

**THE UNITED STATES–SOUTH KOREA FTA:
THE FOREIGN POLICY IMPLICATIONS**

HEARING

BEFORE THE

SUBCOMMITTEE ON TERRORISM,
NONPROLIFERATION, AND TRADE

OF THE

COMMITTEE ON FOREIGN AFFAIRS

HOUSE OF REPRESENTATIVES

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WEDNESDAY, JUNE 13, 2007

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON TERRORISM, NONPROLIFERATION,
AND TRADE,
COMMITTEE ON FOREIGN AFFAIRS,
Washington, DC.

The subcommittee met, pursuant to call, at 10:05 a.m., in Room 2237, Rayburn House Office Building, Hon. Brad Sherman (chairman of the subcommittee) presiding.

Mr. SHERMAN. Everyone, if folks could please take their seats. I will ask staff to close the door to get as much quiet as possible. I want to thank Ambassador Bhatia and Secretary Hill for joining us today as we look at the United States-South Korea Free Trade Agreement.

Almost 200 years ago today, the 12th Congress rather than the 110th Congress was here in Washington. They passed a foreign policy vote, and as a result, 2 months later Detroit was burned to the ground. Today the 110th Congress will also have a chance to pass a foreign policy provision that will accomplish the same result as what happened to the city of Detroit, namely the passage of the South Korea Free Trade Agreement.

Now, as in the past, administration officials have come before us and at least told us that a particular free trade agreement would reduce the U.S. trade deficit, that it would not just create jobs and wealth in America, but it would create more jobs and wealth in America than it lost. Today things are different because now every published study shows that this agreement will cost us more jobs than it will create; cost us more wealth than it will create.

According to a report issued in April of this year by the Korean Institute for Industrial Economics and Trade, an entity that I know Ambassador Bhatia quotes in his report, if this deal moves forward, the United States trade deficit with South Korea will increase by about \$750 million per year for each of the next 10 years. Using numbers put forward by the Peterson Institute on International Economics, we see a similar picture. While they do not project out for as many years, they project an increase in the U.S. trade deficit of \$880 million.

I think Ambassador Bhatia said it very clearly when he was speaking in Korea and said, “From Chile to Singapore, the history of our free trade agreements is that the bilateral trade surpluses of our trading partners go up.” So there is no published report that

indicates anything other than while this agreement will create some jobs and wealth in America that it will cost us more.

But my focus here today in these hearings is not only that this agreement will have a devastating effect on America's working families, not only that it will add to the United States trade deficit but that it will transfer to the executive branch the power to decide whether goods manufactured in North Korea, and particularly in the processing zones of North Korea, enter the United States with this agreement providing additional benefits to those imports.

Now let me stipulate that the administration is made up of patriotic Americans dedicated to our nonproliferation policy, none more dedicated than Ambassador Hill. But each time the administration asks Congress to turn itself into a mere advisory body, they assure that that is a good result because after all, if the administration is exercising the power, they will do so in the patriotic interests of the United States.

Now exactly how will this agreement provide the administration with the power to provide benefits to North Korean exports? The key is these new trade zones or processing zones. The first of these trade zones alone is expected to ultimately employ over 1 million workers and house up to 3 million people.

In the words of the South Korean trade minister, this agreement leaves the possibility that any region in North Korea can be designated as a zone where products made there can be considered South Korean-made and eligible for the benefits of this agreement. So the South Korean people are being told that this agreement will help products created in those special zones. We in the United States are told the opposite. Where does the truth lie?

The truth lies in the text of the agreement, which states that any product that is produced in any part of Korea over which the South Koreans exercise sovereignty gets all of the benefits of this agreement. Where does the South Korean Government exercise sovereignty? According to its Constitution, the entire Korean Peninsula.

Moreover, North and South Korea can enter into agreements at any time to give some slight elements of sovereignty to the South over any of these processing zones. We can only look at Guantanamo or Ramstadt Air Force Base or Embassies here in Washington or illegally parked diplomatic cars down the street to know that different territory is subject to different kinds of sovereignty.

Under this agreement, the slightest scintilla of sovereignty granted by North Korea or acknowledged by North Korea over any portion of these processing zones will give the goods made there carte blanche entry into the United States.

We are about to consider a free trade agreement which is a highly unusual statute. You see, usually we in Congress write the laws. This time it is Ambassador Bhatia and his organization that will write the law, and they have a chance to write a clear one or to make it fuzzy and ask us to trust them.

I have put forward over here and sent to both of our witnesses yesterday, I wish I had done it a little earlier in the afternoon, and I do not expect you to have fully reviewed it, language that can be included in that statute to make it clear that only Congress can

allow goods produced in these zones to enter the United States with the benefits of this agreement.

I will know when you submit your draft to this Congress whether you intend to have clear language to accomplish that goal—this is clear language; I am sure you can draft even better language—or whether your reaction would be, we will leave it vague, but trust us. As an old lawyer, let me tell you the one time I want it in writing is when somebody tells me it does not need to be in writing.

So I look forward to seeing a clear agreement, not a statement that we should simply trust the administration to make the patriotic decision but rather a clear statement in the draft legislation that you submit to us that we cannot amend, which clearly states that this agreement is not as construed by the South Korean official that I quoted earlier.

With that, let me yield to the distinguished gentleman from Orange County, California, the ranking member of the subcommittee.

[The prepared statement of Mr. Sherman follows:]

PREPARED STATEMENT OF THE HONORABLE BRAD SHERMAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA, AND CHAIRMAN, SUBCOMMITTEE ON TERRORISM, NONPROLIFERATION, AND TRADE

I want to thank Ambassador Bhatia and Secretary Hill for joining us today as we look at specific aspects of the proposed U.S.—South Korea FTA.

As we look at this agreement, I am reminded of a certain lesson of history. On June 18, 1812, the United States declared war on Great Britain, and we made—what proved to be—a catastrophic foreign policy decision: We invaded Canada.

Our leaders mistakenly believed that the war would be an easy victory. They were wrong, and two months later we saw the fall of Detroit.

Today, we are not considering an invasion, but a trade agreement with one of our most important allies: South Korea. However, before we go forward with a proposal that the Bush Administration tells us will benefit both sides, we should be certain that we are not setting into motion a plan that will once again lead to the demise of Detroit.

Fundamental to answering these concerns is to ask how the U.S.—South Korea FTA will affect our trade deficit, which last year reached \$836 billion. Our imports world-wide for 2006 (\$1.8 trillion) were double the entire gross domestic product of South Korea. Unsurprisingly, we have a trade deficit with South Korea as we do with the vast majority of countries around the world.

As one of our witnesses, Ambassador Bhatia, recently pointed out, these types of agreements tend to grow our trade deficit. He is not alone in this assessment. According to a report issued in April of this year by the Korea Institute for Industrial Economics and Trade, if this deal moves forward our trade deficit with South Korea will grow by as much as \$750 million annually.

Using the numbers from a study done by the Peterson Institute on International Economics we see a similar picture in which our trade deficit with South Korea will grow by another \$880 million annually.

A full eighty percent of this trade imbalance comes from the auto industry, which brings us strait back to Detroit. Last year, South Korea exported 700,000 cars to the United States, more than 100 times what U.S. carmakers sold there.

We are told that there are some improvements to the barriers that U.S. automakers face, but they are not enough. Ford, Chrysler, and the United Auto Workers are all opposing this agreement because—in the words of a Ford Motor Vice President, “No manufacturer from any county can make significant gains in the Korean market.”

But I am not going to criticize our friends in South Korea. They are doing what most countries do: they are looking out for their own best interests and the interests of their own workers. However, our own trade officials should be doing the same, which clearly they are not.

The auto provisions are not the only issue that needs to be addressed. There is a Trojan Horse in this deal, which I believe will leave both sides unpleasantly surprised.

Unable or unwilling to make the tough decisions regarding outward processing zones in North Korea—like the one at Kaesong—the negotiators have sent us a deal that leaves too many unanswered questions.

This is not acceptable given the serious implications to our efforts to counter the North Korean nuclear weapons program. In October of last year, the North Korean regime tested a nuclear device. The response of the U.S. Trade Representative was to allow the inclusion of language in the US-South Korea FTA that paves the way for special treatment of goods produced in North Korea.

We are told not to worry because the name of the only currently existing outward processing zone, the Kaesong Industrial Complex in North Korea, doesn't actually appear in the text of the agreement. That rational is ridiculous.

This agreement establishes a committee whose composition and real powers are still unclear, but nevertheless has the authority to negotiate the terms of outward processing zones in North Korea.

These special zones will allow goods to be made in North Korea and be treated the exact same way as South Korean goods. We are not talking about a small exception. In the words of the South Korean trade minister this agreement leaves, "the possibility that any region in North Korea can be designated as a zone where products made there can be considered as South Korean-made."

How far-reaching could this be? The first of these trade zones alone is expected to ultimately employ upwards of one million workers and house up to three million people.

Additionally the text of the agreement leaves open another possibility: differing interpretations of the borders of South Korea. The FTA defines South Korea as the land, maritime, and air space over which the Republic of Korea exercises sovereignty. While I certainly welcome the day that North and South Korea are peacefully reunited into a single, free democratic country, I must question the peculiar way in which this was put together. How and by whom will the sovereign authority of South Korea be determined? South Korea's constitution says it extends to the Chinese border.

We have been told that all of these concerns will be addressed eventually. We are told that Congress will retain the authority to authorize the special treatment of goods in North Korea. We have received assurances from the Bush Administration that additional fixes can still be added to this FTA even though South Korean officials have publicly stated that Seoul is unwilling to reopen the agreement.

In order to codify these assurances I would suggest a clarification that we could have in the agreement or implementing legislation.

I want to be absolutely certain that no special trade privileges are extended to North Korea without Congress making the final determination.

I hope that the Administration witnesses will agree to the following:

"No good or service produced in whole, or in part, in the portion of the Korean Peninsula located north of the Korean War Armistice Line shall be eligible for the benefit of this agreement, unless such benefit is recommended by the Committee stipulated in Annex 22-c and thereafter authorized by a specific statute passed by the Congress."

Either this Free Trade Agreement does or does not allow special treatment for goods produced in North Korea.

There can be no maybe and no middle line.

The U.S. Congress must have the final word.

Mr. ROYCE. Thank you, Chairman. Thank you for yielding. I think I have a little bit of good news here because under this agreement, only Congress could allow inclusion of Kaesong goods in the United States. The concept here is a joint panel, a panel in which the United States and South Korea has representation. And if the United States disagrees with the inclusion of the importation of Kaesong industrial goods, which we are not going to do, it is not going to happen.

Mr. SHERMAN. Will the gentleman yield?

Mr. ROYCE. I am happy to yield to the gentleman. I am happy to yield on this moot point, but I will yield to the gentleman.

Mr. SHERMAN. Okay. I want to clarify remarks as to one thing. I know the agreement includes Annex 22-C, which contains a process which involves turning things over to Congress for ratification.

My opening statement was based on the assumption that while 22-C was probably negotiated in good faith, ultimately the administration will regard it as a convenient red herring. It will not use the 22-C process and rather will simply agree that Kaesong and other areas are areas in which the South Korean Government exercises sovereignty, and under the agreement in chief, the products can come into the United States. So I was not unmindful of the last sentence of Annex 22-C.

Mr. ROYCE. Well, reclaiming my time, Mr. Chairman, I think the red herring argument here more likely is the one that asserts that there is some way that the United States would allow goods from Kaesong, the industrial park, into the United States, into this country, because under this agreement as it is drafted now, you and I would have a vote on that.

Let us say for a minute what would never happen did happen and the administration decided to switch its position. At that point, you and I and everyone else—and I have written the administration twice on this point—would be heard from. There is no constituency in the United States for what you are suggesting. I just think that that point needs to be made.

What was agreed to here is a panel established to make recommendations on the possible inclusion of Kaesong goods. Any recommendation from this panel would require congressional approval. I do not think anyone seriously thinks the United States would accept goods coming in from North Korea.

Now this proposed free trade agreement with South Korea is the world's largest agreement of its kind. Given our significant trade with South Korea and even more importantly given our significant security relationship, this agreement deserves close attention.

Starting in 2000 and every year since, I have co-chaired the United States-Republic of Korea Interparliamentary Exchange. The exchange has always included a panel on trade whether we are in South Korea or here negotiating. And I have sat through many sessions in which we pressed national assembly members to open Korean markets. This FTA has achieved much of what we pushed for.

There is some dissatisfaction with the agreement's treatment of autos. South Korea has not lived up to previous agreements to end its discriminatory treatment of American-made cars, which has choked off United States sales in South Korea. The administration has now negotiated the elimination of most Korean tariffs on United States autos. It has also attached Seoul's non-tariff barriers, including with a new dispute mechanism backed by a punitive snap-back of United States tariffs on the 750,000 green cars sold in the United States should Seoul be found to be breaking the rules.

While sympathetic to those wanting more, calls to tie U.S. tariff rates to the sale of X number of United States cars to South Korean consumers would undermine trade. There is a fundamental difference between demanding fair access and demanding market share, which we have never done.

This agreement gives the United States beef industry an opportunity to retake the dominant position it held in South Korea in its import market in 2003 before mad cow disease. South Koreans I believe understand the need to apply science-based safety stand-

ards to United States imports. The beef issue, though, seems to take a new turn every day.

It is unfortunate that the United States could not dent South Korea's protection of its rice farmers. The main losers, though, are Korean consumers who continue paying four times the world market price for rice, just as American consumers lose out to our agricultural subsidies.

I was pleased that the Kaesong Industrial Complex made goods were excluded from this agreement's tariff benefits. As I mentioned, I have written the administration a number of times during the negotiations warning against their inclusion. It would have been indefensible to include goods produced under the wretched conditions of North Korea, directly benefiting its reckless and dangerous regime.

The State Department should go one step further, dissuading South Korea from expanding Kaesong. We should not bolster Pyongyang, including facilitating the release of its ill-gotten gains parked in Banco Delta Asia.

So, in summary, Mr. Chairman, I think although South Korea has agreed to a number of the points that we have been pushing, one of the questions for us is: Why did South Korea agree to this? I think South Korea entered the agreement to get more competitive. Having built its impressive prosperity through trade, South Korea now faces increasing competition from its neighbors, including some of the world's most economically vibrant economies.

Seoul has been liberalizing its economy at a quick pace essentially since its 1997 meltdown, but it knows it has to do more, gaining better access to the United States market but also freely accessing U.S. goods and services. This agreement does that, benefiting us, including many in my home state of California.

It is worth noting that Korean tariffs will be lowered far more than United States tariffs, which are already low. I think all of us should reflect on that point. The United States and South Korea have an important strategic relationship. United States troops are stationed on the Korean Peninsula for our mutual security. If we are honest, though, in some ways, this relationship has been off track. While this agreement appears popular in South Korea now, anti-Americanism has been rising for years, and I do not rule out the possibility of this FTA further stoking it as IMF-imposed reforms brought resentments against us back in 1998. There have been South Korean labor strikes against this agreement. The State Department should prepare outreach efforts to counter this opposition.

I look forward to hearing how this agreement will advance our economic and strategic interests from our witnesses here today, and I thank you very much, Mr. Chairman, for holding this hearing.

[The prepared statement of Mr. Royce follows:]

PREPARED STATEMENT OF THE HONORABLE EDWARD R. ROYCE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

The proposed free trade agreement with South Korea is the world's largest of its kind. Given our significant trade with South Korea, and even more significant security relationship, this agreement deserves close attention.

Starting in 2000, and every year since, I have co-chaired the U.S.-Republic of Korea Inter-parliamentary Exchange. The Exchange has always included a panel on trade. I've sat through many sessions in which we pressed National Assembly members to open Korean markets. This FTA has achieved much of what we've pushed for.

There is some dissatisfaction with this agreement's treatment of autos. South Korea hasn't lived-up to previous agreements to end its discriminatory treatment of American-made cars, which has choked off U.S. sales in South Korea. The Administration has now negotiated the elimination of most Korean tariffs on U.S. autos. It has also attacked Seoul's non-tariff barriers, including with a new dispute mechanism, backed by a punitive "snap-back" of U.S. tariffs on the 750,000 Korean cars sold in the U.S. should Seoul be found to be breaking the rules. While sympathetic to those wanting more, calls to tie U.S. tariff rates to the sale of X number of U.S. cars to South Korean consumers would undermine trade. There's a fundamental difference between demanding fair access and demanding market share, which we have never done.

This agreement gives the U.S. beef industry an opportunity to retake the dominant position it held in the South Korean import market in 2003, before mad cow disease. South Koreans, I believe, understand the need to apply science-based safety standards to U.S. beef imports. The beef issue though seems to take a new turn every day.

It is unfortunate that the U.S. couldn't dent South Korea's protection of its rice farmers. The main losers though are Korean consumers, who'll continue paying four times the world market price for rice, just as American consumers lose out to our agricultural subsidies.

I was pleased that the Kaesong Industrial Complex-made goods were excluded from this agreement's tariff benefits. I wrote the Administration a couple of times during the negotiations, warning against their inclusion. It would have been indefensible to include goods produced under the wretched conditions of North Korea, directly benefiting its reckless and dangerous regime. The State Department should go one step further: dissuading South Korea from expanding Kaesong. We shouldn't bolster Pyongyang, including facilitating the release of its ill-gotten gains parked in Banco Delta Asia.

South Korea has entered this agreement to get more competitive. Having built its impressive prosperity through trade, South Korea now faces increasing competition from its neighbors, some of the world's most economically vibrant economies. Seoul has been liberalizing its economy at a quick pace, especially since its 1997 meltdown, but it knows it has to do more, gaining better access to the U.S. market, but also more freely accessing U.S. goods and services. This agreement does that, benefiting us, including many in my home state of California. It's worth noting that Korean tariffs will be lowered far more than U.S. tariffs, which are already low.

The U.S. and South Korea have an important strategic relationship. U.S. troops are stationed on the Korean Peninsula for our mutual security. If we are honest though, in some ways this relationship has been off track. While this agreement appears popular in South Korea now, anti-Americanism has been rising for years, and I don't rule out the possibility of this FTA further stoking it, as IMF-imposed reforms brought resentment against us in 1998. There have been South Korean labor strikes against the agreement. The State Department should prepare outreach efforts to counter this opposition. I look forward to hearing how this agreement will advance our economic and strategic interests.

Mr. SHERMAN. Thank you. Let me now yield to the vice chair of this subcommittee, Mr. Scott.

Mr. SCOTT. Thank you very much, Mr. Chairman, and it is indeed a pleasure to join you in this very important hearing. Free trade is very important to the continued progress of the American and world economy, but I must state out front that I truly believe that this agreement is what I would refer to as a bad deal for the United States.

You know, many American industries have been negatively impacted by our failure to win concessions on labor standards in trade agreements, from steel to information technology services and even some textiles like Levi's jeans. No greater American name is there than Levi jeans. And to think that now we do not even have one plant in this country manufacturing and producing Levi jeans. In-

dustry after industry after industry has fled, literally fled this nation with whom we have open trade policies but who themselves have lax wage and labor standards.

Let me just pause for a moment because there is a reason why we are looked upon as the greatest country in the world. It is because we have a great and dynamic free economy, and the cornerstone of that economy has been our standard of living. And our standard of living in this cornerstone has been our wage and labor standards.

That is one of the reasons why people are willing to flock here, risk their lives to get here. Our immigration lines are just staggering with people wanting to get in this country because of our high standard of living, and our high standard of living is based upon very, very significant and important wage and labor standards.

The negative consequences of our one-sided trade agreements are no more evident than in my own congressional district in the state of Georgia where American automobile manufacturers such as Ford and General Motors have completely closed shop, completely closed shop.

And what makes matters worse and very intriguing and very revealing in this hearing is not only have Ford and General Motors closed their auto shops in Georgia, these factories have been replaced with Korean auto companies, Kia, but only after the state of Georgia bent over backwards to offer millions of dollars in tax breaks to locate there. That probably more than anything else points to the problem with this bill, with this trade agreement. We are certainly happy to have Kia in our state, but would not it be wonderful if we could have Kia in the state and Ford and General Motors?

I am concerned that if the United States-Korea free trade agreement is ratified as written, this scenario will be repeated over and over again in communities all across this country. Now this is not to say that the United States and Korea free trade agreement is completely all bad news. It is not. But as I said, it is a bad deal.

It would be a boon to Georgia's agriculture sector because our agribusiness is Georgia's economic engine, and I hope that this free trade agreement is amended so that perhaps I can at least think about voting for it and aid the expansion of this industry.

However, this agreement is a long way from being acceptable to me and I hope to many others, not only because of the auto industry's concerns mentioned above but because of the issues surrounding the outward economic zones and the Kaesong Industrial Complex. I fear that treating goods produced in the Kaesong Industrial Complex as though they come from South Korea will funnel hard currency to a government that is rapidly pursuing nuclear weapons technology.

In addition, this treatment could lead to the creation of other outward economic zones in the North and lead to further exploitation of the North labor force, which is not protected by strict labor rights. Thank you, Mr. Chairman.

Mr. SHERMAN. Thank you. Now let me yield to the former chair of the Small Business Committee, a man who I hope has similar views on the concept of fast-track as he does on the concept of this

free trade agreement, a gentleman who understands these trade issues. Mr. Manzullo.

Mr. MANZULLO. Thank you very much, Mr. Chairman, for calling this important hearing on the United States-Korea free trade agreement. I look forward to hearing about the details of the agreement, but at 11:00, I have to leave because we are engaged in negotiations with the Chinese on the Interparliamentary Exchange on opening markets there.

As the senior Republican of the Foreign Affairs Committee, Asia Pacific Subcommittee, I know that South Korea has proven itself over the years as a consistent friend and ally of America. The Korean Ambassador, Mr. Lee, graciously visited the congressional district I am proud to represent less than a month ago, toured key industries, and he also thanked our Korean War veterans for serving to protect his country almost five decades ago. He thanked them for making his country free.

As a strong supporter of free trade and fair trade, I have voted for every free trade agreement since being elected in 1992. I believe that the free trade agreement is a win-win for all countries involved. Advancing free trade agreements is better than the alternative, doing nothing or erecting barriers to imports. We should remember the lessons of the Great Depression. Higher tariffs do not protect jobs.

In fact higher trade barriers make the economy worse. Ninety-six percent of the world's consumers live outside the United States. We must embark on an aggressive trade agenda to tear down the remaining barriers to our exports to where the customers are located. That is why I was encouraged that the United States launched and successfully concluded a historic market opening agreement with South Korea, our seventh largest trading partner, the eleventh largest economy in the world. In 2006, United States exports to Korea reached a record \$32.5 billion, an increase of 17 percent. Illinois exports to Korea totaled \$631 million in 2006. Electronic products and machinery, products that are made in the 16th congressional district, were the top Illinois exports to South Korea.

The United States-Korea FTA would have a significant economic impact on both economies. There are many positive benefits in the agreement in the area of services, in particular, banking, insurance and express delivery, but there is a problem, a big problem, hopefully not a fatal problem. I do not think the agreement goes as far as I would like.

I am very disappointed that our negotiators did not leverage the FTA to prod more changes to the Korean auto market that have been subject to nationalistic pressure for years. I have heard many say that Koreans just do not like the vehicles that foreign manufacturers produce, that the United States in particular does not make vehicles that Koreans want.

I do not buy that argument. I know of at least one auto manufacturer in the U.S. that has done an excellent job of adapting to international market forces in the design of their vehicles. That company is Chrysler, located in my congressional district, and just spent \$.5 billion to upgrade to be a state-of-the-art auto manufacturing facility. It is located in Belvidere, Illinois. It is geared toward exporting. It was retooled with exports in mind.

The Chrysler plant is one of the precious few automotive manufacturers in the U.S. that produces right-hand drive vehicles for sale outside of North America. In 2005, roughly 18 percent of the vehicles produced at this plant were exported. In 2006, the Chrysler Belvidere plant began production of three of Chrysler's best-selling vehicles: The Caliber, the Dodge Caliber, Jeep Compass, and the Jeep Patriot, wonderful automobiles. The Koreans just love to drive them. They are just great cars. We would love to make more and sell them to Koreans.

Now the Belvidere plant exports over one-third of its production outside of the U.S., in my opinion, Chrysler did an excellent job responding to international market demand when they began production and sales of these best-selling vehicles.

Let me give you a concrete example of my frustration with this Korean free trade agreement particular to automobiles. In 2006, the Belvidere plant exported 222 of these top-selling vehicles to New Zealand where they drive on the left side of the road and only 102 to Korea. I have said 102 to Korea. This is astounding when taking into account that Korea's auto market is 10 times the size of New Zealand's.

In 2006, Korean auto manufacturers exported over 750,000 vehicles to the United States alone, 750,000. At the same time, the total of all foreign cars exported to Korea is only 37,000, less than 4 percent of the total Korean auto market. This is an issue not just affecting constituents I represent but every non-Korean automaker in the world.

While some of the barriers to U.S. automakers have been addressed in this FTA, many of the non-tariff barriers have been inadequately addressed or not addressed at all, specifically the inequality in tariff savings, engine displacement tax, environmental standards, self-certification of safety standards, insurance discrimination for foreign autos and the methodology for determining the rules of origin. I think we have got a problem here, folks, a big problem. Non-tariff barriers are nonsense. They are imposed for the very distinct purpose of keeping United States automobiles out of Korea, and they must go. And they were not addressed in this agreement. And I am one of the most ardent free traders in Congress. When I have problems with this, then you have really got a problem.

Because Korea has a well-documented history of imposing non-tariff barriers, the agreement contains the auto tariff snap-back provision. Unfortunately the 25 percent tariff on Korean trucks is not included in this provision and somewhat to the leverage that the United States has to ensure that Korea honors its auto agreement is gone. Additionally, the snap-back provision sunsets in 10 years. So even the limited leverage the U.S. retains to fight non-tariff barriers will be gone.

In light of these concerns, Ambassador Bhatia, I was extremely disappointed, very disappointed, overwhelmingly disappointed by your quote in the *National Journal* where you said, "I do not think there is more that needs to be done in reference to autos." Why do not you talk to me? Why do not you come to Congress or those of us that represent the auto industry that has been devastated by the loss of tens of thousands of jobs in the past 2 years?

I do not know who you are talking to, but you are certainly not talking to the representatives whose constituents are impacted by the fact that you have done nothing to penetrate the seal that Korea has placed around its country to not allow United States automobiles to come in.

Apparently the Koreans are thinking the same thing. This just came out last night and we hear it at 3 in the morning. South Korea will not accept United States auto revisions. It will break the deal. Senior South Korean officials said Wednesday that Seoul will not accept any potential United States proposals to significantly revise auto trade provisions in the two nations' pending bilateral free trade agreement. The Yonhap News Agency reported, "Renegotiation of auto provisions will not happen."

Lee Hye-min, South Korea's deputy chief negotiator in free trade talks with the United States, was quoted, telling SPS Radio, "The renegotiation would only clarify some language in the labor and environment provisions." And listen to this. This is great timing. This is wonderful diplomacy. "If the U.S. requests South Korea to revise auto provisions, it would break the balance of current negotiation results," Lee said.

Well, in that sense, where is the fulcrum, and where is the balance tipped? At this point, I have never seen a free trade agreement come under so much scrutiny not only from people who do not vote for free trade agreements traditionally but from among us free traders. These comments do not reflect the political reality here on Capitol Hill, and I fear they could be very unhelpful in seeing this agreement ratified.

The problem is this. Over the years, we have tried to mark down these non-market or these market barriers. We have been unsuccessful. Now if the Koreans were smart and they wanted this free trade agreement, they would have been showing due diligence and good faith over the past several years. But stubbornness and recalcitrance has replaced good common sense on the part of these good Korean people. And unfortunately our negotiators have not pushed far enough and deep enough in order to help out the U.S. automobile industry.

I can talk about beef cattle and the emphasis on Kaesong and other things in there, but I am just telling you, Ambassador Bhatia, this has got very, very serious problems, and you are going to get it from me continuously, because my congressional district in 1980 led the nation in unemployment at 25 percent as we were devastated. We lost 10,000 highly trained workers and hundreds of families.

We are just crawling back. We are just at the point now where we have invested hundreds of millions of dollars into that congressional district, with over 2,500 factories that are involved not only in automobile production but aerospace and other types of manufacturing.

I want the people in the congressional district that I represent to be proud of this agreement. I do not want to have them second-guess me that I did something to endanger especially the auto provisions of it. Hopefully you can work out the beef issue as I have 300,000 beef cattle in my congressional district also, including my very own small herd. So I look forward to the testimony. I look for-

ward, Ambassador Bhatia, to your going back and renegotiating this. I think we have got big problems. Ambassador Hill, thank you for being here. I know that you are in charge of that area of the world, though you did not do the negotiations, but you did a great job, a tremendous job.

Mr. SHERMAN. Thank you.

Mr. MANZULLO. [Inaudible.]

Mr. SHERMAN. Thank you. I did allow the gentleman from Illinois to go a bit beyond our usual time limit, but his district is so dramatically affected by this agreement that I thought it a good use of discretion.

Now the gentleman from Florida.

Mr. KLEIN. Thank you, Mr. Chairman, and thank you for having this hearing today. I certainly agree and acknowledge a number of the issues. I happen to represent Florida now, but I grew up in Ohio and certainly have a lot of understanding of some of the issues that have been brought forward. [Inaudible] South Korea's involvement in the Iranian energy sector.

Specifically, according to the Department of Energy, in September 2002, Iran signed a \$1.6 billion contract with South Korea's LG Construction to develop phases 9 and 10 of the South Pars gas fields. Multiple South Korean companies have planned deliveries of new oil tankers to the National Iranian Oil Company in 2008 and 2009, including Samsung H.I., which is producing three ships, Hyundai H.I., producing three ships, Hyundai Samho, producing eight ships, and Daewoo S.B., producing and delivering three ships. These are all oil tankers directly relating to Iranian energy sector.

I just believe it is very important in terms of the foreign policy of the United States and what we believe is in our best interest as well as many other countries around the world to deal with Iran in a very forceful way, and that is the purpose of the Iran Counterproliferation Act.

And we would hope that our friends and allies around the world, particularly ones who we are considering serious trade implications with, that these foreign policy implications are taken seriously, that these relationships with the energy sector in Iran are considered and managed in this trade policy and that we do not let South Korea undermine our national priorities. Iran is a dangerous regime, and its energy sector is fueling a nuclear program that could further destabilize the Middle East and have repercussions and consequences throughout the world.

So please, Mr. Ambassador, I appreciate you being here today, both of you, and I hope that as we go forward that these issues are not only considered but are part of any free trade discussions. Thank you, Mr. Chairman.

Mr. SHERMAN. I believe that is our last opening statement and was an excellent opening statement, and I hope those issues are addressed. I would now move to our first witness, knowing that the gentleman from Texas has indicated that he does not have an opening statement.

Ambassador Bhatia has served as Deputy U.S. Trade Representative since November 2005. In his current position, he is responsible for overseeing United States trade relations with East Asia and Southeast Asia. He also oversees U.S. Trade Representatives'

management of environmental and labor issues. I hope very much that you have an opportunity to tell us not just the process that this agreement lays out but the likely economic results, and not just the benefit in the terms of exports and jobs created but also netted against imports and jobs lost. Ambassador.

STATEMENT OF THE HONORABLE KARAN K. BHATIA, DEPUTY REPRESENTATIVE, OFFICE OF THE UNITED STATES TRADE REPRESENTATIVE

Ambassador BHATIA. Thank you very much, Mr. Chairman. Chairman Sherman, Ranking Member Royce, and distinguished committee members, I am delighted to be able to join the subcommittee today, together with my colleague, Ambassador Hill, to discuss the United States-Korea Free Trade Agreement, or KORUS FTA. I would like to offer my complete statement for the record.

Mr. SHERMAN. Without objection, both witnesses' statements will be entered in full in the record.

Ambassador BHATIA. Thank you. This is the most commercially significant free trade agreement the United States has implemented in nearly 15 years. The comprehensive trade agreement would eliminate tariffs and other barriers to trading goods and services, open South Korea's agricultural market, promote economic growth in both countries and strengthen ties between the United States and South Korea. Just as importantly, it would bolster one of the United States' most vital strategic relationships in an increasingly significant region of the world.

I will defer to Ambassador Hill to describe the geopolitical implications of the KORUS FTA and how the deal will serve to fortify the now 50-year-old alliance between the United States and South Korea, and I will focus my remarks on the economic and trade benefits of this historic agreement.

From an economic perspective, Mr. Chairman, the KORUS FTA offers us an opportunity to grow our already significant bilateral trade and investment relationship with one of the world's most diversified and most vibrant economies. It has been said that choosing an FTA partner is like choosing a business partner. And with its fast-growing, dynamic economy and industries and its creative people, South Korea is precisely the kind of business partner the United States needs.

Boasting an average annual growth rate of 4.6 percent over the past 6 years, South Korea is today the world's eleventh largest national economy, with a nominal GDP of nearly \$1 trillion. With approximately 49 million people, its per capita GDP last year was close to \$20,000. South Korea is today the world's thirteenth largest goods import market, our seventh largest goods trading partner and our seventh largest goods export market.

And it is also one of our fastest growing major trading partners, with the growth of United States goods exports to South Korea in 2006 at 17 percent and United States goods imports from South Korea growing, albeit at a substantially lower rate of 4.6 percent.

Now just to place that relationship in perspective, the \$78 billion in bilateral goods trade that we currently enjoy with South Korea is more than 70 percent of the total bilateral trade that we enjoy with all 10 trading partners with whom we have implemented

FTAs since 2000, approximately \$110 billion. And this is the case even though South Korea's current average tariff for industrial goods is 7 percent—ours is approximately 3.5 percent—and for agricultural products is 52 percent. Ours is approximately 12 percent. And those Korean numbers of course will decrease substantially under the FTA.

So now with this background in mind, allow me if you would to touch just a minute on a few of the many benefits that I think U.S. companies, U.S. farmers, U.S. service providers and above all U.S. workers will stand to gain from the KORUS FTA.

First, it would grant unprecedented access to the South Korean market. Under the agreement, nearly 95 percent of bilateral trade in consumer and industrial products becomes duty-free within 3 years of the agreement's entry into force, including key U.S. exports such as electronic machinery and parts, auto parts, power generation equipment, most chemicals and medical and scientific equipment.

U.S. farmers and ranchers, and, Congressman Scott, you obviously referenced the enormous benefit that Georgia will obtain in the agricultural sector from this FTA, but it is not limited to Georgia. It is nationwide. Our farmers and ranchers would benefit from the fact that more than half of current United States farm exports to South Korea, exports that currently face an average duty of 52 percent, will become duty-free immediately.

It contains an unprecedented package of provisions designed to ensure that United States automakers can compete in South Korea on a level playing field. Again, we can address this at greater length in the Q&A session, but the agreement would have the effect of immediately eliminating tariffs on United States automobiles, addressing the tariff barriers and requiring South Korea to address the non-tariff barriers that have precluded to date United States companies from gaining a greater share of the Korean market, including requiring Korea to overhaul its system for taxing cars based on engine displacement, addressing emissions standards.

And all of this would be backed up by an innovative and unprecedented dispute settlement process that will serve as a powerful deterrent to any violation of the FTA's auto-related provisions.

Moving on, it provides substantial benefits for U.S. investors by establishing a stable legal framework that will protect all forms of investment. U.S. service suppliers, as the ranking member has mentioned and Congressman Manzullo has mentioned, stand to gain significantly from this agreement.

Mr. SHERMAN. You are about a minute over. If you could just wrap up.

Ambassador BHATIA. Okay. In the area of intellectual property rights, Mr. Chairman, the agreement provides significantly enhanced standards for protection. So there are substantial gains throughout the FTA for American stakeholders.

You asked, Mr. Chairman, that I address the subject of benefits. I will point you to studies that have been done widely by everyone from the University of Michigan, the Institute of International Economics, many others, suggesting that the potential income gains to the U.S. economy from the KORUS FTA range from \$17 billion to

\$43 billion. It is of course no surprise that it has obtained the substantial support from a diverse set of stakeholders. Again, I point you to my written testimony.

Let me lastly in the time remaining then, Mr. Chairman, make reference to the importance of this agreement to our trade strategy in East Asia. I am happy to deal with this in questions, but I think it would be remiss for me not to point out that without the approval of this agreement, we will be substantially disadvantaged, Mr. Chairman, in our dealings with our trading partners throughout Asia, including strategically with many important competitors, China and others. Thank you.

[The prepared statement of Ambassador Bhatia follows:]

PREPARED STATEMENT OF THE HONORABLE KARAN K. BHATIA, DEPUTY REPRESENTATIVE, OFFICE OF THE UNITED STATES TRADE REPRESENTATIVE

INTRODUCTION

Chairman Sherman, Ranking Member Royce, and distinguished committee members, I am delighted to be able to join the Subcommittee today, together with my colleague Ambassador Hill, to discuss the United States-Korea Free Trade Agreement (or KORUS FTA).

On April 1, the United States and South Korea successfully concluded negotiations on the KORUS FTA, an agreement that if approved by Congress, would represent the most commercially significant FTA the U.S. has implemented in nearly 15 years. This comprehensive trade agreement would eliminate tariffs and other barriers to trade in goods and services, open South Korea's agriculture market, promote economic growth in both countries, and strengthen economic ties between the United States and South Korea. Just as importantly, the KORUS FTA would bolster one of the United States' most vital strategic relationships in an increasingly significant region of the world.

BENEFITS OF KORUS FTA

I will defer to Ambassador Hill to describe the geopolitical implications for the KORUS FTA and how the deal will serve to fortify the 50-year alliance between the United States and South Korea. I will focus my remarks today on the economic and trade benefits of this historic Agreement.

From an economic perspective, the KORUS FTA offers us an opportunity to grow our already significant bilateral trade and investment relationship with one of the world's most diversified and vibrant economies. It has been said that choosing an FTA partner is like choosing a business partner. With its fast-growing, dynamic economy and industries and its creative people, South Korea is precisely the kind of business partner America needs.

Boasting an average growth rate of 4.6 percent over the past six years, South Korea is the world's 11th largest national economy, with a nominal GDP of nearly \$1 trillion. With a population of approximately 49 million people, South Korea's per capita GDP last year was close to \$20,000. South Korea is today the world's 13th largest goods import market, the United States' seventh largest goods trading partner, and our seventh largest goods export market. Korea is also one of our faster growing major trading partners, with growth of U.S. goods exports to South Korea in 2006 at 17 percent and U.S. goods imports from South Korea at almost 4.6 percent.

Just to place that relationship in perspective, the \$78 billion in bilateral goods trade we currently have with South Korea is more than 70 percent of the total bilateral trade that we enjoy with all 10 trading partners with whom we have implemented FTAs since 2000 (\$110 billion). And, this is the case even though South Korea's current average tariff for industrial goods is seven percent and for agricultural products is 52 percent, numbers that will decrease substantially under the FTA.

With this background in mind, allow me to touch for a minute on just a few of the many benefits U.S. companies, workers, farmers, and service providers stand to gain from the KORUS FTA:

- The KORUS FTA would grant unprecedented access to the South Korean market. Under the Agreement, nearly 95% of bilateral trade in consumer and industrial products becomes duty-free within three years of the Agreement's entry into force, including key U.S. exports such as electronic machinery and

parts, auto parts, power generation equipment, most chemicals, and medical and scientific equipment.

- U.S. farmers and ranchers would benefit from the fact that more than half (or \$1.6 billion based on 2003–2005 numbers) of current U.S. farm exports to South Korea will become duty-free immediately, including high value agricultural products such as almonds, pistachios, wine, and cherries. For many other key agricultural goods, such as pork and citrus products, the KORUS FTA will provide unparalleled access to the South Korean market and its prosperous consumer base.
- The KORUS FTA contains an unprecedented package of provisions designed to ensure that U.S. automakers can compete in South Korea on a level playing field. Besides immediately eliminating tariffs on most U.S. priority automobiles, the Agreement would require South Korea to overhaul its system for taxing cars based on “engine displacement” by reducing existing tax rates and eliminating the discriminatory aspects of key taxes. In addition, the FTA addresses current emissions and automotive safety standards that U.S. industry has identified as priorities to ensure that technical standards do not preclude U.S. automotive manufacturers from accessing the South Korean market. Perhaps most significantly, U.S. automakers would be protected by an innovative and unprecedented dispute settlement process that will serve as a powerful deterrent against any violations of the FTA’s auto-related provisions. This enhanced dispute settlement process will cut in half the time for disputes to be addressed and includes a “snap-back” provision that will allow us to suspend our tariff concessions on South Korean imports of passenger cars if Korea is found to have violated, nullified, or impaired an auto-related FTA commitment.
- For U.S. investors operating in South Korea, the KORUS FTA establishes a stable legal framework that will protect all forms of investment. Under nearly all circumstances, U.S. investors will enjoy the right to establish, acquire, and operate investments in South Korea on equal footing with local investors, and investor protections will be backed by a transparent, binding international arbitration mechanism. In short, I believe it is fair to say that the investment protections in this Agreement are as strong as those in any U.S. FTA to date.
- U.S. services suppliers also stand to gain significantly from this Agreement. Korea has vastly improved upon its WTO commitments in this FTA, providing meaningful market access commitments across virtually all major services sectors. In particular, Korea provided greater and more secure access to international delivery services and charted a course for future reform of domestic delivery services. South Korea also made particular strides on legal services, opening up for the first time to foreign legal consulting.
- In the area of telecommunications services, U.S. suppliers will benefit from South Korea’s agreement to permit U.S.-controlled companies to own 100 percent of South Korean telecommunications operators within two years.
- The KORUS FTA goes further than any prior U.S. FTA in securing benefits for U.S. financial services providers in areas such as market access, transparency, and due process. In addition, South Korea has agreed under the FTA to begin the process to ensure that the same rules and regulations apply to Korea Post as apply to private insurers.
- In the area of intellectual property rights, the Agreement provides significantly enhanced standards for protection and enforcement of a broad range of intellectual property rights, including trademark-, copyright-, and patent-related provisions and will provide effective -protection and enforcement for emerging technologies.

Indeed, these are but a few of the many sectors in which benefits were secured for U.S. stakeholders in the course of the KORUS FTA negotiations. Substantial gains were also netted in areas including pharmaceuticals, electronic commerce, government procurement, standards, and competition. In addition, the Agreement will provide for important improvements in transparency and due process in South Korea, including through the most advanced transparency obligations in any U.S. FTA to date, which will benefit U.S. companies trading with South Korea across the board.

These benefits, and the many that I have not had time to provide details on here, will generate significantly improved market access for U.S. companies. Consequently, U.S. exports can be expected to grow appreciably as a result of the Agreement. And, studies published by the University of Michigan, the Institute of International Economics and the U.S. International Trade Commission, among others,

have estimated that the potential income gains to the U.S. economy from a KORUS FTA range from \$17 billion to \$43 billion.

With this in mind, it is important to note that the outcome of KORUS FTA negotiations has been roundly lauded by many business groups. Statements of support for this deal have come from a diverse set of stakeholders, from the National Association of Manufacturers to the Recording Industry Association of America, from the American Council of Life Insurers to the National Pork Producers Council, from the Coalition of Services Industries to the Electronics Industry Alliance—all of which embrace the enormous commercial potential of this Agreement and recognize its significance to American businesses, farmers, ranchers, and workers.

THE IMPORTANCE OF THE KORUS FTA TO THE U.S. COMMERCIAL POSITION IN EAST ASIA

Not only will U.S. stakeholders benefit from increased market access provided by the FTA, the Agreement is important to our trade position and strategy in East Asia as a whole. The FTA will offer American companies a preferential advantage vis-à-vis competitors in the South Korean market, at a time when many of our global competitors are actively seeking to “lock-up” East Asia’s fast growing economies into trading relationships that would exclude the United States. It is worth reflecting on this trend.

Today, there are some 19 free trade agreements in force among members of the Asia Pacific Economic Cooperation (APEC) forum, and many more either under negotiation or consideration across Asia.

- China already has an FTA with Association of Southeast Asian Nations (or ASEAN) that covers goods, and a comprehensive services FTA between the two parties will enter into force in July. In addition, the Chinese are actively negotiating or have proposed FTA discussions with South Korea, Japan, India, Australia, New Zealand, the GCC, Pakistan, and the South African Customs Union, among others.
- Japan has concluded FTAs with Singapore, Malaysia, and the Philippines, and is considering engagement with the major players within Asia, including South Korea.
- India has implemented FTAs with Thailand, Singapore, and Sri Lanka, and is actively entertaining discussions with the region’s larger economies.
- Demonstrating that the interest in establishing trade deals in Asia is not limited to the region itself, the EU launched FTA negotiations with South Korea on May 6, 2007 and is actively courting partners that include China, India, and ASEAN.
- We are witnessing efforts to construct an exclusive Asian regional free trade bloc—so-called ASEAN +3 or +6 arrangements.

A number of these FTAs unfortunately do not constitute high standard, comprehensive agreements of the type that the United States has negotiated. However, they do afford preferential trading positions to the companies of these countries and have the effect of placing U.S. businesses, workers, and farmers at a relative disadvantage in accessing fast-growing East Asian markets. This web of agreements also has the potential to encourage U.S. companies seeking to compete in these markets to relocate production to those countries.

Against this backdrop, the KORUS FTA takes on added significance. To date, the United States has concluded two FTAs in this critical region—with Singapore and Australia, important but smaller economies. A successful FTA with South Korea could provide an important boost to U.S. efforts to remain an active economic presence in a strategically vital region that last year accounted for over 37 percent of total world GDP, 26 percent of global trade flows, and 29 percent of U.S. exports. A KORUS FTA would establish a model that we believe could be replicated with other Asian economies and could help us expand trade liberalization throughout the region.

By contrast, any lessening of focus that results in our inability to complete agreements with major emerging-market economies like South Korea could have unfortunate consequences. It would likely result in a shift of the region’s attention away from strengthening their relationships with the United States to doing deals with other major trading partners.

CONCLUSION

Members of the Committee, I submit to you that we have reached an agreement with South Korea of great economic and political significance to our country. In the

next few weeks we plan to finalize and execute the Agreement, and in due course, submit it to Congress.

From an economic standpoint, the potential benefits of the KORUS FTA to America's workers, farmers, manufacturers, and service suppliers are undeniable. The KORUS FTA will certainly add to the track record of significant growth in U.S. exports and gains in U.S. export share produced by the United States' recent FTAs. Politically, successful implementation is further evidence that a U.S.-South Korea bilateral relationship once centered solely on defense has evolved into one of the most dynamic economic partnerships on the globe. The KORUS FTA is the next step in broadening and modernizing a strategic alliance with a critical ally that is a vital force for stability at a time of change and challenge on the Korean peninsula and in the broader Northeast Asia region.

Thank you.

Mr. SHERMAN. Secretary Hill, we will hear from you for 5 minutes. We will not count the Ambassador's 2½ minutes over against your time.

Ambassador BHATIA. Thank you.

STATEMENT OF THE HONORABLE CHRISTOPHER R. HILL, ASSISTANT SECRETARY, BUREAU OF EAST ASIAN AND PACIFIC AFFAIRS, U.S. DEPARTMENT OF STATE

Mr. HILL. Thank you very much, Mr. Chairman. It is a great pleasure to address this committee and to deal with some of the foreign policy implications of this United States-Korea Foreign Trade Agreement.

The United States's relationship with the Republic of Korea is changing and it is growing into a very mature, healthy and balanced partnership, and we believe one of the greatest examples of the strength of this relationship is precisely this recently concluded United States-Korea Free Trade Agreement.

While the agreement achieves many of our economic goals, it is important to note that the impact of this FTA will go far beyond bilateral commercial benefits. It is an agreement that will be a powerful symbol of our partnership with the Republic of Korea. It will augment our longstanding bilateral security alliance and the robust ties between our two peoples. It will create a new dynamic, reflecting both the growing sophistication of our relationship with the Republic of Korea's increasingly positive global role.

It will strengthen our relationship with one of our most important and reliable allies, serving as a pillar for our alliance in the 21st century as our mutual defense treaty did during the last half of the century. It will decisively anchor the U.S. presence in this most dynamic and rapidly growing economic region in the world.

I will let my colleague, Ambassador Bhatia, who oversaw the negotiation of this agreement, including through several sleepless nights in Seoul leading up to the April 1 conclusion, explain the benefits of the FTA for United States commercial interests and for our global trade liberalization strategy, and they are significant.

I will focus my remarks on the agreement's foreign policy implications. But, Mr. Chairman, before I do that, I have heard from a number of your colleagues a concern about United States autos, and I want to say that when I was serving in Korea as Ambassador and in fact in October 2004, a Chrysler representative came to me and asked if I would host a Chrysler auto show on the front lawn of the residence. And I made sure that other U.S. manufacturers

understood that if they wanted to do that, I would do the same for them.

And so I had several Chrysler models in front of the residence on the lawn. And we invited a lot of Korean press, a lot of prospective Korean buyers there. And in talking to them, the big problem they had with our cars were precisely problems created by their own government, taxes and tariffs, because they liked these Chrysler models. We had the 300M there. We had the Chrysler Cross-Fire, a couple of other models, unfortunately not the ones that Congressman Manzullo mentioned from his district. And there was a lot of interest in them. The problem was taxes and tariffs, and that is precisely the problem that this FTA will be able to deal with.

Let me get back to some of these foreign policy issues. First of all, this FTA will strengthen this partnership, and it will ensure that while we have long been very much focused on defense ties, we are going to maintain or make sure that this partnership continues in the future and is going to do it at a time of change and challenge on the Korean Peninsula and the broader Northeast Asian region, the concrete proof to Korea that we are committed to broadening and modernizing our alliance.

Over the years, our relationship with Korea has been tested in many ways, but I have always been optimistic about it because I have always seen the real benefits of a strong relationship between the U.S. and the ROK. The two countries are bound by shared interests, shared values, underpinning the long-term commitment of both our peoples to making this relationship work.

Korea is not just a regional power anymore. It is growing in global importance. Korean people are active all over the world. They are great travelers. They are students. They are tourists. They are diplomats, missionaries. Korean companies are major investors in many economies all over the world. And more and more our relationship with Korea is characterized as a multifaceted, cooperative partnership in the world.

Korea is the third largest contributor of troops to the forces in Iraq. It has played an important role in Afghanistan as well. And when Secretary Rice meets with her Korean counterpart, Foreign Minister Song Min-Soon, they talk not only about the issues on the Korean Peninsula but also about the Middle East, climate change, spread of democracy and other global interests.

We worked hard to modernize our security relationship in Korea. We have realigned our troops to make sure they are placed and equipped most intelligently to deter any thought of aggression, and I think we are doing that pretty effectively. We have worked very closely with the ROK in the Six-Party Talks to deal with the North Korea nuclear problem. If you have any questions about that, I would be happy to deal with that during this hearing.

I will say that this relationship, this core US-Korean FTA, strengthens our ties to a good friend. I had the privilege of serving in Korea in 1987 when the democracy movement sprang up. It is very heartening indeed to see what has happened to democracy in the Republic of Korea. It is really one of the strongest democracies in the region, and we want to stay very close.

It has a great story to tell in terms of its economy, and very importantly its economy has been spread to a very strong middle

class, good income distribution. So it is precisely the kind of economy that our goods and services I think can do very well in. So thank you very much, Mr. Chairman. I look forward to answering your questions and those of your colleagues.

[The prepared statement of Mr. Hill follows:]

PREPARED STATEMENT OF THE HONORABLE CHRISTOPHER R. HILL, ASSISTANT SECRETARY, BUREAU OF EAST ASIAN AND PACIFIC AFFAIRS, U.S. DEPARTMENT OF STATE

INTRODUCTION

The United States' relationship with South Korea is changing and growing. It is transforming into a mature, healthy and balanced partnership. One of the greatest examples of the dynamism in our bilateral relationship is the recently concluded United States-South Korea Free Trade Agreement (or KORUS FTA).

While the agreement achieves many of our economic goals, it is important to note that the impact of this FTA will go far beyond bilateral commercial benefits. The KORUS FTA is a powerful symbol of the U.S.-South Korea partnership, augmenting our longstanding bilateral security alliance and the robust ties between the South Korean and American people. It will create a new dynamic, reflecting both the growing sophistication of our relationship, and the Republic of Korea's (ROK) increasingly positive global role. It will strengthen our relations with one of our most important and reliable allies, serving as a pillar for the alliance in the 21st century as the mutual defense treaty did during the last half century. And it will decisively anchor the U.S. presence in the most dynamic and rapidly-growing economic region on the globe.

BENEFITS OF KORUS FTA

I'll let my colleague Karan Bhatia, who oversaw the negotiation of this historic agreement, including through several sleepless nights in Seoul leading up to our April 1 conclusion of the deal, explain the benefits of the KORUS FTA for U.S. commercial interests and our global trade liberalization strategy—which are significant. His familiarity with the details of the agreement far exceeds my own. Instead, I will focus my remarks on the agreement's foreign policy implications.

First, the KORUS FTA will strengthen the U.S.-South Korea partnership. It will help ensure that the U.S. partnership with South Korea, long centered on defense ties, remains a vital force for stability at a time of change and challenge on the Korean peninsula and in the broader Northeast Asian region. It will be concrete proof to South Korea that we are committed to broadening and modernizing our alliance.

Over the years, the U.S. relationship with South Korea has been tested in many ways. But I've always been optimistic about it, because I always have seen the real benefits of a strong relationship between the U.S. and the ROK. Our two countries are bound by shared interests and shared values, underpinning the long-term commitment of both Americans and Koreans to making the relationship work.

South Korea is a country that is not just a regional power, but it's growing in global importance. Korean people are active all over the world as students, diplomats and missionaries, and South Korean companies are major investors in many economies. More and more, our relationship with South Korea is growing to be a multi-faceted, cooperative partnership for a more closely knit world.

South Korea is the third-largest contributor of troops to the coalition forces in Iraq and has played an important role in Afghanistan as well. Nowadays when Secretary Rice meets with her ROK counterparts, they talk not just about the situation on the Peninsula, but also about the Middle East, climate change, the spread of democracy and other global issues of shared concern.

We've been working hard lately on modernizing our security relationship with South Korea. We are realigning our troops to make sure that they are placed and equipped most intelligently to deter any thought of aggression by North Korea. I think we're doing that very effectively.

We've also been working very closely with our friends from the ROK in the Six-Party Talks to deal with the issue of North Korea's nuclear program. Ultimately, as we move forward in the six-party process, it's very important that we move beyond denuclearization in North Korea to try to create stronger multilateral mechanisms for problem-solving in the region and for developing a greater sense of community in the region. I think in this regard, South Korean and U.S. interests are very much aligned.

Second, the KORUS FTA strengthens our ties to a good friend that has done good things. I had the privilege of serving in South Korea in 1987 and witnessed the flowering of democracy there. I then went back as Ambassador in 2004 to see what had happened since. It is really quite an inspiration for all of us who believe that democracy is the wave of the future. South Korea has shown the way and become an example for political reform in many parts of the world, especially in Asia.

The FTA will also provide a boost to the steady progress that South Korea has made on economic reform in the last decade. South Korea is one of the world's great success stories in terms of achieving broad prosperity through commitment to a market economy and openness to global trade. By liberating the vitality of its citizens and exposing them to international competition, South Korea has gone from being one of the world's poorest countries at the end of the Korean War to a vibrant democracy, a member of the OECD with a per-capita GDP approaching \$20,000. South Korea also has strong labor laws and environmental protections. All this makes South Korea an excellent trading partner for the United States.

Along with our expanding trade ties, I should also point out the very substantial people-to-people ties between our two countries. There are now over two million Americans of Korean descent living in the United States. They have had a huge positive impact on our country and continue to provide a vital and unique link between the two nations. U.S.-ROK academic ties have also blossomed; in 2006, more than 58,000 South Korean students studied in the U.S., and South Korean students are now the third largest group of foreign students in the U.S. The FTA has the potential to join our two countries together even more closely.

Third, the KORUS FTA will anchor our strategic economic position in East Asia. East Asia and the Pacific region are undergoing a wave of economic integration, with countries binding themselves closer together through steady progress in liberalization of trade and investment. Several plurilateral free trade agreements are in play, and some 19 free trade agreements have gone into force between Asia-Pacific Economic Cooperation (APEC) economies, with at least an equal number of future agreements under negotiation or exploration. The United States has participated as a leader via our gold-standard FTAs with Australia and Singapore. Ratification of the KORUS FTA will further cement U.S. leadership in the dynamic Asian region and debunk critics who falsely complain that we've neglected this part of the world.

South Korea, like the United States, has taken an aggressive approach toward binding trade liberalization. It has completed FTAs with Chile and the European Free Trade Area (EFTA) and is working on a second phase of negotiations with five of the ten ASEAN countries (having already completed a framework and trade in goods agreement). South Korea is also in the final stages of FTA negotiations with Canada, negotiating an agreement with India, just starting negotiations with the EU, and is studying the feasibility of launching an FTA with China. Negotiations with Japan have been on hold the last two years, but it is possible they could be revived. Thus, by ratifying the KORUS FTA, our firms will enjoy a competitive advantage in South Korea—Asia's third-largest economy—ahead of others. On the other hand, if we fail to ratify, we will not just stand still, we will move backwards.

Fourth, and finally, the KORUS FTA will give impetus to global trade liberalization: By demonstrating that two large, advanced economies can conclude a high-quality agreement eliminating both tariff and non-tariff barriers to trade and investment, the KORUS FTA could help spur further trade liberalization both within the Asia-Pacific region and globally. It will send a signal to our other trading partners, encouraging them to open their economies and creating a competitive dynamic that would spur more rapid progress on the multilateral trade liberalization front.

CONCLUSION

The impact of this FTA will go far beyond bilateral commercial benefits. It is a powerful symbol of the U.S.-South Korea partnership, augmenting our longstanding bilateral security alliance and the robust ties between the South Korean and American people. It will create a new dynamic, reflecting both the growing sophistication of our bilateral relationship and the Republic of Korea's increasingly positive role in the world.

Thank you for the opportunity to appear before the Subcommittee. I am happy to answer your questions.

Mr. SHERMAN. Ambassador, your presentation was enlightening in one respect you may not have intended. I have often said that our State Department and even its very brightest and most capable people are less attuned to trade issues than the foreign ministries

of other governments. Perhaps you did not realize that that Cross-Fire that you displayed was over 90 percent European-made.

Clearly it is to the benefit of the Daimler-Chrysler company that they sell such cars in Europe, but I assure that no European ambassador would have had a 90 percent American-made car on the front lawn of their Embassy. I hope that our State Department becomes more attuned to the trade balance.

And, Mr. Bhatia, or Ambassador Bhatia, is there a single published study that says that the free trade agreement with South Korea will lead to a diminution in the net United States-South Korea trade deficit? That was a yes or no question.

Ambassador BHATIA. Mr. Chairman, it is impossible, it is impossible to prior to an FTA going into effect make any assessment as to whether deficits will increase or decrease.

Mr. SHERMAN. The Korean ministry that you cite in your testimony has undertaken to do exactly that.

Ambassador BHATIA. No, Mr. Chairman.

Mr. SHERMAN. They did not predict a roughly \$750 million increase in the trade deficit over the next 10 years?

Ambassador BHATIA. Mr. Chairman, I am not going to make assessments as to who has said what. What I am telling you is that what the theory of the FTA is as you well know is to lower barriers, tariff and non-tariff barriers, on both sides. That is what this agreement does. It does it by addressing that Korean tariffs happen to be much higher than ours.

Mr. SHERMAN. Sir, I am going to reclaim my time. I simply asked you whether there were any published studies. You told me that there are none, and you have tried to say that there could be none.

I would say, especially all of us in Congress say, that we ought to run government more like a business. I cannot imagine coming into a business boardroom and saying this is the deal. We do not know whether it is going to cost us money or make us money. Let us sign on the dotted line because it is a good process.

But let us focus now on how the agreement has the loophole to allow this Trojan horse of North Korean-made goods come into the United States. You are very familiar with this agreement. So there is the Annex 22-C process. But assume long before the committee even meets, long before 22-C becomes operative in any way the North Korean Government grants a few scintillas of sovereignty over the Kaesong acreage to the South Korean Government.

At that point, if the administration in its own wisdom without consulting Congress of course decides that that constitutes South Korean sovereignty over that acreage, are those goods entitled to entry into the United States under this agreement?

Ambassador BHATIA. Mr. Chairman, the issue is very simple. There is no coverage of North Korean goods in this agreement.

Mr. SHERMAN. Does not the agreement clearly state that whatever part of Korea where the South Korean Government exercises sovereignty, those goods can come into the United States, or are you denying that those words are in the agreement?

Ambassador BHATIA. I am making clear that what the agreement provides under the rules of origin, which is Chapter 6, which is consistent with all of the other FTAs that we have done, is that—

Mr. SHERMAN. Excuse me, sir. But this FTA is with a country that claims constitutionally to exercise control over the entire Korean Peninsula. None of our other FTA partners claim constitutional authority over territory ruled by an axis of evil power.

Ambassador BHATIA. Perhaps, Mr. Chairman, it would help if I could point you to Footnote 2 in Chapter 6 of the FTA, which makes quite clear that “a natural person who is domiciled in the area north of the military demarcation line on the Korean Peninsula shall not be entitled to benefits under this agreement.”

Mr. SHERMAN. Okay. So it has to be made by a South Korean company. Now you said a person, the person doing the exporting is the corporation, and that is a South Korean corporation operating. The person is the exporter, not the worker.

Ambassador BHATIA. This is what I am trying to get to, and perhaps I could just finish the explanation. The good needs to comply with standards’ rule of origin, which means that it is produced in the territory of South Korea, in South Korea.

Mr. SHERMAN. The territory of South Korea?

Ambassador BHATIA. It is clearly established. It clearly understood under international the territory of South Korea is what we currently consider the territory of South Korea. It is not Kaesong. It is not north of it. And indeed, Mr. Chairman, I would suggest that the remarks that you have quoted from the trade ministers recognize, explicitly recognize, that the products have to be made in South Korea. That is standard international practice, standard trade law. I really would submit to you, Mr. Chairman, there is not an issue here.

Mr. SHERMAN. Could you address how the definition of what is South Korea would be altered by slight changes in who exercises authority in various elements of sovereignty over the acreage in Kaesong? You have simply assumed that the armistice line is the upper limit or the northern limit of what could ever be South Korean sovereignty. In doing so, you have twisted the agreement and ignored the South Korean Constitution.

Ambassador BHATIA. I would respectfully submit not, Mr. Chairman. You are hypothesizing a situation in which basically territorial boundaries as we currently understand them disappear or move somehow, and that is not what is contemplated by the parties. It is clearly not what a dispute settlement panel would contemplate.

Believe me, Mr. Chairman, we are as sensitive to this issue as anybody for the reasons that Ranking Member Royce mentioned. It is not our intention, as clearly laid out in this agreement, to benefit them. There is not a loophole here, I am quite confident.

Mr. SHERMAN. Let me just end by saying you have drafted an agreement with a loophole that you could drive a Trojan horse through. This is the loophole plug. You can take your hand at drafting another one. When you draft the statute, you either have a plug for this loophole or you will say, oh, it is unnecessary. And when someone asserts that they do not have to put something in writing, clearly and absolutely that is when it needs to be in writing.

With that, let me yield to Mr. Royce.

Mr. ROYCE. Thank you, Mr. Chairman. Again, it seems to me that Congress would have to approve any panel recommendation. And again, I think it is worth noting that Korean tariffs will be lowered far more than United States tariffs, which are already low. We need to keep that in mind.

I was going to ask Deputy Trade Representative Bhatia some have called for the renegotiation of parts of this agreement. Last week the South Korean Foreign Minister said that renegotiation was impossible.

Ambassador BHATIA. Thank you, Ranking Member, and I certainly concur with both of your initial points. Under Annex 22-C, clearly any inclusion of outward processing zones or goods will require reapproaching Congress, coming back in the event that that would ultimately occur. And I very much agree that balance of the benefits here in terms of tariff reduction favors the United States simply given where Korea's tariffs are versus where ours are.

With respect to the issue of renegotiation, the comments that were being made that you were pointing to I think refer largely to changes to labor and environmental provisions in the agreement. Again, to put this in broader context, there was, as you know, Congressman Royce, a bilateral, a bipartisan, excuse me, agreement reached between House Democrats, House Republicans and members of the Senate that really crafts a new way forward for trade agreements, including the Korea trade agreement.

And so we have approached our Korean counterparts, explaining to them that with this new bipartisan agreement, there is the opportunity to capture great bipartisan support we believe for the Korea FTA. The Korean Government has indicated that they are not looking to reopen, by which we mean change substantive balance of benefits terms, market access terms.

We do believe that in due course, when we are able to present them text of labor/environmental provisions, they will appreciate that there is not a change in the balance of the benefits here and that we will be able to secure those provisions.

Mr. ROYCE. There is going to be an International Trade Commission study on this issue of economic advantages.

Ambassador BHATIA. Absolutely. Absolutely.

Mr. ROYCE. Let me shift off of this question of the free trade agreement onto another subject that has nothing to do with the free trade agreement. I will go over to Assistant Secretary Hill. You and I differ for one on facilitating the return to North Korea of the \$25 million in Banco Delta Asia. I want to focus on North Korea's so-called legitimate activities that has a lot to do with the Kaesong Industrial Complex, which I do not think is impacted by this agreement at all.

But Kaesong and [inaudible] and these other projects, these other [inaudible] which we know is one of the most repressed Mt. Kumgang one that appears to many to be determined to advance its nuclear weapons program despite your efforts. As you know, the North Korean Government derives hard currency from that project, leases and fees, surcharges, levies on North Korean wages which are paid. The North Korean Government is repaid basically in hard currency.

So the government is the beneficiary of a large part of the payments. Kaesong is a hard currency generator for the North Korean regime. I was going to ask you if you view that as a concern or not.

Mr. HILL. Well, certainly the purpose of Kaesong from the South Korean or the Republic of Korea perspective is to try to introduce some modern concepts into North Korea, get some North Korean factory workers used to dealing in a modern international style factory. To be sure, the workers are paid at a level that is far less than workers in South Korea working in South Korean factories.

Mr. ROYCE. I understand the Korean perspective on this.

Mr. HILL. Yes.

Mr. ROYCE. But these facilities are going to be vastly expanded if certain factions of South Korea have their way. And from our perspective, from our perspective, given the fact that the hard currency goes into a regime which makes its foremost purpose its military preparations, buildup, at least from the factors that I know, should not that be a concern from our perspective?

Mr. HILL. I think we need to monitor overall what the accrual of money is to the North Koreans. So far it has been pretty small. I mean, we are talking about essentially a pilot program. And increasingly the South Koreans have negotiated where the money is paid directly to the workers, which has been another concern of ours.

Certainly we have to monitor how the expansion of it could contribute to North Korea's military strength, but for now, I think what the project is really doing is introducing some very much needed reforms and an element of new thinking into the country. Bear in mind, it is in one small place. It is essentially an industrial park right now.

Mr. ROYCE. It is. It is. But the goal is to make it huge. And it is not in this trade agreement, but the reason it is in trade agreements with Singapore and so forth, South Korea is negotiating, is to try to build that thing up, that complex up. What I am sharing with you is that this is one of the few ways in which that regime has the currency to continue its armament buildup of missiles, of R&D for missiles, of nuclear weapons. And should our other efforts fail to constrain that, this source of revenue is what I am most concerned about, the revenue that the regime uses for ends which are definitely not going to be in our interest.

Mr. HILL. I understand, and I think we need to continue to monitor that. Absolutely.

Mr. ROYCE. Thank you. That is all.

Mr. SHERMAN. I yield to the vice chair of the subcommittee, Mr. Scott.

Mr. SCOTT. Thank you very much. I guess my line of questioning is probably on two tracks. First of all, Ambassador, I guess what concerns me is the fact that last year South Korea exported 700,000 automobiles into the United States, and last year United States auto companies exported just 5,000 into South Korea. What do you say about that?

Ambassador BHATIA. Congressman, it is because that is the challenge that our auto companies face. With or without this FTA, South Korea is going to export not 700,000 but 800,000 or more cars into the United States. Right now we have a 2½ percent tariff

on cars. It is not slowing down Korean exports into the United States or anywhere else.

What our auto companies want to do and I believe desire to do and should do is break into foreign markets, and that is what FTAs generally should allow it to do, and that is in particular what this FTA allows it to do.

By breaking down the tariff, by taking the tariff from 8 percent down to zero, and by eliminating each of the non-tariff barriers that our auto companies have identified for us, be it discriminatory taxes, be it emissions standards that differ from our own, be it a process's lack of transparency in the Korean process, and this FTA, and we at USTR have been working these issues for many years, have systematically gone through, identified what those barriers are and have addressed them in this FTA.

And if Korea does not live up to its obligations, we have the right to come back with this snap-back tariff after an expedited dispute settlement process is 6 months, put back into place the 2½ percent tariff, which last year would have amounted to \$250 million without a cure period, which is a very, very powerful disincentive.

So the question is when you asked me what do I say about that, I say we have got to get our 5,000 cars up. We want to see GM factories and plants in your district and everywhere else, but we have got to do that by breaking down the barriers in the foreign market because we are not closing off our market. We are not doing it right now. We are not going to.

Mr. SCOTT. You think that the tariffs is a way to do that. Let us review these tariffs for a moment. Under this plan, the United States will immediately eliminate its 2.5 tariffs on the vast majority of Korean-produced vehicles and auto parts, correct?

Ambassador BHATIA. Yes, it would. If you effectively look at it, there are three categories of cars based on liter size. Two of the three categories—

Mr. SCOTT. I regret that my 5 minutes, Mr. Chairman [inaudible].

Ambassador BHATIA. Sorry. Okay. Effectively it would eliminate within 3 years.

Mr. SCOTT. The 2.5 tariff on autos over 3,000 cc's would be phased out over 3 years?

Ambassador BHATIA. Exactly.

Mr. SCOTT. And the 25 percent U.S. tariff on light trucks will be phased out over 10 years?

Ambassador BHATIA. That is correct.

Mr. SCOTT. And Korea will immediately eliminate its 8 percent tariff on autos and its 10 percent on trucks?

Ambassador BHATIA. That is correct, sir. Yes.

Mr. SCOTT. Well, here is the rub in all of this. The reductions in the United States tariffs will trigger a surge in automotive imports from Korea. You understand that?

Ambassador BHATIA. Congressman Scott, I actually think most analysts project that given the way Korean auto production is looking going forward, in reality, over the course of the next year or 2, you will see a substantial probably diminution in the balance of their sales here that come from imports. They are moving production to Georgia and to Alabama.

Mr. SCOTT. The tariff arrangement makes it relatively easy for Korean automakers to ramp up production for exports to the United States?

Ambassador BHATIA. No. With due respect, Congressman Scott, the Korean production plan is clearly to produce substantially more here in the United States. So they have opened the factory—

Mr. SCOTT. But answer this question for me then.

Ambassador BHATIA. Yes.

Mr. SCOTT. Why did the Government of Korea state that it expects this proposed free trade agreement to generate over \$1 billion in annual increase in its auto trade surplus with the United States?

Ambassador BHATIA. Because there will be tariff savings, Congressman, based on the cars right now coming in to, I do not know the reason, but I would speculate that it may be because there are tariff savings that are derived from the reduction of the 2.5 percent tariff.

Mr. SCOTT. Given all this lopsidedness, given the 700,000 versus the 5,000, which accounted for over 87 percent of the overall \$13.4 billion United States trade deficit with Korea was our automobiles?

Ambassador BHATIA. Yes.

Mr. SCOTT. Given all of this, given this imbalance, why does this free trade agreement not contain any guarantees or mechanisms for the United States to gain substantially greater access to the Korean auto market? I mean, there is one glaring need, and it is not even here.

Ambassador BHATIA. Again, with all due respect, Congressman Scott, I have to disagree. I think this agreement as I have described contains mechanism after mechanism that addresses non-tariff barriers as well as the tariff issues that will break down. So you have got the 700,000 versus 5,000 number. That is exactly right. The way to change that balance is by breaking down those non-tariff barriers, which is precisely what this agreement does, and have a unique mechanism to make sure that those commitments are lived up to.

Mr. SCOTT. There is nothing in this agreement that requires Korea to open its markets to United States-built automobile [inaudible] before it could receive the benefit of reductions in our U.S. automotive tariffs. There is nothing here, and that is the rub.

I know my time is up, but I want to go to my other point, the Kaesong area, Mr. Hill. And I have a great concern that this pilot program would benefit North Korea's economy, in turn benefit the North Korean [inaudible]. Their whole major possibility of exports evolves around their nuclear capacity. [Inaudible], especially in relationship to Iran and that relationship. Now is not it a fact that this Kaesong project employs 11,000 North Koreans?

Mr. SHERMAN. That will have to be the last question.

Mr. HILL. Yes, it does. It is actually about 13,000 average wages, with overtime around \$67. The government takes upwards of 30 percent of that for various social benefits.

Mr. SCOTT. Thank you.

Mr. SHERMAN. I would point out that the choice is not just between continuing our unequal tariff relationship now or this free trade agreement. We also have the prospect if we do not enter this

free trade agreement of using the prospects of higher U.S. tariffs to negotiate a real fair trade agreement.

With that, I would like to call on the gentleman from Illinois, Mr. Manzullo.

Mr. MANZULLO. Thank you very much. First of all, I want to publicly commend Korea for sending Ambassador Lee to the United States. I had the opportunity to be with him two or three times. He does an outstanding job representing the people of Korea. He is open and is willing to be transparent. I cannot think of a finer diplomat to represent Korea than Ambassador Lee, and the least I can do is to publicly thank him. He is listening, and he knows that I am not blaming these problems on him. He realizes that there are difficulties. He has always had an open door.

Ambassador Bhatia, I just want to share with you the closed door that your office has had with mine. We have e-mailed you on several occasions. We have asked you to come in. Your staff has stonewalled us.

And I just cannot think of anything worse that your office can do than to have zero relations with the United States Congress, especially knowing that Chrysler plant is located in my district. You might want to take a look at the members of your staff that stonewalled a United States Congressman who requested your presence [inaudible] with you. This is extremely serious. I just want you to be aware of it.

The third thing is the question is Koreans continue to come up with non-tariff barriers. I just want to throw this out because it is typical of what you did not address. The Korean Insurance Commission just decided to stop providing insurance for two-seater sports cars. Of course, Koreans do not make such cars. This was done for the specific purpose of hurting imports.

I mean, that is stupid to get rid of something like that, and that is why the level of frustration is at code red here today. I mean, do not you believe that all of Korea's non-tariff barriers can be eliminated to allow for fair and open trade in autos when Korea has ignored two previous auto MOUs with the United States?

Ambassador BHATIA. Congressman, first of all, if I could address the point of visiting with your office. I apologize that apparently requests have not been responded to. I can assure you first of all that I did not know of any requests, and I am more than happy to come up and visit with you, whatever your convenience is.

I would say that we have done extensive outreach to Members of Congress with an interest in the automotive sector as well as other areas. I can mention that I have met with Congressman Levin, Congressman Camp, Congressman Walberg, Congressman Knollenberg, Congressman Ryan, Senator Stabenow, throughout this process. I continue to engage in conversations with members as well as other stakeholders of interest. I do apologize that we have not been in to visit with you, but I look forward to rectifying that in the very, very near future.

If I can, Congressman, address the issue of non-tariff barriers generally. USTR, as you know, has been at the forefront of trying to break down both tariff and non-tariff barriers into the Korean market now for 20 years. Those non-tariff barriers, and the indus-

try has identified these to us, fall principally into three or four categories.

Leaving aside tariffs, which are high in and of themselves, the non-tariff barriers include taxes based on engine displacement size. Where our larger tariffs are subject to progressively higher taxes, domestic taxes, in Korea, this FTA equalizes that. This FTA puts us on a level playing field with over 90 percent of the cars that are sold in Korea. So that is addressed.

Secondly, it deals with standards, principally emissions standards.

Mr. MANZULLO. This says sports cars. [Inaudible] exactly?

Ambassador BHATIA. No. Congressman, I am not familiar with the sports car issue. The insurance rate issue I have some familiarity with. Two points on that. One is to the extent private companies are setting insurance rates, obviously that is neither the government's business here nor in Korea. To the extent there is government involvement, to the extent there is governmental involvement here, without this FTA, we have no ability to address those problems in Korea. With this FTA, we have the ability to stop them from doing it.

Mr. MANZULLO. The problem I have with it, you come in with the promises that say just give us this agreement and we have a resolution dispute panel. Well, the time to resolve this is before we sign the FTA.

Ambassador BHATIA. I absolutely agree, Congressman, that the time to resolve this is from now on. But my point is with this dispute settlement system, which is unique, which we have never done before, which creates a hammer out there of two—if you look at last year's tariffs paid, \$250 million that if Korea does not honor its commitments, its tariff, non-tariff, any auto-related commitments in this FTA, we have an expedited dispute settlement process if we win that tariff snap-back into place.

Mr. MANZULLO. If they have not honored anything in the past 20 years, what makes you think they are going to change their mind now?

Ambassador BHATIA. Because we have a binding legal agreement.

Mr. MANZULLO. That has nothing to do with it. You enter into these free trade agreements on good faith. Just because you have something that is binding, can United States insurance companies do business, auto insurance do business in Korea? Have you allowed that?

Ambassador BHATIA. Absolutely. The insurance area and the services area perhaps is one of the biggest breakthroughs in this FTA where U.S. companies are going to have substantially more penetration.

But if I could perhaps give one message to the Congressman, I mean, I am just quoting from an objective report that has been filed by one of our leading auto companies with us and in turn made public. I will just quote one sentence: "General Motors believes"——

Mr. WU. Apparently you have no significant issues with engaging in hand-to-hand combat with folks up here on the dais, and I am going to permit the chairman to continue that combat in a moment.

You know, one of the concerns I have with the overall thematic foreign policy, laying aside whether this administration has adequately consulted Congress or any other branch of government on significant issues in the last 6 years or not, laying that issue aside, when you have a certain belief system about what the facts on the ground are and do insufficient investigation of what the facts indeed are, if you guess right, things are okay. But if you let ideology override the facts on the ground, you do not just get the administration into trouble. You get the whole country into a mess. And that has been in my view a problem.

What I see in the language on the chart over here is from my perspective reasonable language which takes care of a problem which the chairman has identified. You can correct my view of history if you wish in your further conversations with the chairman, but it is my recollection that there are still some shall we say conflicting claims with respect to the Korean Peninsula, and the chairman has put a finger on that. I am otherwise sympathetic, perhaps more sympathetic to this agreement than others, because we are dealing with a democracy, a relatively prosperous democracy with respect for the rule of law. But I find it extremely puzzling. I find your resistance to accepting reasonable language extremely puzzling, and I hope that it is not a continuation of the pattern of the triumph of ideology over facts on the ground that I have seen in other arenas the last 6 years.

With that, I yield the balance of my time to the chairman.

Mr. SHERMAN. I thank the gentleman from Oregon for his generosity. Mr. Bhatia, where in the agreement is there anything that prohibits or limits South Korean investment or loans to Iran? Is there any such provision in the agreement?

Ambassador BHATIA. Prohibitions on what foreign governments may or may not do like that do not fall into the scope of our FTAs.

Mr. SHERMAN. The answer is it is not there. I just referenced Mr. Klein's opening statement. I think it was an excellent statement. Congress is moving toward what should be a better foreign policy for the United States, which is that our free trade agreements include such prohibitions. And it is at least of concern that no effort was made or at least no successful effort was made to deal with the Iran issue in this FTA.

Moving to the Kaesong issue, as I have said, I think that by redefining sovereignty, that is the chief way in which the administration should it choose this will allow North Korean goods to come into the United States. My friend, Mr. Royce, says that the sole way that Kaesong and other processing zone goods would come into the United States is through Annex 22-C, which lays out a process. So let us look at that process.

Section 5 thereof says that after the committee acts, each government will seek legislative approval. Does this mean that if goods are going to come in pursuant to 22-C that you would need Congress to pass a statute authorizing it, or does it mean instead that you could simply notify Congress of your intention to take action and see whether Congress passes a statute prohibiting it?

Ambassador BHATIA. No.

Mr. SHERMAN. To the former, latter or something else?

Ambassador BHATIA. Effectively the latter. I mean, it contemplates—excuse me, the former. I think it is the former based on my memory what you are describing. It would contemplate that changes in rules of origin that would be needed to effectively allow goods from Kaesong or any other outward processing zone would require us to come back and seek legislation from the Hill.

Mr. SHERMAN. So you would need legislation and you would not simply give notice to Congress and ask us to disapprove?

Ambassador BHATIA. No, that is not what we contemplate.

Mr. SHERMAN. Needless to say, the drafting here would allow some successor of yours to take a different position, which is why I at least had to get you on the record here.

Mr. ROYCE. Mr. Chairman, if you would yield for a minute?

Mr. SHERMAN. I yield for a minute.

Mr. ROYCE. You understand I feel this is a moot point, but if you would like, the two of us could write a letter to that effect for legislative intent and we can get this issue off the table.

Mr. WU. Reclaiming my time, I would be much more impressed if the administration were to put it in writing.

Mr. SHERMAN. Yes. Well, we would like a letter from the USTR and the Secretary of State addressing this issue, defining what the words “seeking legislative approval” mean in Section 5 of Annex 22-C and also commenting upon whether such legislative approval is an absolute necessary precursor for whether any goods can come in under the 22-C process, because I could see the administration taking the position that says, well, we are responsible for seeking legislative approval, we will go seek it. In the meantime, we will let the goods in. So we will need something on timing and something on whether it requires an act of Congress.

So I now turn to the gentleman. I believe the next on the list is the gentleman from Texas.

Mr. POE. Thank you, Mr. Chairman.

Ambassador BHATIA. Thank you.

Mr. POE. I represent probably the largest refinery area in the southeast, southeast Texas. What land we do not have refineries on we grow rice. This portion of Texas used to have 600,000 acres of rice, long-grain rice. That was 25 years ago. Now our rice fields are down to 200,000. The number one problem is markets. I am a free trader. I believe in it. But as things would happen, long-grain rice from Texas, the number one market used to be Cuba and then Iran and then Iraq.

[Laughter.]

Mr. POE. We all know what has happened. We do not really trade with those people anymore, and then when we were selling rice, getting rice for Iraq, the government for some reason was buying it from Vietnam. So rice farmers, they would just like some markets. And this free trade agreement, we deal with avocados and sunflower seeds and lemons, but we do not deal with rice, and that concerns me because it is not free trade for rice.

Rice is an exception because it is better for South Korea to have a quota than it is for the United States to be able to go into that market and compete on the world scale, and I want to know why. What do I tell the rice farmers who are going broke down there in Texas? What would I tell them in this free trade agreement that

is supposed to help free trade, benefit the United States, why we agreed to an agreement that has a quota on rice?

Ambassador BHATIA. No. No, Congressman, you know, I will be perfectly frank with you. I mean, we pushed extremely hard to gain additional market access in rice from the very beginning to the very end of these negotiations. In the final hours of the negotiations, Korea made clear that it would walk away from the deal. It would be unable to do the deal. Politically it would be unable to do the deal rather than include rice, additional market access in rice.

So the choice that we faced on behalf of the country was to take the very, very good deal that was on the table that would afford substantial market access not only for all of the other agricultural commodities you mentioned but also for services industries, including refinery services and many other industries, versus a perfect deal, which would have included additional market access on rice, which we could not get. So that was the choice that we faced.

I would prefer—I wish it were the case that we had obtained additional market access, either tariff reductions or additional TRQs for rice, but they are not in the agreement. But what I would point out to you, Congressman, are a couple of things.

First of all, there is a parallel process to this FTA that has been ongoing in the multilateral sphere to obtain additional market access to the Korean rice market. And in 2004, we and Korea along with other partners multilaterally achieved a substantial amount of additional market access for American rice farmers, including those in your district.

And under that agreement, it comes close to totally doubling the total amount of rice that Korea is obligated to import over the next 10 years. It provides guaranteed market access for us of a little over 50,000 metric tons of United States rice each year. And it makes a portion of that imported rice available directly to Korean consumers.

And under that agreement, I am happy to point out, United States rice exports to Korea have continued to grow. So in 2006, they purchased 63,000 tons, metric tons, of United States medium grain rice, which is about a quarter of Korea's total rice imports. So there is a parallel process underway which I can assure you we are going to continue to push on. I guess—

Mr. POE. Excuse me.

Ambassador BHATIA. Yes.

Mr. POE. But if we sign this agreement, the deal is done.

Ambassador BHATIA. On the bilateral.

Mr. POE. So no rice is a part of this agreement. Why do not we just stand firm and say if you do not include rice, we are not signing? Why do not we just do that? It is called hardball.

Ambassador BHATIA. Well, I believe, Congressman, we have played—

Mr. POE. I will never be a diplomat, by the way.

[Laughter.]

Ambassador BHATIA. We pushed very, very hard on a lot of issues that required enormous political changes in Korea and will require enormous political changes in Korea. This was one that the trading partner made very clear this just simply was going to re-

sult in the end of the agreement. And the choice was the enormous balance of benefits there that we stood to obtain. I will say that we have a strong commitment, Congressman, and you have this from us at USTR, from the administration. There is a strong commitment to continue to push for rice market access through the multi-lateral and other processes.

And finally I would simply point out that breaking down the barriers, protectionist barriers, in a market like Korea where there are a lot of agricultural sensitivities I believe will run down to the benefit of rice exporters and others because it will show that you can break down these barriers, you can allow in agricultural commodities, and it does not result in the end of their domestic production. It does not result in farmers being put out of business. And I look forward to the day in the not too distant future where that sensitivity level is lowered and where we can extend trade still further.

Mr. POE. Well, the farmers are going out of business. They are tilling their land under and just leaving it because the land is so bad it will not grow anything but rice. So that is a concern for me in this free trade agreement that we do not include rice.

Ambassador BHATIA. I understand.

Mr. POE. I just want you to be on notice.

Ambassador BHATIA. Thank you.

Mr. POE. Thank you, Mr. Chairman.

Mr. ROYCE. Mr. Chairman?

Mr. SHERMAN. I will yield to the ranking member for a unanimous consent request.

Mr. ROYCE. Thank you, Mr. Chairman. Mr. Wu, our colleague, had raised a point, and I have a letter from our USTR, Susan Schwab, in response to a letter I had written her earlier. She says in the letter as a result, "The Korean Industrial Complex is not explicitly mentioned or covered anywhere in the FTA. The goods made in the KIC are not eligible for FTA trade preferences." And she says, "Goods from the Korean Industrial Complex would not obtain preferences under the agreement without additional legislative action by both the United States and Korea."

And so, without objection, I would like to ask that this letter—
[The information referred to follows:]

EXECUTIVE OFFICE OF THE PRESIDENT
THE UNITED STATES TRADE REPRESENTATIVE
WASHINGTON, D.C. 20308

MAY 09 2007

The Honorable Edward Royce
U.S. House of Representatives
Washington, D.C. 20515

Dear Congressman Royce:

Thank you for your letter regarding the United States-Korea Free Trade Agreement (KORUS FTA) and the Kaesong Industrial Complex (KIC). As you know, the United States maintained a strong position throughout the negotiations with Korea that the final FTA would be between the United States and the Republic of Korea and would only cover goods from those two countries. As a result, the KIC is not explicitly mentioned or covered anywhere in the FTA, and goods made in the KIC are not eligible for FTA tariff preferences.

The FTA establishes a government-to-government committee to review whether conditions on the Korean Peninsula may be appropriate for further economic development through the establishment and development of outward processing zones. The Committee will meet one year after the FTA enters into force and on an annual basis thereafter, and will set the criteria that must be met before goods from any outward processing zone may be considered originating goods for the purposes of the FTA, and thereby eligible to receive preferential treatment under the Agreement. Language in the Agreement notes that such criteria would include, but not be limited to, improved labor standards and practices and progress toward the denuclearization of the Korean Peninsula.

Any decision made by the Committee with respect to whether goods from an outward processing zone should qualify as originating goods would serve as a recommendation to the Governments of Korea and the United States, which in turn would need to obtain legislative approval for any amendments to the Agreement with respect to the outward processing zone. Consequently, goods from the KIC could not obtain preferences under the Agreement without additional legislative action by both the United States and Korea.

I hope this information addresses the concerns raised in your letter. I look forward to working with you on Congressional approval of the KORUS FTA. Please contact me if you have any additional concerns.

Sincerely,



Susan C. Schwab

Mr. SHERMAN. It will be made part of the record, but I will comment that the Secretary there did not address the issue of what would be the case if South Korea began to exercise certain small elements of sovereignty over the acreage in these facilities. It is obvious that this letter is true as things stand today. But with a little bit of window dressing, you can reach an entirely different conclusion unless those words are in the statute that Ambassador Bhatia's department is going to present to Congress.

So we will decide whether we are going to just take a letter, Ambassador, which can be changed just by changing a few of the elements of sovereignty or whether we are going to have that language in the agreement. With that, let me yield to the gentleman from Arkansas—or okay. I will call first on the gentleman from Colorado.

Mr. TANCREDO. Thank you, Mr. Chairman. Mr. Ambassador, as a general rule of thumb, I am for the elimination of artificial barriers to the free flow of goods. Unfortunately I have found myself in the position recently of having to vote against several trade agreements because of the cross-border trade in services provision [inaudible] in those agreements. And the standard language I am talking about reads, "Cross-border trade in services or cross-border supply of services means supply of a service from the territory of one party into the territory of another party."

The provision also stipulates that each party to the agreement ensures that local and national "measures relating to qualification requirements and procedures, technical standards and licensing requirements do not constitute unnecessary barriers to trade in services" to guarantee that our domestic laws are "not themselves a restriction on the supply of services."

A concern is that these such provisions, including, for instance, the reformed Chile Free Trade Agreement, could empower our trade partners and challenge the validity of our immigration limits, our visa requirements or even licensing requirements and zoning rules as a "unnecessary barrier to trade" and act as a restriction to the supply of services. The Congress could petition that we be forced to change our immigration laws by this trade section.

I have assurances from the administration, by the way, that these provisions have nothing to do with immigration. Last year I remember when former chairman of the House Ways and Means Committee, Bill Thomas, stated that we are currently in this—by the way, we are having a debate on this very topic, on the amendment that I offered. He said that we were currently in delicate negotiations in the World Trade Organization on market access, and one of the provisions was the question of temporary movement of illegal aliens.

So what I would like to know is whether the administration intends to make immigration a component of U.S. trade policy, and will the United States-Korea Trade FTA sustain the provision and/or the cross-border trade in services provision?

Ambassador BHATIA. Congressman, I appreciate your question, and I know of your longstanding interest in this issue of whether our FTAs somehow contain provisions dealing with immigration and allowing through trade in services provisions commitments to it, whether they contain commitments. I can assure you that is not

the case in this FTA, and I will just read to you one sentence from a relevant chapter:

“Nothing in this chapter or any other provision of this agreement shall be construed to impose any obligation on a party regarding its immigration measures, including admission or conditions of admission for temporary entry.”

So I think hopefully that should provide you the reassurance is there. It is not intended to affect immigration.

Mr. TANCREDO. Thank you for that. And then if I could, I see I have a little bit of time left. I just would like to get into a different area. One of Korea's primary competitors in several different economic sectors happens to be, for instance, Taiwan. And as you know, President Chen's top priority is the bilateral trade agreement with the United States.

I fear that we are driving Taipei into the arms of Beijing by failing to more aggressively push for an FTA with Taiwan, and it is one of our most important economic and security concerns in the region. I know that we are focused here on Korea, but I would like your take on why we have not been able to get an FTA with Taiwan.

Ambassador BHATIA. Congressman, we or the U.S. Trade Representatives' Office, but generally the administration, are obviously very focused and committed to deepening and strengthening our trade relationships with Taiwan. It is a major trading partner for us. I actually went to Taiwan last year, to Taipei, to lead our Trade and Investment Framework Agreement discussions. It is not quite an FTA, but it is a comprehensive effort to address trade and investment barriers that might preclude or otherwise prevent the integration of the economic relationship. And I am delighted to tell you that I think it is going very well, and indeed we will have another TIFA meeting this summer here in Washington.

We are working concretely to address barriers sector by sector with Taiwan, be it in the investment area, be it in trade and agricultural goods, be it in trade and services, and it is proving to be quite successful. As far as future FTAs go, that is always something that we undertake in consultations with Congress. It would of course require us to get an extension of trade promotion authority for any contemplation of any FTA with any partner, but we are happy to remain in contact and consultation with you on that.

Mr. TANCREDO. Thank you, Mr. Ambassador. Thank you, Mr. Chairman.

Mr. SHERMAN. Thank you. Let me point out for the record that the average inflation adjusted wage for American workers has gone up by a full 5 cents in the 20 years plus since we first had fast-track. We have an \$800 billion trade deficit, and it is of course attributable to the fact that when we negotiate these deals, we start with our own tiny tariffs, never threaten to increase them, and then come back with the best deal we can having never played hardball or sought free trade. With that, let me yield to the gentleman from Arkansas.

Mr. BOOZMAN. Thank you, Mr. Chairman. Coming from Arkansas and also being a major rice producer, maybe the largest, I would associate myself with Mr. Poe's remarks in the sense again of

someone that has been very supportive of trade agreements. Certainly we support fair trade.

Ambassador BHATIA. Yes.

Mr. BOOZMAN. One of the concerns I have about the rice thing being on that is we start picking out these areas that are sensitive. Does that make it that much more difficult as we do agreements in the future?

Ambassador BHATIA. You know, Congressman, we have been asked and I have been quite clear, we have been quite clear, Ambassador Schwab and others, that we do not see this as a precedent. We have made quite clear to our trading partners that we do not see an exclusion of rice to be a precedent in future FTAs.

Mr. BOOZMAN. Well, not so much rice, but, I mean, when you start targeting these things in general, it is rice this time. Again, you know, when you start doing that, does not that make it more difficult as you go along?

Ambassador BHATIA. It very much remains our policy, our goal and our desire to have FTAs be as comprehensive as possible because, frankly, the benefits to be derived not only by us but by our trading partners are through having a comprehensive FTA. Where one of our exports is excluded, their consumers, the trading partner's consumers, are deprived the benefit of competitive American products. So I can assure you it remains our goal and our desire to have comprehensive FTAs.

Mr. BOOZMAN. If we strike a deal, if we do the FTA, how will that affect our trade with the other partners in the area, people like China and Japan?

Ambassador BHATIA. Well, Ambassador Hill can probably talk about the broader geopolitical significance of the FTA within the region. I can tell you from a trade negotiator's—I beg your pardon?

Mr. BOOZMAN. I do not mean to interrupt. In addition to that, because of this FTA, would that lead to more FTAs with partners that we are trading with there?

Ambassador BHATIA. I can tell you that our trading partners in the region have sat up and taken notice of this FTA. I hear it from all of our major trading partners. And indeed I think they see whether or not this FTA gets through as being a major litmus test of our commitment to the region, our commitment to opening markets, and I think it could have a very, very beneficial effect on further trade liberalization in the area.

Mr. BOOZMAN. Thank you, Mr. Chairman.

Mr. SHERMAN. Thank you. We will now begin a second round, and it will at least try to have some questions for Ambassador Hill or Secretary Hill, who has shown incredible patience here, but I still have more questions for Ambassador Bhatia. First what is the revenue cost of this agreement in lost tariff revenue to the Treasury? Do you know or not?

Ambassador BHATIA. I am sorry. The revenue cost I do not have the precise number, Mr. Chairman.

Mr. SHERMAN. Is it over or under \$1 billion a year?

Ambassador BHATIA. I will not hazard a guess. We can find out and let you know.

Mr. SHERMAN. What is the cost of the trade assistance package where we are going to help workers in Don Manzullo's district

when they are displaced, et cetera? What is that cost going to be? Do we have that?

Ambassador BHATIA. We have, as you know, Mr. Chairman, working with the Congress, have passed a trade adjustment assistance package that is—

Mr. SHERMAN. How much is it going to cost?

Ambassador BHATIA. There is no country-specific. It is a program that exists for all of our trade agreements.

Mr. SHERMAN. It is the more you do the more you spend. What is the incremental cost of this agreement, or have we not bothered to figure that out?

Ambassador BHATIA. No. But again, you are asking us to project transition costs here. I would submit that the agreement will have a very beneficial effect in terms of stimulating more jobs here in the United States, though.

Mr. SHERMAN. Clearly there are going to be winners and losers. All of the published reports say more losers than winners. But putting that aside, we both agree that there are going to be winners and losers, that the Treasury of the United States is going to be called upon to help the losers, and you do not know how much that will be.

But we do know the Treasury is going to lose money from tariffs. It is going to lose money to provide assistance from the inevitable losers. And all that money is going to come from the money available to provide for education in states like mine. Where are we going to get the money from those two sources without cutting domestic expenditures in districts unaffected by trade?

Ambassador BHATIA. You know, Congressman, obviously your issues go well beyond the Korea FTA to trade liberalization generally. I mean, I would submit to you that the record of trade liberalization as an engine of economic growth, as a force for improving standards of living of Americans for the past 50 years—

Mr. SHERMAN. A whole nickel.

Ambassador BHATIA. No, Congressman.

Mr. SHERMAN. A whole nickel of increased wages. I agree you can point to income statistics, because if 1 million people lose money and one billionaire is created, the economists will say, well, national income went up. The fact is American workers have seen their incomes go up by a full nickel over the last 20 years since fast-track was adopted.

But getting away from the economic effects and looking at the fiscal effects, we work for the Federal Government. We supposedly care about the U.S. fiscal deficit. This thing is going to cost us money, as I identified, in two different ways. You have asked us to introduce agreement without even an attempt to make a cost estimate.

Are you claiming that the reduction in Federal revenues on the tariff side and the expenditure of Federal funds on helping those people who you say are not so many, but however many there are who are hurt by this agreement, have an undisclosed cost, but somehow are you suggesting the Federal Reserve Board simply print more greenbacks to cover those costs?

Ambassador BHATIA. Congressman, Mr. Chairman, I think, and I mentioned these in my opening remarks, I mean, the estimates

of the benefits to the U.S. economy from this are between \$17 billion and \$43 billion. The forecasts, I mean, let me just give you an example on—

Mr. SHERMAN. What do you mean by benefit? How can you have an agreement which will increase the U.S. trade deficit according to every published report and uncontradicted by anything you have said and then say it is going to increase our income? What it is going to do is provide some additional exports and a somewhat greater amount of additional imports. And we have an \$800 billion trade deficit, and you suggest that we do more of the same and make it up in volume.

Ambassador BHATIA. No, I do not, Mr. Chairman. First of all, I think that the—again, I do not know that these estimates are deficits that you are coming up with. Let us assume, though, let us assume—

Mr. SHERMAN. Would not you bother to read the only published economic analyses of what effect this is going to have on our trade deficit?

Ambassador BHATIA. Mr. Chairman, if you assume for a moment even hypothetically, which I disagree with, that there were to be an increase in trade deficit, the substantial amount of additional exports that would be provided by this, the substantial amount of additional exports that would be provided, would in my mind create substantial new job opportunities here in the United States. That has been the record of all of our trade liberalization. And I think the supposition that somehow this is going to be the exception to that rule just clearly is not borne out by what has happened in the past.

Mr. SHERMAN. Your position is if we lose 1 million jobs and we gain 900,000 jobs, that is a \$900,000 job gain?

Ambassador BHATIA. No, I think it is the other way around, Mr. Chairman. If you look, for instance, last year, a loss of 13 million jobs for which the estimate for trade's role in that 13 million job loss has been 3 percent, less than 3 percent, but the creation of 15 million new jobs, often higher-paying jobs, often more rewarding jobs because of its relationship to international trade I think makes a compelling case that trade is the avenue for growth for the American economy.

I mean, that is the record of the last 50 years of America's international economic engagement. And Korea stands to benefit us more than most of the other FTAs because it is such a rich, fast-growing, dynamic economy to have as a trading partner.

Mr. SHERMAN. Reclaiming my time, you cannot have an increase in the trade deficit and say you are increasing on a net basis the number of jobs and that those jobs that you are creating are greater pay than those that you are losing. It is simple math. If you are exporting a little bit more, then importing a lot more, you are losing jobs.

Now the only way you could be gaining jobs is if those exports involve low-paying jobs and those imports involve high-paying jobs. But you cannot have an increase in the trade deficit and at the same time say that you are making America richer.

With that, let me move to Ambassador Hill. We have two objectives. One is a commercial objective, and the other is a foreign pol-

icy objective. As Ambassador Bhatia has said, this is a great deal for South Korea commercially. To what extent have you and the State Department been involved in making sure that in order to get these benefits, South Korea reduces its subsidies, investments, processing zones, et cetera, with North Korea until that regime changes and develops?

Mr. HILL. Well, first of all, with respect to the FTA, of course we worked very closely with USTR to ensure that some of the problems that existed prior to the negotiation of the FTA were addressed. We were dealing with issues of barriers to our pharmaceutical industry. For example, our Embassy in Seoul has been very much involved in that sort of thing. The State Department here has been very much involved in trying to deal with some of these problems so that we could get to the point where we felt there would be a successful FTA.

Secondly, with respect to the South Korean policies toward North Korea, in particular Kaesong, I think we do need to understand that as South Korea looks at North Korea, they see a somewhat different picture than from what we see in Washington. First of all, they see a peninsula that was divided, a divided peninsula through no fault of the Korean people. I mean, this is something that happened in the depths of the 20th century, a great tragedy I think that every Korean feels.

For example, I have mentioned this before. When they are able to arrange these family unification visits, probably these are not really noticed very much in Washington, but when the Red Cross is able to bring family members from North Korea together with family members from South Korea, it is enormous news in South Korea. So I think we have to understand that because they are so much closer to North Korea, they very much feel the effects of this division.

With respect to Kaesong, this has been a pilot project designed to try to engage North Korea in the hopes that by having South Korean factories in North Korea, this can have an effect on beginning what I think everyone understands will be a very long road toward some sort of reform and then eventual transformation in North Korea.

Our concern has been to make sure that as South Korea conducts this policy—it was known in their previous administration as Sunshine Policy, now it is discussed more as an engagement policy—we want to make sure that as they approach North Korea, we are not at cross-purposes for the Six-Party process, because at the end of the day, we need North Korea to denuclearize. There is very little that we can do with North Korea, frankly, that anyone can do with North Korea as long as it is pursuing nuclear weapons.

So we need to make sure these policies, that is, the South Korean approach to North Korea and the Six-Party process approach to North Korea, are somehow coordinated. And I am very pleased to say we have done that. In the recent months as we have gone through this very difficult stage, South Korea has not been providing food aid to North Korea. They have been trying to coordinate with us in the Six-Party process to ensure that there are no mixed messages. And I think we have done a good job in addressing that.

But, Mr. Chairman, I want to stress that getting North Korea to give up weapons that they have been developing for several decades is a tough job, and we have no choice but to stick with it. And if we are going to be successful, it is going to be because we worked with other friends and allies in the region, and I would say our work with South Korea is very important in this regard.

Mr. SHERMAN. Thank you for your efforts on trying to bring CND, that is to say complete nuclear disarmament, to the North Korean regime. As you have explained, it is understandable why South Korea would view things just a bit differently than we would. We obviously think our approach is better, though we understand their approach.

My question was, have we used the leverage of negotiating this free trade agreement to get South Korea to move off of its policies that we understand closer to the policies that we prefer, the ones that are a little tougher on North Korea until it abandons its nuclear program? In particular, you have said that no one can really do business with North Korea until they give up their nuclear program, but South Korea is going forward with these processing zones, which as I said in my opening statement, the addition of up to 1 million workers is just one of the issues of the zones.

So let me ask you this. As far as the agreement negotiations, were we able, or did we even try, to get South Korea to move closer to our position of putting tough economic pressure on the North Koreans until we see some changes?

Mr. HILL. Well, Mr. Chairman, after the North Koreans conducted missile tests last July, in fact July 4, the South Koreans suspended any expansion of this Kaesong facility, so it remains really a pilot project. Now they will expand it as there is progress in the nuclear talks. So I think that we have a linkage there which I think is important to us.

With respect to the connection or the linkage to the FTA, I want to emphasize that we have negotiated an FTA on the basis of what we believe are objectives for us, that is, it is in our interests to have this FTA. Now obviously when you negotiate, you negotiate with a partner who needs to have it in his interests as well, so there has been a balance of interests in the FTA.

But I think clearly as we have moved ahead with this FTA, it has helped bring the United States and the South Korean positions closer together on North Korea because we are in very, very close consultations these days as never before, and I think we have the FTA negotiations to thank for that.

Mr. SHERMAN. My concern is that South Korea reacts only temporarily to the provocations from the North. For example, the North tests a nuclear weapon. Then they test a rocket. Now you point out when they test the rocket, South Korea suspends Kaesong. What did South Korea do in response to the nuclear test? Have they done anything economically?

Mr. HILL. Actually since that time, they have continued not only the suspension of Kaesong but also the suspension of bilateral assistance to North Korea. So it has been held far below what it was the previous year, and that is because of these two tests, first the missile test and secondly the nuclear test which took place 3 months later in October.

Mr. SHERMAN. Did they take these actions in response to the first provocation or the second?

Mr. HILL. The first, this is the missile test, was they took the action to halt the expansion of Kaesong, which they were going to review, but in the process, North Korea had this nuclear test. And after the nuclear test, they resolved to maintain that restriction.

Mr. SHERMAN. So the second provocation simply caused a continuation of adverse actions, sanctions, whatever you want?

Mr. HILL. That is correct, yes.

Mr. SHERMAN. Would you expect that this same tough line would be continued by South Korea if we can go another 12 months or 24 months with no additional provocations but no additional concessions from North Korea?

Mr. HILL. Actually I do. And I think the mood in South Korea as a result of the North Korean nuclear test has shifted than what it was 2 years ago. I also like to think that our willingness to engage diplomatically with China and with the other partners and even directly within the Six-Party process with North Korea has also helped improve or helped bring the United States and South Korea closer together in policy terms. So I think we can count on South Korea as a very reliable ally as we go forward in this process.

Mr. SHERMAN. Yongbyon continues to operate right now, and North Korea will have more nuclear material at the end of the day than they had at the beginning of the day?

Mr. HILL. Yongbyon has been up and down due to maintenance concerns. It is our hope, though, that as we move to implement our February agreement, and I expect you will see some developments very soon in that regard, that we will have Yongbyon shut down, and then we will go to the next phase, the elements of which have already been agreed, which is to disable Yongbyon.

It does not solve our problem because we have 50 kilos already of fissile material. Those kilos must be abandoned according to our September 2005 agreement. We also have to run to ground the issue of highly enriched uranium purchases that they made. So to shut down Yongbyon is a first step in a long process.

Mr. SHERMAN. Well, I thank you for your work on this issue. I am not quite as optimistic as you are. I am not characterizing your comments as optimistic.

Mr. HILL. Thank you.

Mr. SHERMAN. Just characterizing myself as even a little bit more gloomy. And I want to thank the two witnesses for coming before this subcommittee and spending over 2 hours with us. Thank you very much.

Ambassador BHATIA. Thank you.

Mr. HILL. Thank you.

Mr. SHERMAN. All right. You did a great job.

[Whereupon, at 12:05 p.m., the subcommittee was adjourned.]