develop substantial sales in Pakistan and C asks to join with A and B in future sales but A and B refuse to let C join with them. Are A and B subject to treble damages for boycotting C? Is the Division, assuming it has the legal power to do so, compelled to serve as a referee and compel A and B to allow C to join with them? Moreover, Pakistan is but one of many potential markets -- could one advisory opinion grant a dispensation for A and B to act jointly in all markets? Suppose a broker asks A and B to let him serve as their broker and this request is denied through a joint

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1/ See 15 U.S.C. § 65 (1976). Controversies can generally be handled more expeditiously, and at less expense, at these hearings than in a formal court proceeding. Morever, in contrast to a judgment in favor of the United States in a criminal or civil antitrust action, an adverse determination at an adjustment hearing does not establish a prima facie case for private treble damage plaintiffs. 15 U.S.C. § 16 (1976).

decison by A and B. Does the broker have a cause of action? The problems are endless. In short, when two or more companies undertake a long term committment to act jointly in export selling no one can anticipate all of the various problems which will be encountered. Hence, there is generall no way for a single advisory opinion to provide sufficient protection to make the advisory procedure an effective method of encouraging businessmen to engage in the complex field of export trade.

POLICY FORUM

The Realities of United States Foreign Trade and The Fictions Of Our Cartel Advocates

by Emil Sherer Finley

Emil Sherer Finley is the founder, president and chief executive officer of International Commodities Export Company (ICEC), a division of ACLI International.

Painful facts make fools of some of us all of the time, and almost all of us some of the time. When all the known evidence says "green," some of us proclaim "red" in the hope of finding some evidence of red. When we need fairness, some of us would impose judges who have pre-judged our cases. When we have proof that people have hurt us, some of us would reward them lest they not reform. When we have to know the facts, most all of us resort at some stage to fictions to shelter us from the unpleasant reality. When in doubt, we quite frequently legislate.

Not that truth, beauty and right action don't often emerge and win out. It is the glory of free speech and a democratic process that quite often pigheaded wrongness gets defeated in the marketplace of ideas and therefore in the halls of Congress. It involves a struggle that is rarely inviting. But we have to be existentialists, if not optimists; for to be otherwise is to leave the field by default to the beguiled, the misled and, alas, the greedy. Conscience requires a fight.

In trying to deal with some woes of our foreign trade, we have been besieged and somewhat beguiled by the misled and, yes, the greedy. The cartel advocates are in the marketplace to overcome painful facts with fictions. Realities, which once seen would help us to deal rationally with the painful facts, are lost. And some very good men have made some very wrong proposals.

PAINFUL FACTS AND FOOLISH REACTIONS

The most painful facts of our foreign trade are that in six out of the last eight years the United States has had a deficit balance of foreign payments; and inflation has boomed along, with the cheapened dollar only exacerbating the flow of money out by reducing our buying power. Last year we had a deficit in our balance of trade of $30 billion.

We are not used to such things. All was right with our trade in this century up to 1971. Because we get worried it becomes time to panic or to avoid real panic by frenzied action. It becomes time to look for quick solutions. And it becomes time to treat painful facts as if they have nothing to do with our own faults, for self-blame is still more painful. We begin to create myths from long-ago half-truths or from no-truths. Thus, it must be that the foreigners at our gates are conspiring against us and are taking advantage of our good nature and fairness. They bribe better or bigger; they are more organized in combating our poor, fractionalized industries. Indeed, we see grand cartels, government sponsored, taking away our business; and all the while our Justice Department's Antitrust Division and our notions of free competition do not allow us to fight back. Foreigners come here with impunity, and we go nowhere but that we are faced with stifling, organized resistance in Washington and unfair, subsidized competition from the outsiders. The answer—so we are then told—is to fight back with the same weapons. Let us create our own cartels. There are even suggestions that we were wrong in this post-Watergate era to demand that our industries stop bribing foreign officials. Nonsense: all of this.

One need not take seriously the all-too-serious "jokes" about the need to out-bribe our foreign competitors. In the long run, self-defeating corruption cannot be justified. If our society must save itself by being corrupt, then it is not worth saving. I won't dote, but the fact is that Americans can compete successfully without bribing. If there is a cartel that is needed, it is a cartel that has one rule: thou shalt not bribe.

As to the drive to create more cartels, that requires some analysis, for it is not plainly immoral and becomes amoral only when reality catches up with the fictions that are used to support the cry of more cartels.

Here is the reality.

THE WEBB-POMERENE ACT

There is already in existence in the United States a piece of cartel-creating legislation dating from 1918, the Webb-Pomerene Act. The Webb Act allows for the creation of associations of producers of goods solely for the purpose of engaging in export trade. The associations can operate if they register with the Federal Trade Commission and as long as they do not restrain the export trade of any "domestic competitor." Webb associations are not supposed to "enter into any agreement, understanding or conspiracy, or do any act which artificially or intentionally enhances or

depresses prices within the United States . . . or which substantially lessens competition within the United States or otherwise restrains trade therein." Under a consistent interpretation by the FTC and as followed by the courts, Webb associations can and do fix prices and set up quotas.

"Under a consistent interpretation by the FTC, and as followed by the courts, Webb associations can and do fix prices and set up quotas."

While the original vision of the Congress and of the Federal Trade Commission Report that recommended the Webb Act saw the true function of the association as a cost-reducing expediter, there is no question that the role of price-fixer and market allocater has been the predominant feature of Webb associations over the years. In brief, Webb associations have taken on the usual roles of cartels. Thus, we have in America government sanctioned cartels that are exempted in the export trade from the normal operation of the antitrust laws.

The prime justification b· in 1918 for Webb associations was that t. ., were needed by small companies in order to compete with foreign subsidized businesses and cartels. At the time, American corporations were only beginning to become factors in world commerce. The theory was that associations could cut costs and thus would allow American corporations to compete successfully on the basis of price as well as quality of goods.

WEBB ACT PERFORMANCE

In 1967, the Federal Trade Commission completed a study—an empirical study—of Webb associations over their first 50 years. The report found that the Webb Act had failed to promote United States exports in any significant way during those 50 years. The 1967 FTC study revealed that the export associations that succeeded for any length of time were those involved in industries where the members were leaders of a domestic oligopoly, were dominant factors in the foreign trade and dealt with a homogeneous product. The small company did not take advantage of the Webb-Pomerene Act. Of the 465 members of Webb associations during the period between 1958 and 1962, for example, only 17 per cent had assets of $1,000,000 or less, and only 22 per cent had assets of between $1,000,000 and $5,000,000. The large firms counted for about 80 per cent of all exports by Webb associations. There were never any more than 57 registered associations in any one year, and some companies were members of more than one association. During that same period of 1958 to 1962, Webb associations accounted for only 2.4 per cent of total United States dollar exports. The 1967 FTC Report concluded:

> "In summary, Webb-Pomerene activity is limited to comparatively few associations handling a limited range of products, and the number of beneficiaries from such activity is also quite small. . . . These members [of Webb-Pomerene associations], for the most part, were drawn from the upper reaches of the business population and, at the same time, were the major beneficiaries of Webb-Pomerene assistance. . . . Fifty years of experience, including a recent period of uninterrupted trade expansion, reveals the Webb-Pomerene Act as no panacea for the expansion of foreign trade by small business and, indeed, points to the conclusion that it plays a very minor role in over-all U.S. exports." (FTC Report, pp. 317-18.)

The data available since 1967 proves that nothing has changed. If anything, the utter failure of our legalized cartels in promoting American exports is more pronounced. By 1976, only 1.5 per cent of the total U.S. exports came through Webb associations and the number of registered Webb associations was only 33. Today, there are 35 registered associations with 338 members, many of which are in more than one association. The registration rolls at the FTC make it plain that the firms that benefit most from the Webb Act are still those that market homogeneous products and dominate their industries. I have taken a look at the nature of the products of the 35 currently registered Webb Act associations. Only four of them seem to be in industries where there are non-homogeneous products.

As of 1976, a total of six Webb associations accounted for nearly two-thirds of the dollar value of all Webb-assisted exports. These six associations (plus one other) are the only presently registered associations that were in existence in 1962. Four of the big six produce homogeneous goods: dried fruits (2), rice products and paper. The other two are both film-industry associations, formed by the 10 dominant firms in the industry.

". . . there is no question that the role of price-fixer and market allocater has been the predominant feature of Webb associations over the years. In brief, Webb associations have taken on the usual roles of cartels."

The pattern is clear. Webb associations have benefited those firms that need help the least, and the firms use the associations not to promote volume but to stabilize export prices. Since the future (and past strength) of United States exports lies in complex, differentiated products, Webb associations are not likely to play any larger role in the United States export picture than they have in the past.

THE EFFECT ON DOMESTIC TRADE

Although irrelevant to small United States companies and insignificant in the scheme of over-all exports, Webb associations have had a deleterious effect on domestic pricing and competition.

With most homogeneous products there is a traditional relationship between the domestic price and export price (usually a percentage "discount" on the domestic price). Usually, the export market is viewed as a way to sell off "surplus" and ward off domestic price deterioration. As a result, export price fixing is always bound to mean price fixing or stabilization in the domestic market. We cannot be blind to what common sense screams at us: When major producers of the same or virtually the same product set export prices in unison and "predict" what they will be for the future, they know necessarily that they are helping to set a level for domestic prices and are helping to stabilize these prices.

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There is also a domestic monopolizing aspect to Webb associations. Successful Webb Act associations dealing in undifferentiated products control or dominate the "surplus" export market; and that surplus market often is the difference between a profitable trading year or an unprofitable one. Even when large producers remain outside the cartel, the road to survival or entry of the small firm is more difficult.

That Webb-Pomerene cartels are needed to fight foreign cartels has always been grounded in a theoretical fallacy and no real truth. The existence of foreign cartels that fix prices theoretically could only *help* American competition. They could only create price umbrellas for their American competition. In the United States, for example, when these Webb-Pomerene Act associations come into being, the large American companies outside the cartels are quite happy because they can easily underprice the rigid cartel or the cartel sets a price that the competitors gladly follow. Indeed, it is a commonplace in the true market that the best policemen of Webb-Pomerene pricing are those outside the cartel.

In fact, as the FTC found in 1967, large oligopolistic American corporations do not need the associations to compete with any foreign business concern or groups of concerns. Today American companies dominate the fields where Webb associations operate successfully. By stabilizing prices and establishing quotas, the members of Webb associations do not compete in any traditional sense with the foreigners. If they wanted to compete for business, they would not be fixing prices, they would be setting prices independently based on costs and reasonable profit. And dealing mostly in homogeneous products and in dominated markets, Webb association members do not compete unless they compete on prices or services that amount to price savings.

THE REACTION ABROAD

It is a fact that Webb associations are welcomed by their supposed enemies abroad. When Webb associations are created or expand, the foreign competitors hail the event. The "reviews" abroad become "mixed" only because the *purchasers* of the products—usually found in undeveloped nations—know that they can expect increases in the United States prices and stabilized prices everywhere. All one has to do—if one really wants to find out what the reality is—is to read the trade journals when one of these Webb Act associations is created or increases its membership.

For example, *Green Markets*, a fertilizer market trade weekly published by McGraw-Hill, reported that Brazilian traders and users were quite unhappy when the Phosphate Chemical [Webb-Pomerene] Association—"Phoschem"—expanded its membership of fertilizer producers last year. The July 17, 1978, edition quoted one Brazilian "source" as saying it was "rotten." Another Brazilian was reported to have said, "We expect drastic increases in U.S. prices." Another said that it was likely to "jeopardize" the "import volume." Brazil is a major importing market for American fertilizers. But the article further reported: "One Canadian *producer* thinks higher U.S. export prices might even stabilize the Canadian market and help his company." It said also: "An official of the South African Fertilizer Society [a cartel] said stable prices and a better market would probably result." The article noted: "Most European producers are optimistic. They feel that as well as raising prices, the Phoschem expansion will provide the market stability which has been absent in recent months."

That's reality. What Webb Act cartels are about are price stabilization, price-increases, production control, hoped-for worldwide "regulation," not competition and vigorous promotion of American products. The result is less trade for us—controls, controls, controls for the sake of prices. It is no accident that since Phoschem's expansion, the prices of its products—export and domestic—have gone up about 50 per cent and that hike does not reflect cost increases. Inflation guidelines are ignored. And so the theories of those not in the marketplace are exposed as fantasies. Read what businessmen say; listen to us in the trade, who know our "customers."

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SEVERAL OTHER REALITIES

Furthermore, the function of selling agent is not best done by a Webb-Pomerene Act association or, in fact, often done by the associations. Again, a little investigation will show that Webb association members do their own selling and their own marketing and use the association offices only as a conduit and a means to prevent competition. According to the FTC, only eight associations reported sales agencies in the United States and only six reported overseas agencies in 1976. Moreover, only 12 directly assisted exports, and these exports accounted for less than 17 per cent of dollar Webb-assisted exports in 1976. As the FTC has found: All the sales functions can be, and have been done historically, with more vigor and with a lot more results by independent exporters. Agreed market division means complacency and no real promotion. Webb associations beget an atmosphere of "cordiality" with foreign competitors that is indistinguishable from gentlemen's agreements.

Moreover, it is a fact that in many industries where Webb associations exist, there is no real foreign competition. Even if you believe the answers that the associations have supplied to the annual FTC questionnaires, Webb Act associations have hardly been fighting foreign cartels. Only 11 out of the presently registered associations have claimed competition from cartels or government-sponsored organizations. And their answers have to be suspect; there is, at least, hyperbole in them.

Again Phoschem provides a good example. Its answers to the FTC claim competition from overseas cartels and foreign government organizations. In the two major products that it deals with, diammonium phosphate and triple superphosphate ("DAP" and "TSP"), Phoschem has no significant competition in most world markets. And, by some "magic," Phoschem will not offer much material to those few places where the foreign production has had its "traditional" sway. Over-all, the Americans dominate what they choose to dominate. They are the giants. In 1977, for example, the world export trade in DAP and a related product totaled 1,870,000 tons (of P^2O^5). The American share of that market was 1,367,500 tons (of P^2O^5). In 1977, the total world export of TSP totaled 996,500 tons (of P^2O^5). American exports accounted for 504,600 tons (of P^2O^5).

Thus, there is no need for Webb-Pomerene Act associations in fields such as the one with which Phoschem is involved; they serve nothing but anticompetitive ends. And Phoschem, I submit, is typical.

Our problems stemming from the Webb Act cronyism and artificial price structuring are exacerbated by still another development unforeseen in 1918: Multinational corporations are found in good number among Webb associations. And they aren't merely multinationals in unrelated businesses; many Webb association members have foreign subsidiaries that (1) buy from the Webb associations and (2), believe it or not, compete with the Webb associations—without the slightest compunction and without protest within the associations. There hasn't been a word of criticism from the Federal Trade Commission. Necessarily, where multinationals participate in American price-fixing and quota-setting, something beside the promotion of American exports has to be involved. In fact and in effect, our foreign competitors participate in our price-fixing decisions and their interest is not in "selling American."

Factually, foreign buying "cartels" have come about in response to price-fixing selling cartels—our Webb associations. There is no evidence that foreign buying cartels or foreign government purchasers have hurt United States exports or forced anybody to sell anything other than at a fair and profitable price. There is no evidence that they have had an unfair bargaining position vis-a-vis American exporters. We in the market know that the reality is that government agencies are most often easier to deal with than multiple foreign purchasers. It is not a fact that we sell cheaper to government sponsored buyers. For example, Asian government agencies and buying cartels traditionally pay higher prices than do the multiple private purchasers in Brazil.

When you are concerned with standardized products in demand—the products that are the prime items for Webb-Pomerene associations—there are, in fact, no barriers with which the Webb-Pomerene Act has to deal. With these products, there are producing nations and there are consuming nations. Consuming nations are always disturbed by cartelization, because they know that that means higher prices (and in the instance of fertilizers and Phoschem, for example, higher food prices for their populations). The hurtful barriers come, if at all, from *producing* nations to protect home industry. Webb-Pomerene Act associations and the Webb Act itself have nothing to do with fighting those barriers. Webb-Pomerene associations encourage those barriers because they naturally tend to respect them. Price-minded cartels are interested in keeping out foreign competition from the United States (because they are the major producers here). There is

an understood rule of reciprocity at work, which stabilizes prices and protects home markets.

All of the facts should tell us, then, that we should have more competition, not less competition, if we want to increase our trade. Give us more aggressive marketing, not less. The facts establish, at very least, that Webb association export outlets are hardly worth the harmful effects on the domestic market. Those facts should also advise us: Be careful of these price-fixing and quota-setting organizations with their meetings, constant information-sharing and daily price-"predicting."

THE RESPONSES AND THE DANFORTH BILL

But our balance of payments is bad; and that means fewer jobs at home, a weaker dollar, a greater impetus to inflation and a thousand other ramifications that economists say we fail heir to. So the cartel believers come out of the woodwork and are listened to. Groups of them, particularly the National Construction Association, importune the Commerce Department. (They know enough to stay away from watchful Justice and sleeping FTC.) They go to the Congress. And, despite the empirical evidence that lies for the reading in FTC reports and records and despite a recent critical report of the President's special commission on the antitrust laws, we have the Commerce Department lobbying for more cartels and the lessening of restrictions on them. And we find some very able Senators believing in the benefits of more cartels and the lessening of restrictions on them. Logic and the facts are ignored; myths and plain fiction take over.

Indeed, Senator Danforth in conjunction with Senators Bentsen, Chafee, Javits and Mathias (a most formidable group) introduced a bill in the Senate last February that would amend the Webb-Pomerene Act by expanding its antitrust exemptions to allow for more restraints on domestic commerce, enlarging its coverage to activities beyond foreign export trade (as long as they were incidental to it) and placing services as well as goods under amended Webb Act protection. The bill would transfer supervision of the associations from the moribund Federal Trade Commission to the friendly Commerce Department and insulate the associations from direct Antitrust Division oversight. While there would be pre-registration screening for new Webb associations, all present associations would be grandfathered into the antitrust exemption, and no private person could sue to revoke or alter any association's status. A review of the new procedures under the Act would occur seven years from now.

The bill itself and Senator Danforth's Senate speech in support of it make it plain that it is the product of fear and fiction. The "findings" that appear in the bill as a preamble give the painful and scary fact of a $30 billion trade deficit in 1978, tell ominously of foreign government subsidized competition to United States exporters, note the fall of the United States' share of total world exports from 19 per cent in 1968 to 13 per cent in 1977 and then declare:

> "Small and medium-sized firms are prime beneficiaries of joint exporting, through pooling of technical expertise, help in achieving economies of scale, and assistance in competing effectively in foreign markets. . . "

That foreign government subsidized competition is not so terrifying and that small and medium-sized firms have never benefited from such joint exporting are now beside the point. Red has become green by proclamation and because of painful facts. The pre-judgers—the Department of Commerce—are the new guardians. The oligopolists and multi-nationals are to be rewarded by automatic inclusion in the new and more tolerant system. When one should hesitate, we legislate.

In his speech to the Senate introducing his bill, Senator Danforth acknowledges the poor performance of Webb associations as promoters of commerce and the fall-off in membership. But he gives some reasons. The first reason for Webb failure, he says, is that the "vast majority of the . . . Webb-Pomerene associations lacked sufficient product-market domination to exert foreign market price control and membership discipline." That, of course, is not changing facts; that is misreading their import. What Senator Danforth is telling us is that only the giants (1) have been able to use the Act and (2) have connived successfully to fix prices because they are dominant and can make their price-fixing stick. That hardly speaks for the need for more associations or the desirability of more leeway for *all* of them!

> "Senator Danforth's bill . . . is the most serious, recent and erroneous reaction to unfavorable foreign trade events. . . . The bill at best sets our sights away from where they should be. It is frightening that very sound men can be so misled."

Senator Danforth then tells us that the second reason for poor Webb-Pomerene performance is our "traditional" primary focus on the domestic market. Surely the primary focus of most of our indigenous industries will always be on our domestic market, the biggest market in the world; but the past two decades have witnessed an explosion of interest in foreign markets and a vast expansion in foreign trade. And look how Americans have jumped—tripped over themselves—at the opening of opportunities in China. Sufficient focus, there is; and foreign trade will expand. The facts bespeak a reason for failure other than a lack of focus on foreign trade: Interest in associating has not similarly expanded because the Webb Act can only

benefit the dominant few in very special industries.

For his third reason for Webb-Pomerene failure, Senator Danforth offers the fact that services are not covered by the Webb Act. He then says that the President's National Commission for the Review of Antitrust Laws and Procedures recently recommended that services be covered. That is a gloss. The independent Commission appointed by the President made its report last January. There was a section on the Webb-Pomerene Act. The report reviewed the poor performance of Webb-Pomerene associations. It rejected the proposition that the Webb-Pomerene Act be expanded or even be kept in place. In fact, a number of Commissioners would have repealed it with no further ado. The report declared that automatic exemptions are not warranted, and a needs test should be required of all would-be registrants. The report urged that the Congress review the Webb-Pomerene Act with a view to repealing it or substantially restricting it. Its recommendation on services was that *if* the Act were retained then it saw no reason not to include services as well as goods.

Whatever, this catering to services is narrow special-interest legislation, a sop to the construction industry pressure groups. I predict that, if the special legislation ever comes to be, it will not spark any more activity abroad; it will only benefit the large corporations already in the market by a gift of immunized collusive price-setting—which will have the usual "predictive" price-setting influence in the domestic market.

For his fourth and "perhaps most important" reason why Webb-Pomerene has failed, Senator Danforth offers the hostile attitudes of the FTC and the Antitrust Division of the Justice Department and the fears that businessmen have that they will be declared antitrust violators if they join the associations. The fear of the FTC has to be a fiction; it has been a docile watchdog; more than docile, it has wagged its tail. It has gathered information from the associations without questioning the accuracy of anything and has done nothing with that information. It let one association rig bids for United States government AID-financed contracts for years; it was the Justice Department and eventually the Supreme Court that put a stop to that multi-million dollar raid on our Treasury.

As to the Justice Department, it has never made a wholesale attack on Webb associations, generally leaving them to the FTC. The Antitrust Division, however, can and does bring a welcome skepticism and questioning to bear on these cartels. Industry and the Congress should be grateful that someone is there ready to worry about whether permitted collusion has slipped into illegal conspiracy in domestic trade. Remember, under the Webb Act, people who are competitors and are not supposed to be setting prices for the domestic trade are in daily contact. They are constantly exchanging price, cost and supply information. They are continually agreeing to prices for future exports based on what they believe will be future market prices here and abroad. That's at least dangerous territory, if not (as most businessmen who have had experience with Webb associations believe) absolutely lethal ground for fair, competitive pricing.

Still the Antitrust Division has moved dramatically in all the Webb Act years only against the AID gougers. It has respected the Webb-Pomerene exemptions, even if many believe them to be unworkable. The only people who need fear (and, I submit, who have ever feared) the Antitrust Division are those who would *explicitly* (if covertly) use Webb Act functions as an occasion to agree to fix prices and set quotas in the domestic trade. Angels do not fear to tread where a haven is made for the unholy. It is not fear that has kept people away from Webb Act associations, but the fact that they don't find them helpful.

CONCLUSION

I have picked on Senator Danforth's bill because it is the most serious, recent and erroneous reaction to unfavorable foreign trade events. While it is hard to imagine that the Congress will pass the measure or the President would sign it (even though the Commerce Department cartel advocates speak to us as if they have the ear of the President), the bill at best sets our sights away from where they should be. It is frightening that very sound men can be so misled.

"Let us not for the sake of some minor hoped-for export trade advantage bring in certain major foreign trade and domestic market disadvantages."

Because the evidence is so overwhelming, I am emboldened to suggest what is needed. Let us reaffirm our belief in competition by private enterprise. Let's do away with the inherent unfairness of price-fixing; it is an instrument for oppressing all of us and fosters "greed" to our detriment. Let's speak no more about encouraging cartels. If anything, we should be looking to get rid of them. If there be any truth to the need for limited export associations, let the burden shift to those who would seek an exception to antitrust laws to prove they are not anticompetitive. Let us not for the sake of some minor hoped-for export trade advantage bring in certain major foreign trade and domestic market disadvantages. In any event, let us, first, undertake the study the President's Commission urged—before legislating. It makes no sense to put a truck in high gear and our foot on the pedal until we know whether the grade around the curve is steep.

Let us not be beguiled, misled or scared out of our common senses. ■