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**Hearing of the U.S. Senate
Committee on Commerce, Science, and Transportation
Interstate Commerce, Trade, and Tourism Subcommittee**

on

“The Imbalance in U.S.-Korea Automobile Trade”

**Wednesday, September 24, 2008
10:00 a.m.
253 Russell Senate Office Building**

**Testimony by
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on behalf of the

**U.S. Chamber of Commerce
U.S.-Korea Business Council
American Chamber of Commerce in Korea
U.S.-Korea FTA Business Coalition**

The U.S. Chamber of Commerce, the U.S.-Korea Business Council, the American Chamber of Commerce in Korea (AMCHAM Korea), and the U.S.-Korea FTA Business Coalition would like to thank the Interstate Commerce, Trade, and Tourism Subcommittee for the opportunity to provide their views on U.S.-Korea automobile trade.

The U.S. Chamber is the world's largest business federation representing three million businesses of every size, sector and region. The U.S.-Korea Business Council, an affiliate of the U.S. Chamber, is composed of U.S. companies that are significant investors in and exporters to Korea. AMCHAM Korea represents hundreds of U.S. companies doing business in Korea. The U.S.-Korea FTA Business Coalition is a group of over 500 U.S. companies, trade associations, industry organizations, and chambers of commerce representing businesses of every size and sector of the U.S. economy that support the U.S.-Korea Free Trade Agreement (FTA), which was signed on June 30, 2007. The U.S.-Korea Business Council serves as the Coalition's secretariat.

Our four organizations believe that the U.S.-Korea FTA is the best solution for addressing many of the factors that have contributed to the historical imbalance in U.S.-Korea automobile trade. This is one of the reasons why the member companies and associations of our organizations enthusiastically endorse the U.S.-Korea FTA, the most commercially significant U.S. trade agreement concluded in over a decade.

This agreement provides very substantial benefits to all sectors of the U.S. economy. It enjoys broad support among U.S. manufacturers, farmers, and the services sector. By eliminating trade barriers in every sector of the Korean market to U.S. goods and services and securing a more open and competitive Korean market, the agreement will generate billions of dollars in new U.S. exports, creating new American jobs and economic growth.

Under the U.S.-Korea FTA, nearly 95 percent of bilateral consumer and industrial goods trade will become duty-free within three years; almost all remaining tariffs on goods will be eliminated within ten years. According to the U.S. Department of Commerce, Korean tariffs on U.S. industrial products average approximately 6.2 percent—twice as high as the equivalent U.S. rate. Over 80 percent of U.S. merchandise exports to Korea are manufactured products, and the agreement will bring tangible and significant benefits to U.S. manufacturers—including U.S. auto producers and auto parts makers. We note that the agreement covers trade in remanufactured goods, which will additionally create new export and investment opportunities for U.S. firms producing these products, including machinery and auto parts.

Korea's complex regulatory system and other non-tariff barriers have in the past limited opportunities for U.S. manufacturers and others to compete and succeed in Korea market. The U.S.-Korea FTA addresses these challenges with strong provisions and protections that open Korea's market, protect U.S. interests, and set the bar higher for future trade pacts. These provisions include expanded market access for U.S. producers in Korea in sectors where they currently face restrictions on investment and on their operations. The agreement will also guarantee transparent and predictable regulatory and rulemaking procedures in Korea, protect and enforce intellectual property rights, enhance investment protections, and help ensure the fair and transparent application of competition policy for all U.S. companies doing business in Korea. These and other

elements of the FTA will level the playing field for U.S. businesses competing in Korea's dynamic \$1 trillion economy. Moreover, the FTA will deepen the ties between the United States and Korea, reinforcing a bilateral partnership that has promoted regional security and prosperity in East Asia for more than fifty years.

While today's hearing focuses on the issue of U.S.-Korea automobiles trade, we are including as an attachment to this testimony a report issued by the U.S.-Korea Business Council on the broader and very substantial benefits that the U.S.-Korea FTA will provide the U.S. economy if the Congress approves the agreement.

Our organizations are sensitive to the challenges facing the U.S. automobile industry in the current domestic and global economy. We recognize the leadership role that the U.S. automobile industry has played in opening markets and removing unfair trade barriers to U.S. goods and services all around the world, to the benefit of the entire U.S. economy. Moreover, we are acutely familiar with the challenges that the U.S. automobile industry long encountered in the Korean market. AMCHAM Korea and the U.S.-Korea Business Council repeatedly have called on the Korean government to eliminate tariff and non-tariff barriers and other discriminatory policies that have severely limited opportunities for U.S. automakers to compete in the Korean market.

We urged Korean and U.S. trade negotiators to include strong provisions addressing these issues in the U.S.-Korea FTA. And that is, in fact, just what they did. We are pleased that the U.S.-Korea FTA includes commitments by the Korean government to address virtually every tariff and non-tariff market access barriers to U.S. automobiles in Korea raised by the U.S. auto industry during the FTA negotiations. Once the FTA is ratified, we are committed to working hand-in-hand with the U.S. auto industry to make sure that Korea fulfills all of its FTA commitments.

Delaying or rejecting the U.S.-Korea FTA on the basis that it does not go far enough in opening Korea's market to U.S. autos will not right the imbalance in bilateral automobile trade. Rather, the best way to accomplish this goal is by ratifying the U.S.-Korea FTA and by focusing our energy on ensuring that Korea faithfully fulfills its FTA commitments. If we do that, we can ensure that Korean tariff burdens on U.S. auto makers are eliminated; that tax burdens are significantly reduced; that existing non-tariff barriers are addressed and new ones are not imposed; and that the Korean government does not dampen sales in other ways.

How the U.S.-Korea Free Trade Agreement Will Reduce Barriers to Auto Trade

It is important to recognize how much the U.S.-Korea FTA does to eliminate many of the Korean trade barriers to U.S. autos. The agreement will eliminate immediately Korea's tariff of 8 percent on U.S. passenger vehicles, 10 percent tariff on U.S. trucks, and almost all on U.S. auto parts, which currently range from 3 percent to 10 percent. These cuts will instantly give U.S. auto and auto parts manufacturers a price advantage in the Korean market.

The FTA reduces substantially the taxes levied on autos, and eliminates their discriminatory effect on U.S. and other foreign vehicles. Under the FTA, the Korean government will amend its

Special Consumption Tax and Annual Vehicle Tax to reduce existing maximum tax rates and to further eliminate aspects of these policies that have discriminated against U.S. autos on the basis of engine size. This “cascading” set of taxes disproportionately affects U.S. automakers because U.S. vehicles tend to have relatively larger-sized engines than Korean vehicles. The Korean government has also made a commitment under the FTA not to impose any new engine displacement taxes or to apply these taxes in a discriminatory manner. Korea will also publicize the availability of an 80 percent refund of its Subway Bond Tax for purchasers of new automobiles, yet another tax that has been a barrier in the Korean market for U.S. autos. These reforms, when implemented, will reduce tax rates on U.S. autos in the Korean market to the same level as virtually all Korean autos and increase their price competitiveness.

The FTA includes specific commitments in the automotive area by the Korean government not to employ technical regulations that create unnecessary barriers to trade, and to cooperate on harmonizing standards. In particular, the Korean government has agreed not to apply emission standards more stringent than those used by the state of California and agreed to use a less stringent standard used in California for small volume manufacturers. Low volume manufacturers (those which sell fewer than 4,500 vehicles a year) are exempted entirely. The FTA provides for imported motor vehicles to be exempt from any new or amended Korean regulations related to self-certification for safety standards for at least two years after the date on which the regulations or amendments are issued; these standards will then only apply to models under certain conditions. By bringing Korean standards more closely in line with those applied in the United States, the FTA will further lower manufacturing costs and retail sales prices for U.S. autos in the Korean market.

The FTA includes important mechanisms for resolving autos-related trade disputes. A unique and innovative autos-specific dispute settlement mechanism will provide expedited resolution of disputes under the agreement. If the agreement’s dispute settlement panel finds that Korea has not complied with its obligations in the agreement’s auto provisions, it can authorize the United States to reimpose import duties on Korean automobiles. To enhance the enforcement effect, this expedited process—just for autos—will result in decisions in half the time of the normal dispute settlement mechanism. The FTA also establishes an autos working group to address regulatory issues that may arise and to review and provide comment on potential new Korean regulations affecting auto manufacturers. Under the FTA, when the Korean government is developing new regulatory measures for consideration, it must provide information on these proposals to the working group, thereby giving U.S. stakeholders an opportunity for early involvement in the process. In addition, the FTA ensures that non-governmental parties, including auto companies and labor unions, may provide advice and input to the U.S. government throughout the dispute resolution process. These and other stakeholders may take part in the activities of the autos working group. All of these commitments are binding obligations, something the United States did not have in past automotive arrangements with Korea.

In addition to its autos-specific provisions, the U.S.-Korea FTA also addresses standards and technical barriers to trade (“TBTs”) and many other practices that the Korean government long used to protect Korea’s market for a variety of manufactured goods from foreign competition. During the FTA negotiations, our organizations urged that the FTA eliminate Korea-unique standards and standards-setting, testing and certification procedures that are not in line with

international norms, not carried out in a transparent or predictable manner, and that have adversely affected the ability of U.S. companies to provide goods and services in the Korean market. The FTA includes commitments by the Korean government to enhance transparency in the development and implementation of technical regulations and related conformity assessment procedures. Under the agreement the Korean government will provide national treatment to U.S. entities for participation in the development of standards, technical regulations, and conformity assessment procedures. Korea has also committed to publishing the criteria used to recognize conformity assessment bodies, and to explain objectives and how proposed regulations will address those objectives when regulations are notified for comment and again when they are adopted as final. The Korean government will also make publicly available all comments received on proposals, notify proposals for comment even if they are based on international standards; allow at least forty days for written comments on proposals; publish notice of proposed and final regulations in a single official journal; and in publishing final regulations will include responses to significant comments received together with an explanation of the revisions made to the proposal.

Under the FTA, the Korean government is required to promote reliance on international standards that are consensus-based. Moreover, in areas where Korea recognizes non-governmental bodies to perform testing and certification for compliance with its technical regulations, the agreement includes the Korean government's commitment to provide national treatment to U.S. conformity assessment bodies and for Korea's government authorities to provide national treatment when testing and certifying U.S. products. The agreement also provides for the establishment of a bilateral committee to strengthen FTA and WTO commitments on TBTs, which will monitor implementation and promote cooperation.

Beyond these important provisions, the U.S.-Korea FTA contains further commitments by the Korean government that stand to benefit the U.S. auto industry and thus contribute to reducing the imbalance in U.S.-Korea automobile trade. These include: enhanced intellectual property rights protections and enforcement; new protections for U.S. investors and a more stable legal framework in Korea for investment-related cases; strong competition policy provisions; and statements by the Korean government that it will not discourage the purchase or use of U.S. goods or services—an important commitment in light of past “anti-import” campaigns in Korea.

In short, the U.S.-Korea FTA has stronger and more comprehensive provisions related to the automotive sector in the areas of taxes, tariffs, standards and technical barriers, and dispute settlement, than any other U.S. trade agreement. It provides a powerful tool for restoring balance to U.S.-Korea automobile trade and an important opportunity for ensuring that U.S. automakers and auto parts manufactures can fairly compete in the Korean market.

Anticipated Economic Effects of the U.S.-Korea FTA on the U.S. Auto Industry

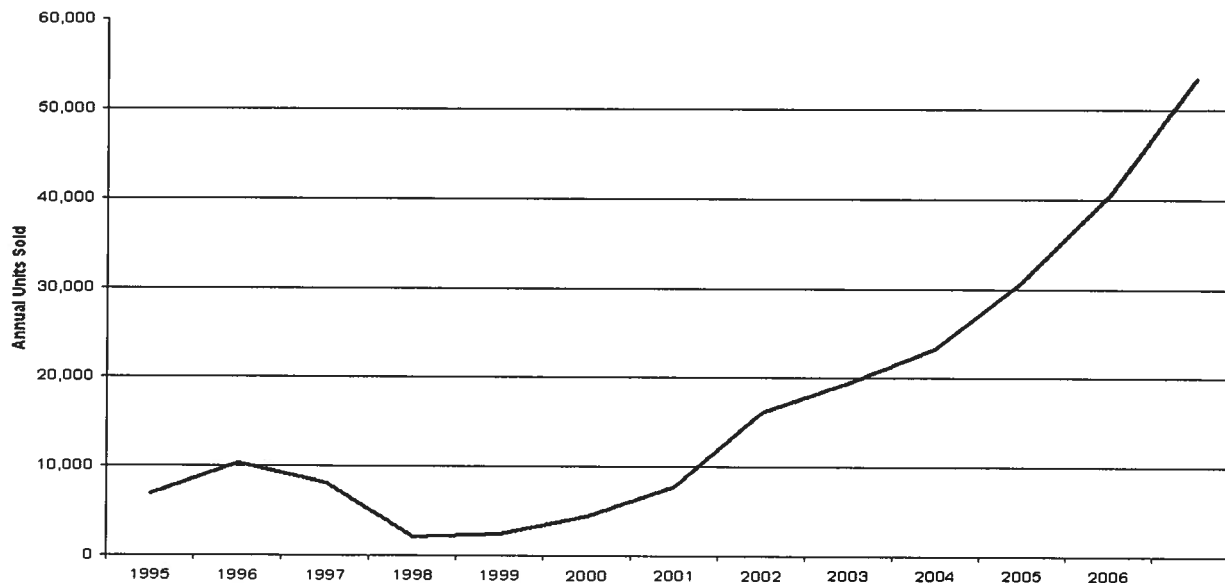
The U.S.-International Trade Commission (USITC) noted the agreement's benefits to the U.S. automotive sector in its September 20, 2007 assessment of the possible impacts of the FTA. The USITC forecasted that “U.S. exports of passenger vehicles to Korea would likely experience a large percentage increase as a result of the FTA” following full implementation of the FTA's

provisions on standards and certification requirements, taxes, regulatory reforms, and other measures addressing non-tariff barriers.¹ Its economic simulation estimated that exports of U.S. motor vehicles and parts to Korea would increase between \$294 million and \$381 million (45.5 percent to 58.9 percent).² The USITC observed that the removal of Korea's 8 percent tariff on U.S. passenger cars and 10 percent tariff on light trucks under the agreement would "likely have a positive effect" on U.S. exports, enabling U.S. companies to lower the price of their vehicles in the Korean market. It also concluded that the tax reforms included in the FTA would "more or less" equalize the total taxes paid on imported and domestic vehicles. While the USITC simulation also forecasted that U.S. imports of Korean motor vehicles and parts could increase by \$1.3 billion to \$1.7 billion (9 percent to 12 percent), it also forecasted that 55 percent to 57 percent of this estimated increase would be diverted from other foreign motor vehicles and parts sold in the United States.³ For this reason, the USITC concluded that the risk of any decline in output or employment for the U.S. automobile industry and U.S. auto parts manufacturers from the FTA "would likely be negligible."⁴

Rapid New Growth for U.S. Auto Exports to Korea

It is important to recognize that Korea is no longer the closed market it once was to U.S. and other foreign automobiles. In fact, foreign import penetration of the Korea haven auto market has grown exponentially in recent years—as evident from the below chart⁵.

Total Import Sales in South Korea, 1995-2007



¹ U.S. International Trade Commission (USITC). The U.S.-Korea Free Trade Agreement: Potential Economy-Wide and Selected Sectoral Effects. Washington, DC: U.S. International Trade Commission, September 2007. p. 3-74.

² USITC, *ibid.*, p. 2-8.

³ USITC, *ibid.*, p. 3-82.

⁴ USITC, *ibid.*, p. xviii

⁵ Korea Automobile Importers & Dealers Association.

For the first seven months of this year, the total market share of foreign autos in Korea was at 6.54 percent. In comparison, the market share for foreign vehicles in Korea was 5 percent in 2007, 3.89 percent in 2006, 2.7 percent in 2005, and 0.26 percent in 1999. U.S. automakers sold 6,235 cars in Korea in 2007, an increase of nearly 37 percent over 2006 sales levels, and have already sold more cars in Korea during the first seven months of this year—4,584 vehicles—than they did in all of 2006.⁶

The U.S.-Korea FTA would be beneficial to U.S. companies looking to increase their market share and product offerings in Korea. For example, General Motors announced earlier this year a study to examine the potential for introducing the Chevrolet brand into Korea. Currently, GM only sells the Cadillac brand in Korea, apart from its Korea-manufactured Daewoo brand. Ratification of the FTA could provide incentives for U.S. automakers to expand their brands and models available to Korean consumers. Indeed, the best way to continue to increase U.S. market share in Korea's auto sector is through Congressional approval of the U.S.-Korea FTA.

The Costs of Inaction

Delaying or rejecting the U.S.-Korea FTA on the basis that it does not go far enough in opening Korea's market to U.S. autos is not a solution for addressing the imbalance in U.S.-Korea automobiles trade, nor will this promote the competitiveness of the U.S. auto industry in the Korean market. Rather, it risks placing the U.S. automotive industry at risk of further market imbalances and erosion of its market share in Korea. European and Japanese automakers are subject to the same tariffs, non-tariff barriers, standards and regulations in Korea as U.S. motor vehicles, yet have rapidly increased their market share in Korea; through the first half of this year, Japanese and German models comprised Korea's top ten-selling foreign autos.

The foreign auto companies' proven success in Korea is a cogent argument for ratification of the U.S.-Korea FTA soon. Another is Korea's current negotiation of a network of bilateral and multilateral trade agreements with the European Union, India, Canada, and other countries. Korea is also studying possible FTA talks with China and the possible reopening of its FTA negotiations with Japan, which are currently in a hiatus. The U.S.-Korea FTA, if put into effect first, will help to set the terms for these negotiations and other future trade agreements. That is important as we do not want to have less comprehensive agreements set the rules of trade for us. Korea is close to completing its FTA with the European Union. If that agreement was put into effect before the U.S.-Korea FTA, the U.S. auto producers would be at a substantial competitive disadvantage to European competitors. This would only further exacerbate the imbalance in bilateral auto trade.

⁶ Korea Automobile Importers & Dealers Association.

Conclusion

The U.S. Chamber of Commerce, the U.S.-Korea Business Council, AMCHAM Korea, and the U.S.-Korea FTA Business Coalition believe that the best way to address the U.S.-Korea auto trade imbalance is through the ratification and implementation of the U.S.-Korea FTA and the strict enforcement of its provisions. Our organizations and our member companies view the agreement as a landmark opportunity to level the playing field in one of our country's most important overseas markets and international partners, and in doing so generate new jobs and economic growth across the United States. Our organizations welcome the opportunity to provide the members of the Interstate Commerce, Trade, and Tourism Subcommittee with additional information about the U.S.-Korea FTA.