

# Regulatory Reform in Japan

Enhancing Market Openness through Regulatory  
Reform



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## FOREWORD

Regulatory reform has emerged as an important policy area in OECD and non-OECD countries. For regulatory reforms to be beneficial, the regulatory regimes need to be transparent, coherent, and comprehensive, spanning from establishing the appropriate institutional framework to liberalising network industries, advocating and enforcing competition policy and law and opening external and internal markets to trade and investment.

This report on *Enhancing Market Openness through Regulatory Reform* analyses the institutional set-up and use of policy instruments in Japan. It also includes the country-specific policy recommendations developed by the OECD during the review process.

The report was prepared for *The OECD Review of Regulatory Reform in Japan* published in 1999. The Review is one of a series of country reports carried out under the OECD's Regulatory Reform Programme, in response to the 1997 mandate by OECD Ministers.

Since then, the OECD has assessed regulatory policies in 16 member countries as part of its Regulatory Reform programme. The Programme aims at assisting governments to improve regulatory quality — that is, to reform regulations to foster competition, innovation, economic growth and important social objectives. It assesses country's progresses relative to the principles endorsed by member countries in the 1997 *OECD Report on Regulatory Reform*.

The country reviews follow a multi-disciplinary approach and focus on the government's capacity to manage regulatory reform, on competition policy and enforcement, on market openness, specific sectors such as telecommunications, and on the domestic macro-economic context.

This report was prepared by DoHoon Kim, Administrator, and Akira Kawamoto, Principal Administrator, of the Trade Directorate of the OECD. It benefited from extensive comments provided by colleagues throughout the OECD Secretariat, as well as close consultations with a wide range of government officials, parliamentarians, business and trade union representatives, consumer groups, and academic experts in Japan. The report was peer-reviewed by the 30 member countries of the OECD. It is published under the authority of the OECD Secretary-General.

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## Executive Summary

### Background Report on Enhancing Market Openness through Regulatory Reform

Does the national regulatory system allow foreign and domestic enterprises to take full advantage of competitive global markets? Reducing regulatory barriers to trade and investment enables countries in an expanding global economy to benefit more fully from comparative advantage and innovation. This means that more market openness increases the benefits that consumers as well as producers can draw from regulatory reform. Maintaining an open world trading system requires regulatory styles and content that promote global competition and economic integration, avoid trade disputes, and improve trust and mutual confidence across borders.

Recognising the benefits from the integration in the open multilateral trading system, Japan has improved market access in the context of border measures to a level equal to or better than many other OECD countries. However, enhancing market openness by relaxing behind-the-border measures such as domestic regulations has been relatively slow in Japan. Japan has recently undertaken a number of promising deregulatory programmes such as the two Three year Programmes for the Promotion of Deregulation. Those Programmes clearly state *inter alia* that enhancing market openness is one of most important objectives. However, despite some progress made by these programmes, the Japanese regulatory system in many respects is still perceived as unfriendly to new competition, especially foreign competition. This may be due to the relatively poor extent to which six efficient regulation principles related to market openness identified by the OECD are integrated into the Japanese regulatory system.

Lack of transparency is one of main weaknesses of the Japanese regulatory system, because of both opaque administrative culture and lax implementation of laws. The weak enforcement of competition policy is another major weak point, because anti-competitive practices by private firms or semi-public organisations are seen to pose obstacles for market access in Japan. Major trading partners frequently express concerns about these two principles: transparency and application of competition policy. In addition, despite positive aspects such as the role of the Office of Trade and Investment Ombudsman (OTO), Japan is often criticised for acquiescing in many burdensome administrative procedures which are felt to unnecessarily hamper imports and inward investment.

Japanese regulatory reform programmes have closely reflected pressures from major trading partners to address the perceived causes of a wide range of trade friction. However, for reform to be truly effective more attention must be paid to the overall objective that is sought rather than particular problems that have arisen. Reform must thus move beyond being a reaction to foreign pressures and must instead be fully embraced by public authorities as being foremost in the interest of the national economy: to strengthen its competitiveness in an open global economy and to promote the welfare of its people. Japan needs to demonstrate clear commitment to its regulatory reform programmes through bold and coherent policies, linked with a strong commitment for rapid implementation.

## 1. Market openness and regulation: the policy environment in Japan

The Japanese government recognises explicitly the benefits that have accrued to the Japanese economy from the opportunities available today to globalise economic activities -- opportunities which arise to an important extent from the open multilateral trading system.<sup>1</sup> Thanks to their participation in world competition, Japanese manufacturing industries have often succeeded in acquiring a high level of competitiveness and enhancing the national economic welfare.

The benefits of regulatory reform from the market openness perspective are still potentially very large in Japan. This has been shown by numerous studies on price differences between the Japanese domestic market and comparable foreign markets.<sup>2</sup> These price differences are persistently high despite the progress made in trade liberalisation, deregulation and structural reform, perhaps due to high trade protection for agriculture and some manufacturing sectors (according to Sazanami's work) or due to the inefficiency of highly regulated service sectors and utilities (according to Daiwa Economic Research Institute). The combined effects of both are probably responsible. The Japanese government, recognising the potential benefits, has also conducted surveys on price differences.<sup>3</sup> According to these surveys, citizens of Tokyo pay 8-30% more for

their purchases than citizens in major other international cities and Japanese industries are paying almost twice as high for non-manufacturing intermediary inputs compared to their competitors of, and more than three or four times higher compared to those of other Asian emerging economies (see section 4.3 for detailed discussion).

Recognition of the benefits of globalisation and of further market opening reform have been reflected more and more in Japanese trade policy. In order to integrate its economy in the world trading system, Japan has continuously reduced its general tariff rates so that it now has one of the lowest average tariff rates within the OECD area, with 4.8% for all products and 2.5% for manufactured products.<sup>4</sup> The relative absence of formal non-tariff border measures in Japan is notable as well.<sup>5</sup> Japan has been also active in world-wide and regional trade talks/negotiations such as the WTO and the APEC.

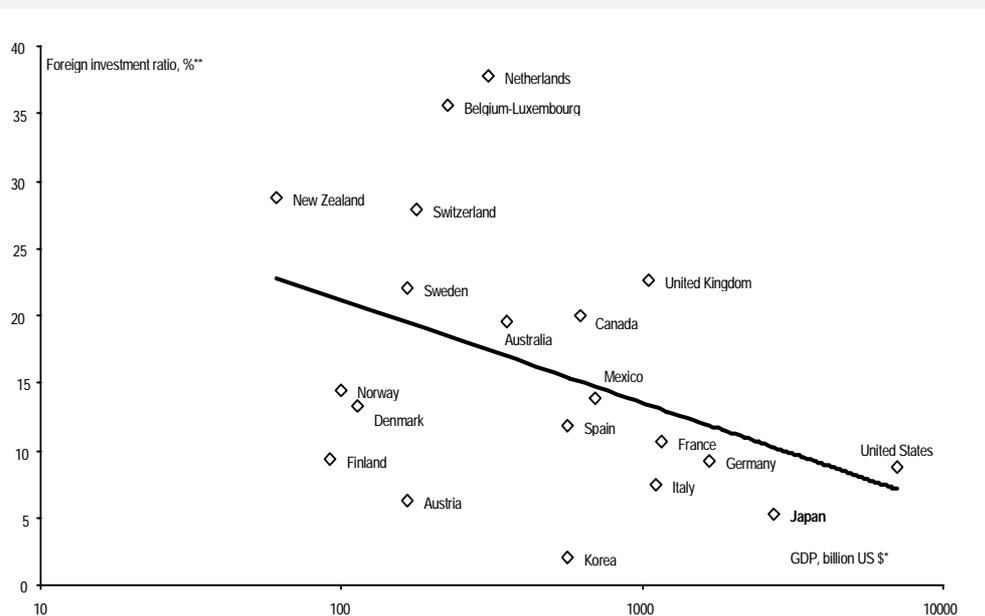
Japan has also made clear that it intends to increasingly open its economy to global competition through deregulation. In its “Three-Year Programme for the Promotion of Deregulation” announced in March 1998, the Japanese government has committed to achieving “an open and fair *socio-economic system which is internationally open* and based on principles of self-responsibility and market mechanism”. Some recent measures of regulatory reform have indeed resulted in visible improvement in Japanese market openness, such as oil import deregulation. Moreover, the Japanese government has shifted from its former export promotion policies to focus more and more on the promotion of imports and inward investment. For example, many supplementary incentives to imports and inward investments have been introduced, in addition to the ordinary financial and fiscal incentives for domestic activities. Japan has strengthened policy efforts on infrastructure for imports and inward investments, especially by expanding FAZs (Foreign Access Zones).<sup>6</sup> It also gives technical assistance for this purpose at the bilateral and/or regional level. In order to implement these measures vigorously, Japan adopted in 1992 a special law on Extraordinary Measures for the Promotion of Imports and the Facilitation of Inward Investment. In 1995, this law was prolonged for a further 10 years.<sup>7</sup>

However, against the background of the lingering large-scale Japanese surplus in trade, many trading partners have continuously raised concerns about the effective openness of the Japanese market. Compared to other OECD countries, Japan has been far below average in attracting foreign direct investment, despite the government’s expressed policy stance to welcome it (see Figure 1). This has been seen by trading partners as a sign of the restrictive nature of the Japanese business environment, notably arising from domestic regulations. Indeed preliminary figures for 1997 suggest that despite recent market opening, FDI (foreign direct investment) inflows to Japan amounted to only US\$ 3 224 million, it did not even place amongst the top 25 countries with respect to FDI inflows<sup>8</sup>, despite the fact that Japan’s economy is the second largest in the world.

Since the 1980s, major trading partners have paid more attention to Japan’s domestic regulations and its economic system, which they perceive as unfriendly to competition from foreign products and services. The US and EU have urged Japan to reform domestic regulations in order to enhance market access as well as domestic (behind the border) obstacles.<sup>9</sup> These trade talks have prompted Japan to take several deregulatory initiatives. *Recent Japanese deregulation programmes, especially those in the 1990s, therefore, cannot be dissociated from trade talks with major trading partners.*

Bilateral US-Japan consultations in several sectors began in the 1980s. Deregulation became an element of major trade debate in 1990 under the Japan-US Structural Impediment Initiative Talks, which targeted regulatory restrictions in sectors such as large-scale retail stores (see Box 1). The Japanese Cabinet stated in 1991 that one way of reducing trade impediments was to promote deregulation more strongly, and it recommended further measures in the telecommunication, financial services, and energy sectors. The Japan-US Framework for a New Economic Partnership, established in July 1993, centred on deregulation measures in eight areas related to international trade and investment. With the EU, Japan reached a bilateral agreement in the form of understandings in June 1995, to implement some deregulatory measures for automobiles and components.

Figure 1. Share of stocks of inward and outward direct investment in GDP in OECD countries in 1995



\* GDP measured at current prices and current PPPs in billion US dollars

\*\* Average of inward investment and outward investment relative to GDP (except for Mexico, inward only);

Source: OECD, *The Review of Regulatory Reform in the Netherlands*, calculated from AFA databases (DSTI, EAS Division) and DAFPE's Foreign Investment Database.

### Box 1. Japanese retail distribution and Large Scale Retail Stores Law

As an article of *International Economic Review* says, the Japanese system is characterised by large numbers of small retailers and few high-volume discount stores. The dominance of small retailers in Japan's distribution system has been attributed to traditional Japanese factors such as the importance of fresh food in the Japanese diet, which requires frequent shopping trips, and the role of offering employment opportunities for non-qualified or retired persons especially in relatively rural areas. This distribution system has been an unfavourable factor of market competition for foreign products, because incumbent producers have had dominant positions vis-à-vis wholesalers and retailers.

The Large Scale Retail Store Law has been pointed out by trading partners as another factor which has indirectly served as a market obstacle for foreign products. Under the Law, the shopping space size of a proposed large scale store has been subject to consultation with local small retail stores.<sup>10</sup> This, in turn, has hampered market access for new products and new competitors including foreign ones, as small retail stores tend to prefer long term relations with wholesalers or manufacturers.

Important changes in the law since the early 1990s have eased the opening of large stores. OECD, *Economic Survey*, 1995 states that liberalisation of Japan's Large Scale Retail Store Law has resulted in a sharp increase of applications to open large stores and overall gains are estimated at as much as US \$45 billion.

Despite the recent decision to abolish the Law, foreign parties are still concerned that openings of large scale stores may be impeded. One reason is that regulating powers will be transferred to local authorities whose political leaders are likely to be influenced by the political power of regional co-operatives of small retail stores. Foreign parties are also concerned that the new law concerning the measures by large scale retail stores for preservation of living environment, could be used in a prohibitive way. On the other hand, some regional authorities which are less dependent on small retailers may try to attract large stores to stimulate the regional economy. In this case, abolishment of the Law can have a favourable effect on market competition.

Source: *International Economic Review*, Retail Distribution in Japan, September/October 1997, *OECD Economic Survey on Japan*, 1995.

International discussion has been increasingly focused on the public sector's regulatory requirements and processes. Trading partners have complained about complex rules, opaque decision-making, and non-transparent instructions from ministries and have urged Japanese government to make efforts to open government processes and simplify regulations. "Questions about the openness of the Japanese market have turned away from conventional trade policy issues towards differences in national business practices and regulations, which are not overtly protectionist..." the OECD Economic Survey noted in 1991.<sup>11</sup> Besides, more attention is being given to harmonising procedures, standards, and rules with international norms.

While regulatory reform has been underway since the early 1980s to improve the competitiveness and efficiency of Japanese firms, economy-wide programmes of deregulation were initiated only in 1995, when the "Deregulation Action Programme" was launched. Those Programmes have clearly stated *inter alia* enhancing market openness as one of most important objectives. However, while trading partners have welcomed the progress to date, their requests for Japanese regulatory reform have persisted as well and the number of requests is increasing. It has been difficult to have a general picture of the current status of Japanese regulatory reform from market openness perspectives, due to the complexity, sheer size and coverage of regulatory questions as well as their continuous evolution. An overview of the reform and trade discussion will be useful at this juncture.

Bilateral trade talks, while addressing many concrete issues, have put relatively less priority on questions which tend to take longer to resolve. Trading partners have been keen to explain that their requests will not only serve foreign traders or investors but also benefit the Japanese economy, especially industrial competitiveness and consumer interests. However, bilateral trade discussions may have given the Japanese public the impression that reform, even if undertaken, has been imposed from the outside. Such impression may have diluted the effectiveness of market openness perspective in reform discussions. External pressures are sometimes discussed in Japan as useful and even necessary for meaningful reform. But there are also limits: if used excessively, the public image of such external pressures will deteriorate and negative views may be promoted by those who would like to maintain status quo of regulations.

Some observers hold the view that in the context of the Japanese political economy, the balance of power is advantageous for resisting reform.<sup>12</sup> Thus far, the business sector, especially the export oriented sector, has been the major promoter of regulatory reform in Japan. Its concerns over competitiveness in future have pressed government for deregulation initiatives, although there still remain strong sectoral reservations, especially by regulated firms. Academics and media are sometimes strongly in favour of deregulation, but neither seek to be involved in detailed issues. Consumer voices have only been weakly heard in Japan, although they will stand greatly to benefit from reform. They have not come out strongly for government efforts toward deregulation and in some cases they have been hostile to further market openness.<sup>13</sup>

This image of strong external pressures and weak domestic support for reform suggest that clearer recognition in Japan of the economy-wide interests in both regulatory reform and market openness would be crucial in creating a firmer basis for future reform. When reform in a market openness perspective benefits foreign trade and investment, Japanese consumers and firms will benefit as well. Not only foreign voices, but also a growing number of surveys by Japanese institutions have found market openness perspectives are beneficial for the Japanese economy. Studies on price differentials between domestic and international markets have revealed that such differentials mainly reflect Japanese market access problems and that Japanese people are losing one of their main sources of welfare increase, in other words foreign sources, because of problems in the Japanese regulatory system. The Japan External Trade Organisation (JETRO) has published a number of sectoral studies from a market openness perspective. The 1997/1998 OECD Economic Survey also states the need to promote such a perspective: "While deregulation has been opening up new business opportunities and international competition has been exerting pressures on companies to remain competitive, changes in the Japanese business sector overall have not been sufficient to arrest the trend declines in profitability and the rates of new company formation".<sup>14</sup>

As seen in this section, market openness perspectives have been a strong driving force in past Japanese regulatory reform. They will continue to play an important role in the future. However, external pressure on specific issues is not a sufficient basis for bringing the sea-change in domestic regulation that is needed to achieve the benefits sought for the Japanese and world economies. On the one hand, more focus on domestic regulatory *systems* in trade talks will help to focus on more fundamental issues and thus resolve the trade debate more effectively. On the other hand, the reform discussion in the domestic context needs to be strengthened, linking recognition of the domestic benefits to greater market access. Japanese people may recognise that regulatory reform is not to simply reduce trade tension but also to reinvigorate the economic efficiency and to avoid welfare loss to Japanese economy.

## 2. The policy framework for market openness: the six “efficient regulation” principles

An important step in ensuring that regulations do not unnecessarily reduce market openness is to build the “efficient regulation” principles into the domestic regulatory process for social and economic regulations, as well as for administrative practices. “Market openness” here refers to the ability of foreign suppliers to compete in a national market without encountering discriminatory or excessively burdensome or restrictive conditions. These principles, which have been described in the 1997 OECD *Report on Regulatory Reform* and developed further in the Trade Committee, are:

- *Transparency and openness of decision making;*
- *Non-discrimination;*
- *Avoidance of unnecessary trade restrictiveness;*
- *Use of internationally harmonised measures;*
- *Recognition of equivalence of other countries’ regulatory measures; and*
- *Application of competition principles from an international perspective.*

They have been identified by trade policy makers as key to market-oriented and trade and investment-friendly regulation. They reflect the basic principles underpinning the multilateral trading system/WTO in which many countries have undertaken certain obligations. The intention of the OECD country reviews on regulatory reform is not to judge the extent to which any country may have undertaken and lived up to international commitments relating directly or indirectly to these principles; but rather to assess whether and how domestic instruments, procedures and practices give effect to the principles and successfully contribute to market openness. Similarly, the OECD country reviews of regulatory reform are not concerned with an assessment of trade policies and practices in Member countries.

In sum, this report considers whether and how Japan’s regulatory procedures and content affect the quality of market access and presence in Japan. An important reverse scenario -- whether and how inward trade and investment affect the fulfilment of legitimate policy objectives reflected in social regulation -- is beyond the scope of the present discussion. This latter issue has been extensively debated within and beyond the OECD from a range of policy perspectives. To date, however, OECD deliberations have found no evidence to suggest that trade and investment *per se* impact negatively on the pursuit and attainment of domestic policy goals through regulation or other means.<sup>15</sup>

## *2.1 Transparency, openness of decision making and of appeal procedures*

To ensure international market openness, foreign firms and individuals seeking access to a market (or expanding activities in a given market) must have adequate information on new or revised regulations so that they can base their decisions on an accurate assessment of potential costs, risks, and market opportunities. Regulations need to be transparent to foreign traders and investors. Regulatory transparency at both domestic and international levels can be achieved through a variety of means, including systematic publication of proposed rules prior to entry into force, use of electronic means to share information (such as the Internet), well-timed opportunities for public comment, and rigorous mechanisms for ensuring that such comments are given due consideration prior to the adoption of a final regulation.<sup>16</sup> Market participants wishing to voice concerns about the application of existing regulations should have appropriate access to appeal procedures. This sub-section discusses the extent to which such objectives are met in Japan and how.

Lack of transparency in the Japanese regulatory system has been one of the major subjects of Japan's own regulatory reform efforts and important concern of major trading partners. Transparency is related with all the phases of the regulatory process: from the stage of formulating regulations to that of implementing them, including the stage of changing or reforming them. The Japanese government, recognising the importance and necessities to take actions to enhance transparency,<sup>17</sup> has undertaken various reform projects in this light in its administrative procedures. Despite these commitments and many attempts to improve the situation, there still remains the scope for further improvement.

Trading partners' concerns with regard to the non-transparency problem are consistent with Japan's own reform in this area and suggest the necessities to improve the situation. For example, the US has asked Japan to enhance transparency by improving use of the following strategies:<sup>18</sup>

- Notice and comment procedures for regulations;
- Information disclosure requirement for government entities;
- Examination procedures for licences, permits and approvals;
- Consultation process of advisory councils;
- Private sector regulations; and
- Information on administrative guidance.

The EU has also asked for improvements to transparency in several areas:<sup>19</sup>

- Information disclosure;
- Examination of all administrative guidance on competition policy principles;
- Prior publication of and opportunity for comments on regulatory proposals;
- Links and connections between industry associations and the administration; and
- Publication of deliberations within advisory bodies.

According to major trading partners,<sup>20</sup> numerous non-transparency cases can be also found at the sectoral level, for example: implementation of the Building Standards Law for the housing sector; opportunity to comment on health care policies; the approval process of new products and services and regulations of private sector organisations in the financial services sector; the slot allocation system of international airports; the procurement process and review and comment procedures in the energy sector; consideration of a more cost-oriented interconnection accounting system for telecommunications; lack of comment opportunities before the advisory council on motor vehicle regulations; tariff review mechanisms;<sup>21</sup> and approval procedures for medical machines.

Concerning administrative culture, Japanese bureaucrats have often relied on “administrative guidance” rather than established laws and rules to enforce their policies. Trading partners have been concerned that this traditional administrative style may have reduced the level of transparency for outsiders, especially foreign ones (see background report on Government capacity to assure high quality regulation in Japan for more detailed discussion of administrative guidance).

The new Three year Programme has recommended that regulatory authorities ensure transparency when using administrative guidance, and many ministries and agencies seem to be following that recommendation. In June 1998, the Ministry of Finance announced that it had codified about 400 cases of guidance in a more formal form.<sup>22</sup> Even though this was well received by the financial sector, including

foreign participants, an American firm in the sector still expressed concerns about non-transparent characters of Japanese administrative procedures.<sup>23</sup> According to it, despite the codification, the substance of most guidance has not changed much and some guidance still remains unwritten.

According to the Administrative Procedure Law, regulatory authorities should use guidance only based on the voluntary co-operation of subject parties and not treat them disadvantageously because of the non-compliance (Article 32). Therefore, administrative guidance seems to be officially no longer used in a binding manner. But, consultation continues to be used as a means to control the sectors, to co-ordinate their interests and even to disseminate regulatory information which may be used in the regulatory decision making process.<sup>24</sup>

Another issue is transparency of consulting procedures. Ministries and agencies rely on over 200 advisory councils (*shingikai*) to get broader general views on policies and policy directions. Advisory councils are composed of eminent scholars, journalists, and industry specialists including business leaders. Because of their composition, the advisory councils are considered to represent both general public opinion and specialist views. They are often called upon when ministries or agencies need to know public opinion before they make an important decision. However, because many members of advisory councils are involved in the sectors, and even come directly from incumbent business, they can be considered as “inner circle” members. In fact, advisory council members are usually selected by bureaucrats in a discretionary way. Moreover, the advisory councils’ reports are usually (and always in the past) drafted by the bureaucrats who are supposed to consult them. Although there has been progress in terms of opening discussions by advisory councils to the public, further efforts are needed (see Box 2). The “public comment procedures” for regulatory decision making process that took effect in April 1999 are also promising.

Furthermore, many regulatory decisions are made without consulting advisory councils. Lower level regulations such as ministerial orders as well as other administrative conduct that may have regulatory effect<sup>25</sup> are not subject to advisory council discussions in most cases. Moreover, there is a risk that not all the advisory council members, because of their part-time status, may be able to spend much time discussing detailed issues in depth.

**Box 2. Shingikai (advisory councils): source or obstacle of transparency ?**

In Japanese policy processes including those concerning regulations, an important role is played by advisory councils (*shingikai*), or other forms of ad hoc meetings<sup>26</sup> for administrative operations under various names, such as discussion groups (*kondankai*) or study groups (*kenkyukai*). In most cases, competent government authorities serve as the active secretariat: identifying the issues to be discussed; proposing the candidates for such councils and ad hoc meetings; preparing for the discussion, such as providing issue papers and technical data; and drafting reports to be submitted by councils and ad hoc meetings. Use of such processes has been justified by 1) the fact that decisions often require technical expertise and practical knowledge; 2) the corporatist like rationale that consensus among relevant social interests should be achieved. Once the reports are published, their recommendations are regarded as more or less authorised and are likely to be translated into administrative actions, including regulations.

Although in principle those councils and ad hoc meetings have useful functions, criticism has been raised that they are vulnerable to abuse: they may be too susceptible to manipulation by the authorities that support them. The fact that fair and open discussion is not guaranteed has been seen as a weakness of the process: for example, who guarantees that all relevant interests are represented and their voices heard? Foreign trading partners have been among the first to complain that the process should be more open. They are systematically excluded from this policy making process even if they have crucial interests. They charge that regulations, as an overall result of the process, therefore operate in a sub-optimal manner. Foreign voices, when they have been included in those processes as reflected in the Final Report on US-Japan Structural Impediment Initiatives in 1990, have played a catalytic role for progress to date.

The Japanese Cabinet decided in September 1995 several measures to increase the transparency of councils and ad hoc meetings. It was agreed that advisory councils in principle should meet in open session and/or publish minutes. If these are impossible for good rationales which are announced to the public in advance, a summary of discussion at each session should be published. Those efforts across the government have been monitored by the Management and Co-ordination Agency. Its most recent report in March 1998 noted that 73% of advisory councils (*shingikai etc.*) have opened their discussions through open sessions and/or publication of minutes, up from 50% in 1996. The report states that 21.7 % of advisory councils have received opinions from general public.

While the number of advisory councils opening the discussion to the public has recently increased, concerns, especially those by foreign trading partners, remain, since some advisory councils still only publish summaries of discussions, instead of full minutes. In addition, some ad hoc meetings do not publish anything at all.<sup>27</sup>

Furthermore, the goal of transparency may not be achieved if crucial deliberations, such as those on recommendations or interim reports, do not take account of a wide spectrum of views including those of foreign trading partners. In Japanese regulatory reforms, they have played an important role in promoting alternative ideas not heard in the “insider” discussions. Exposing crucial deliberations to public comments will safeguard the decision from being pressured by incumbent interests. Introduction of cross-cutting public notice and comment procedures as announced on October 20, 1998, will have a significant effect in opening regulatory procedures. Such an example is seen in regulatory reform discussions on telecommunications. The US, in its recent submission to the Japanese government on deregulation, has identified further areas that merit specific voluntary efforts in this regard, i.e. retail distribution, ports deregulation and construction.

In the past, very few administrative procedures provided for comments and/or consultation by foreign parties on new or modified regulations before they were adopted. Inquiry commissions were sometimes convened and open public hearings were on occasions held for that purpose. Substantial progress has recently been made. Under the Three year Programme, as discussed in the background report on Government capacity to assure high quality regulation in Japan, the Cabinet recently adopted the proposal for the requirement of public comment procedures made by the Management and Co-ordination Agency. The requirement is applied to all governmental decision-making processes from April 1999. A standardised comment period is set at one month. This measure is expected to contribute to greater transparency in regulatory procedures in Japan. Furthermore, the “Central Government Restructuring Bill” stipulates that when an important bill is formulated, citizens’ opinions including those of experts and interested parties, should be heard.

Box 3. Japanese regulatory system: different forms of regulations and administrative conduct that may have regulatory effect

Type of regulation	Nature	Procedure	Remarks
<i>Horitsu</i> (laws)	Within the Constitution, any regulations can be set by laws.	<ol style="list-style-type: none"> <li>1. Collect views from private sector through an informal or, if necessary, formal channel.</li> <li>2. Exchange views with other ministries departments in an informal manner.</li> <li>3. Start formal consultations with other ministries for agreements on draft.</li> <li>4. Bring the draft to vice ministers meeting for approval.</li> <li>5. Bring the draft to cabinet meeting for an approval.</li> <li>6. Discussed and approved in the relevant Diet committee and in the Diet.</li> </ol>	<ul style="list-style-type: none"> <li>• An example of formal communication channel is <i>Shingikai</i> (advisory council).</li> <li>• Contacted ministries are those deemed relevant by the drafter. Cabinet Legislation Bureau must be always consulted.</li> <li>• Paper-based communication through minister's secretariats.</li> <li>• Members are senior civil servants. Unanimous approval is necessary. No records of discussion available.</li> <li>• Printed laws are available in the Gazette.</li> </ul>
<i>Seirei</i> (cabinet orders)	Orders made by the cabinet in order to implement provisions of the Constitution or laws. <sup>28</sup>	(same as 1. to 5. above)	<ul style="list-style-type: none"> <li>• Printed cabinet orders are available in the Gazette.</li> </ul>
<i>Shorei</i> (ministerial orders)	Orders made by a minister (1) in order to implement the relevant laws / cabinet orders, or (2) in case the laws / cabinet orders delegate authority to the minister. <sup>29</sup>	<ul style="list-style-type: none"> <li>• Only ministers can issue ministerial orders.</li> <li>• No binding procedure exists in government-wide level.</li> </ul>	<ul style="list-style-type: none"> <li>• Printed ministerial orders are available in the Gazette.</li> </ul>
Type of administrative conduct	Nature	Procedure	Remarks
<i>Tsutatsu</i> (internal orders)	Communication tool from officials in higher positions to their subordinates, which may include unified interpretation of laws. Only valid and binding within government organisations.	<ul style="list-style-type: none"> <li>• Although the National Government Organisation Law stipulates that only ministers and heads of commissions and agencies can issue internal orders, it is inherent for the heads of hierarchical organisations to issue them.</li> <li>• No binding procedure exists in national level.</li> </ul>	<ul style="list-style-type: none"> <li>• Senior officials are usually entrusted by the minister to make internal orders.</li> <li>• Consultation with other ministries is rare.</li> <li>• Printed internal orders are available to the public on a request basis.</li> </ul>
<i>Jimu Renraku</i> (communication notes)	Communication tool within bureaucrats, whose content can be anything such as report, interpretation of laws or factual notices. Only valid within bureaucrats.	<ul style="list-style-type: none"> <li>• No binding procedure exists.</li> </ul>	<ul style="list-style-type: none"> <li>• Consultation with other ministries is rare.</li> <li>• Not available to the public</li> </ul>
<i>Gyosei Shido</i> (administrative guidance)	“Administrative actions taken by administrative organs, although without legal binding force, that are intended to influence specific actions of other parties... in order to realise an administrative aim” <sup>30</sup> Internal orders and communication notes can be a basis of administrative guidance as bureaucrats follow them, and sometimes show them to “other parties” in order to make recommendations, suggestions, requests or warnings to “other parties”.		

Information on established regulations (laws, cabinet orders and ministerial orders) is all published. Foreign parties can obtain that information. It is generally not translated into foreign languages except for a few areas. As Japan has notified the WTO, all of Japan's national legislative and regulatory measures are published in “Kanpo” (the official national gazette) and/or “Horeizensho” (Japan's Comprehensive Statute Book), and all of its prefectural regulatory measures are published in “Kenpo” (the prefectural gazette) or its

equivalent.<sup>31</sup> Information on important regulations and policies can be found electronically on individual ministries' and agencies' Internet sites. But, in general the use of the Internet to disseminate regulatory information still lags well behind leading examples among OECD countries.

This openness does not apply to administrative conduct that may have regulatory effect, such as internal orders and communication notes.<sup>32</sup> Even though these regulations have as strong binding power as higher level regulations vis-à-vis bureaucrats in the regulatory decision making process, they are usually neither published nor communicated to the outside. It is sometimes difficult for foreign parties to know the reason why a certain administrative decision is made, especially when the decision is on the basis of these lower level regulations. This is one important source of the non-transparency of the Japanese regulatory system for foreign parties (see Box 3).

Concerning the openness of appeals procedures, foreign parties have three avenues to lodge appeals against administrative actions. The first is to address their appeals directly to the administrative bodies (superior bodies, if they exist) under the procedures established in the Administration Appeal Law. This should be the most streamlined and speedy procedure according to the Japanese government, because appeals are usually treated directly by administrative agencies. A drawback is that no time limit is defined in the Administration Appeal Law. In some cases, inquiry commissions can be convened to treat appeals in a neutral way, if special provisions are established in individual laws. In general, whether or not they address appeals, they can file a suit in the courts under the Administration Case Litigation Law. Even if in the cases where the Administrative Appeals are required by laws before suits, when no decision concerning an appeal is rendered within three months from initiation of the appeal, then foreign parties can file a suit in the courts under the Administration Case Litigation Law.

The second way to appeal is to file a suit in the courts against administrative actions for the purpose of cancelling them, as defined under the Administration Case Litigation Law. However, it may be time-consuming, especially considering the underdevelopment of Japanese legal services (see background report on Government capacity to assure high quality regulation in Japan about issues on Japanese legal services).

The third way is to lodge an appeal with the Office of Trade and Investment Ombudsman (OTO - see Box 5). The OTO is an independent government body which has the vocation to deal with market openness issues at the government-wide level. The appeals treated here tend to be limited to complaints within the existing regulatory system and OTO's authority has not been used to change the system itself. Among the three avenues of recourse, the most frequently used by foreign firms has been OTO. However, OTO cases have declined recently, too, possibly reflecting the disappointment by foreign parties about the limitation of its authority<sup>33</sup>. Foreign firms point out the risks arising from bringing issues publicly to the appeal procedures, because of the wide range of discretionary power of regulatory agencies. Foreign firms have to be concerned by possible retaliation by the agencies.

## **2.2 Measures to ensure non-discrimination**

Application of the non-discrimination principle aims to provide effective equality of competitive opportunities between like products and services irrespective of country of origin. Thus, the extent to which respect for two core principles of the multilateral trading system -- Most-Favoured-Nation (MFN) and National Treatment (NT) -- is actively promoted when a country develops and applies regulations is a gauge of its overall efforts to promote trade and investment-friendly regulation.

Preferential agreements give more favourable treatment to specified countries and are thus inherent departures from the MFN principle. The extent of a country's participation in preferential agreements (which overall can be trade-creating or trade-diverting) is not in itself indicative of a lack of commitment to the principle of non-discrimination. However, in assessing such commitment it is relevant to consider the attitudes of participating countries towards non-members in respect of transparency and the potential for discriminatory effects. Third countries need access to information about the content and operation of preferential agreements in order to make informed assessments of any impact on their own commercial interests. In addition, substantive approaches to regulatory issues such as standards and conformity assessment can introduce potential for discriminatory treatment of third countries (if, for example, standards recognised by partners in a preferential agreement would be difficult to meet by third countries).

Japan is firmly committed to the MFN principle, although there are limited exceptions to this in the investment field (see below). The Japanese government has encouraged regulatory bodies to respect the non-discrimination principle, in their application of domestic regulations. Japan has adopted the MFN principle under the GATS with no exception. Furthermore, as Japan is not engaged in any kind of preferential trade agreement, it does not give more preferential treatment to some trading partners than to others under any regional framework. The only regional co-operation entity in which Japan takes part in is APEC. Since APEC has adopted "open regionalism", Japan respects the MFN principle in this regard.

Although the MFN principle is apparently well-respected in the Japanese regulatory system, some concerns have been assessed relating to Japan's commitments resulting from bilateral trade talks with major trading partners such as the United States, EU, and Canada. One concern is the risk of giving more priority to specific market openness issues raised by particular trading partners than to other issues.<sup>34</sup> The process may give those trading partners relatively large trade benefits, even though the issues are resolved without neglecting non-discriminatory principle.

With regard to the national treatment principle, there are several specific examples of formal exceptions for which trading partners have raised concerns: prohibition against partnerships between Japanese lawyers and foreign legal consultants and against the employment of Japanese lawyers by foreign legal consultants; and discrimination between foreign and domestic banks in funding mechanisms via the Bank of Japan. With regard to inward investment, Japan still maintains some notable exceptions to national treatment through regulations defined in the Foreign Exchange Law and other individual laws. Under the Foreign Exchange Law, a party desiring to acquire a certain percentage of shares in certain sectors through direct investment in Japan must first notify the Ministry of Finance. Affected sectors can be categorised into three groups. First, sectors which are liable to be detrimental to national security, to hinder the maintenance of public order, or to obstruct the protection of public safety. Telecommunications services (only NTT)<sup>35</sup> and electricity are notable examples of sectors that fall into this group. Second, sectors for which Japan has maintained reservations in the OECD code for the liberalisation of the movement of capital.<sup>36</sup> Third, Japan also maintains limited investment barriers based on reciprocity.<sup>37</sup>

Even though the Japanese regulatory system has evolved to reduce formal exceptions to the national treatment principle, many trading partners express their concerns about *de facto* discrimination in various fields. This *de facto* discrimination may be due to the fact that foreign firms, as newcomers, often lack the level of information that domestic incumbents have from their long-term relationship with regulators. When other administrative conduct that may have regulatory effects is applied, this scenario becomes particularly probable. Illustrative examples raised by trading partners are numerous. For example, the majority of domestically-produced fork-lift trucks and other industrial trucks (FLT) are placed in the "small-sized special m.v." category whereas the great majority of imported FLT are in the "large-special m.v." category, and the latter group is subject to stricter requirements. Foreign motorcycles tend to be large size which is more suitable for tandem ridings. Yet, the motorcycle market in Japan, in particular that for the large size motorcycle, is distorted due to the prohibition of tandem ridings on national expressways (see Section 3).

Moreover, foreign investors must wait for 30 days, counting from the date the Minister of Finance and the minister with jurisdiction over the sector receive the notification, before they can effectively start to materialise investment activities. Further, when it is deemed necessary to examine whether the notified direct investment 1) is liable to be detrimental to national security, to hinder the maintenance of public order, or to obstruct the protection of public safety; 2) causes a notable adverse effect on the smooth operation of the national economy, the Minister of Finance and the minister with jurisdiction over the sector are allowed to examine the case for a maximum of five months from the date of notification.<sup>38</sup>

Concerning non-discrimination, there seem to be more problems at the level of self-regulation of Japan's numerous industry associations and professional services associations than at the level of government regulations. Many Japanese ministries and agencies delegate technical regulations to these kinds of associations. Some associations, on occasion, apply self-regulation in a discriminatory way between their members and potential foreign competitors. Many concerns are expressed by trading partners about discriminatory practices of those associations.<sup>39</sup>

Japan is one of the most highly regulated countries in professional services, such as legal and accounting services.<sup>40</sup> The associations of these professional services apply many cases of exclusionary self-regulation, not allowing foreign counterparts the same opportunities to practice their professions in Japan as their own members. In addition, concerns are raised by trading partners about discriminatory practices on the part of Japanese manufacturers of flat glass: withholding of supply, use of restrictive trade associations, discriminatory pricing against customers who purchase foreign flat glass and the glass distribution network.<sup>41</sup>

Checking the drafting of regulations for their conformity with international treaties, e.g. those that include MFN treatment and national treatment, is the co-responsibility of the Cabinet Legislation Bureau and the Ministry of Foreign Affairs (MOFA). When higher level regulations (laws and cabinet orders) are discussed at the cabinet level, these two bodies should monitor whether they conform with Japanese international obligations and recommend any necessary changes. However, there is no central government body monitoring conformity with international treaties when ministries and agencies are implementing regulations, that is, at the level of administrative practices. Furthermore, as explained in the previous subsection, since lower level regulations (ministerial orders, internal orders, and communication notes) are not subject to cabinet level discussions, they are not monitored by these two bodies.

### **2.3 *Measures to avoid unnecessary trade restrictiveness***

To attain a particular regulatory objective, policy makers should seek regulations that are not more trade restrictive than necessary to fulfil a legitimate objective, taking account of the risks that non-fulfilment would create. Examples of this approach would be to use performance-based rather than design standards as the basis of a technical regulation, or to consider taxes or tradable permits in lieu of regulations to achieve the same legitimate policy goal. At the procedural level, effective adherence to this principle entails consideration of the extent to which specific provisions require or encourage regulators to avoid unnecessary trade restrictiveness (and the rationale for any exceptions), how the impact of new regulations on international trade and investment is assessed, and the extent to which trade policy bodies as well as foreign traders and investors are consulted in the regulatory process.

Japan does not have explicit provisions requiring administrative procedures to be trade and investment friendly. Individual ministries and agencies are responsible for applying regulations and administrative procedures in ways that do not affect the free flow of trade and investment. They have often used their regulations in an “unnecessarily trade and investment restrictive” way in cases such as “demand-supply adjustment clauses” according to which they can prohibit new entry because of excess supply capacity (even when it is foreseen); and officially authorised cartel arrangements. Restrictive regulations have often

been justified as to help achieve non-economic policy objectives such as safety. These regulations, while not explicitly discriminatory against foreign firms, have negative impact on trade and investment in many cases. Furthermore, these measures have been suspected to be used to protect vested interests of domestic firms.<sup>42</sup> As a result, with the notable exceptions of ministries overseeing sectors traditionally exposed to foreign competition, ministries and agencies tend to prefer regulations giving them close control of sectors rather than those enhancing market competition, economic efficiency and trade and investment.

One feature in Japanese administrative culture is that Japan tends to give regulators wide discretion in regulatory processes. Even though the Administrative Procedure Law obliges regulatory bodies to enhance administrative transparency and efficiency, it has not lived up to expectations. Predictability of processes can significantly reduce compliance burdens of regulated firms. Japanese bureaucrats should pay much attention to the effects of policy tools on the economy and on international trade and investment, while respecting proper administrative procedures defined at the Administrative Procedure Law when they choose their policy tools.

There is no provision which requires individual ministries and agencies to take account of the potential impact of their new or modified regulations on trade and investment. Moreover, contrary to most OECD countries, Japan does not have a well-established system of regulatory impact assessment for proposed regulations. Therefore, the choice of more trade and investment friendly regulations and/or administrative procedures relies upon the discretion of individual ministries and agencies (see the discussion on regulatory impact assessment in the background report on Government capacity to assure high quality regulation in Japan).

Trade restrictive administrative procedures are found in numerous fields. Regulations related to construction business and building materials have been frequently noted as unnecessarily burdensome and complicated by major trading partners such as the US, the EU, and Canada.<sup>43</sup> Japan has applied a complex regulatory system in this sector for reasons of Japanese cultural difference (preference for wooden houses and high risk of fire) and geographical/climatic difference (earthquake and typhoon). However, the complexity of the regulatory system of this sector has been pointed out as major trade restricting obstacle. Japanese quarantine and inspection procedures for fresh fruits and vegetables, flowers, frozen foods, and food supplements are also frequently criticised issues for unnecessary trade restrictiveness by many trading partners. Concerns expressed by trading partners are numerous in other sectors: burdensome regulations for electricity equipment (turbines and compressors, standby generator sets, power main signalling devices etc.) under the High Pressure Gas Law, the Electricity Utilities Industry Law and others (see section 3); onerous tariff and licensing procedures, and burdensome certification procedures in the telecommunications sector; complicated examination procedures for telecommunications equipment; long customs clearance processing time, high user fees, short operation hours, and non-uniform application of customs regulations; excessively long and costly approval procedures for medical devices; costly and burdensome testing methods for pharmaceuticals; regulation allowing only paper-base invoice in spite of the Electronic Data Interchange (EDI) system; new vehicle registration process; licensing procedures for new entrants to the insurance market and restrictions on asset management; and application of unit testing rather than type approval for machinery.

Burdensome regulations have hampered inward investment as well. Complex legal provisions related to mergers and acquisitions have been pointed out as an important obstacle to direct foreign investment in Japan, though other cultural and institutional barriers such as a high level of cross-shareholding between allied companies; a low percentage of publicly-traded common stock; widespread mistrust of foreign ownership; reluctance of *keiretsu* members to see fellow members under foreign control; and non-transparent accountancy regulations are also noted.<sup>44</sup>

Despite the apparent lack of general provisions to avoid unnecessary trade restrictiveness in the Japanese regulatory system, some progress has been made in this regard. In fact, the Office of Market Access

(OMA: cabinet level meeting in the context of OTO) adopted the “Policy Actions on Market Access Issues as Concerns Standards, Certification and Others” in July 1997. It stipulates that government bodies should avoid the use of standards, technical regulations and conformity assessment procedures including sanitary and phyto-sanitary regulations which are unnecessary obstacles to trade.<sup>45</sup>

Apart from legal provisions, MITI and MOFA play a role for this purpose in the Japanese administrative system. As MITI is mainly in charge of trade policy, it makes comments on regulations from the trade perspective through deliberations at the drafting stage, when new regulations are proposed for cabinet discussions. As MOFA verifies the changes in regulations from the point of view of conformity with international treaties, it should also check whether regulations have trade restrictive effects against those treaties. Hence, it is possible for newly proposed regulations to be checked from an international perspective. However, as some regulations contain specific technical elements related to specialised ministries and agencies, it can be very difficult for trade policy bodies to correctly assess the trade and investment impact. In addition, when regulations are established through ministerial orders, internal orders, or communication notes, they escape oversight by these trade policy bodies.

The lack of open consultation between government bodies (especially between trade policy officials and sectoral officials) makes serious regulatory reforms difficult, even if they are politically supported (even strongly pushed by prime ministers such as Hosokawa and Hashimoto) or if they are the subject of commitments at trade talks. Instead, sectoral regulatory authorities tend to prefer the “deregulation process” to organised consistent “regulatory reforms” at the government-wide level, because the former option implies that they can make relatively minor concessions and preserve their controlling power in the sector (see Box 4).

**Box 4. Lack of intra-governmental co-ordination impeding trade flows**

(An example of trade facilitation)

Japan introduced the Customs electronic data interchange (EDI) system in 1978. Today approximately 90% of import/export declarations are processed through the EDI system. With the EDI system, exporters, importers and their customs brokers can submit their declarations electronically from their offices. The EDI system improves the accuracy of declarations and speeds up customs procedures as a whole.

However, customs procedures are not the only regulations at the border. There are others such as quarantine, sanitary, phyto-sanitary, food security, and import/export licenses. Under the Japanese Customs law, merchandise not cleared by border controls of agencies other than Customs cannot obtain import permission from Customs. Among other agencies' regulations, until very recently, trade-related procedures were not computerised nor linked electronically to the Customs EDI system. The lack of electronic linkage among computer systems reduces the value of the Customs EDI system from the point of view of paperless and smooth information flow and avoidance of input duplication and error. That results in a delay to import clearance, raises storage costs, and reduces the competitiveness of foreign products. Since 1990, the US has complained about the lack of cooperation between Customs and other agencies, requesting Japan to establish an integrated import processing system. Other interested bodies have echoed these concerns.

In 1997, the sanitary and phyto-sanitary EDI system and the food security EDI system were linked electronically to the Customs EDI system. But, MITI's import/export license EDI system and the port authority's EDI system are under development and the possibility of their linkage to the Customs EDI system has just been taken into consideration.

In addition to the role of monitoring regulations from an international perspective, MITI operates a training program on the rules of the WTO and other international trade policies in order to enhance market openness. This program is for all government officials. It is deemed to improve public officials' perception of market openness. But as it is on voluntary basis, its impact to date has been limited.

One of the most important steps in favour of market openness which has been taken by Japan was the establishment of the Office of Trade and Investment Ombudsman (OTO) <sup>46</sup> in 1982. The OTO, a unique organisation, among OECD members, aims to reduce obstacles to market openness by receiving complaints on market access, relating to imports or inward investment, and by organising inter-ministerial co-ordinating efforts to deal with those complaints. The OTO has dealt with more than 500 complaints concerning market access. It has made several reports on major problems of market access and has taken government level policy actions to enhance market openness (see Box 5).

#### Box 5. OTO: the Japanese way to enhance market openness

**Objective:** The OTO (Office of Trade and Investment Ombudsman) was established on January 30, 1982 for the purpose of improving market access to Japan, through receipt and processing of complaints concerning market opening issues, including procedures for import of goods and services, direct investment in Japan, and government procurement.

**Submission of complaints:** Complaints are received mainly by the Secretariat of the OTO, established at the Co-ordination Bureau of the Economic Planning Agency. They can be brought to other relevant sections of the Japanese government, Japanese diplomatic missions and the JETRO. In the latter cases, they will be transferred to the OTO Secretariat. Complaints may take any form such as direct visit, mail, phone and/or E-mail (Internet), if they are clearly understandable and concern specific matters. As a general rule, they should be addressed directly by a complainant. However, proxy complaints will be accepted without the name of a complainant through foreign government organisations, foreign diplomatic missions, foreign government affiliated trade promotion organisations and/or other organisations approved by the OTO (e.g. foreign chambers of commerce and industry in Japan, major Japanese chambers of commerce and industry and other major business bodies).

**Solving complaints:** An (initial explanatory) answer will be delivered to the complainant within 10 days after the submission of the complaint to the OTO. If it takes more than one month to cope with the issue, the complainant will be kept informed by progress reports at least once every month. When the complainant does not agree with the explanation given by the relevant ministries or agencies, the issue will be deliberated by the Grievance Resolution Committee. Any issue which takes more than three months to cope with will also be deliberated by the committee. The final result will be reported to the complainant in written form.

**Intra-government communication:** In the best case, issues are resolved at the level of the OTO Co-ordination Meeting whose members are working level bureau directors. Otherwise, it can go up to the OTO Executive Meeting whose members are vice-ministers of ministries and agencies concerned. In extreme cases, the OMA (Office of Market Access: established on February 1, 1994 to reinforce the OTO), which is presided over by the Prime Minister and whose members are ministers, will decide. Apart from this administrative line of discussion, the MAOC (Market Access Ombudsman Council) is established to gather more neutral opinions and to give advice to the OMA. The MAOC is composed of distinguished scholars, business leaders and others. The Grievance Resolution Committee which is established under the MAOC will discuss any issue which cannot be resolved at the working level co-ordination meeting.

**Accomplishments:** As of February 25, 1998, the OTO has received a total of 568 complaints. 552 of those complaints have been processed. In 185 cases, Japanese procedures have been modified to facilitate imports. The OTO has given explanations on 209 other complaints judged to be based on misunderstandings.<sup>47</sup> Since FY 1992,<sup>48</sup> the MAOC has compiled yearly its "Recommendations on Market Access Issues as concerns the Standards, Certification and Others" concerning problems indicated by foreign and domestic businesses. Through this process, the MAOC has dealt with 293 cases, and has made 112 recommendations. Based on these recommendations, the OMA has taken "Policy Actions on Market Access Issues as concerns the Standards, Certification and Others" to implement them at the administrative level. Source: EPA document.

Despite its positive role in enhancing market openness and reducing unnecessary trade restrictiveness of regulations, the OTO seems to be losing the initial positive view of some trading partners.<sup>49</sup> According to those trading partners, the OTO has become another example of the “Japanese way of enhancing market openness”: the focus of activities is increasingly on border measures, shying away from issues behind the border. They evaluate the OTO as follows: its strengths are its policy objectives and its composition, which includes foreign representatives, and its weaknesses are its lack of authority vis-à-vis other ministries and agencies and the fact that most issues handled lead to minor improvements in implementation of regulations rather than more fundamental change in regimes. They believe that even if most activities of the OTO are helpful to solve specific minor market access problems, those are far from sufficient to effectively enhance market openness in Japan and to contribute to structural reforms of the Japanese economy.

#### **2.4 Measures to encourage use of internationally harmonised measures**

Compliance with different standards and regulations for like products often presents firms wishing to engage in international trade with significant and sometimes prohibitive costs. Thus, when appropriate and feasible, reliance on internationally harmonised measures (such as global standards) as the basis of domestic regulations can readily facilitate expanded trade flows. National efforts to encourage the adoption of regulations based on harmonised measures, procedures for monitoring progress in the development and adoption of international standards, and incentives for regulatory authorities to seek out and apply appropriate international standards are thus important indicators of a country’s commitment to efficient regulation.

In Japan, government’s involvement in standards and conformity assessment procedures is relatively active and Japanese consumers have a high level of confidence in the Japanese quality and safety systems. Some Japanese people have even expressed concerns that international alignment might degrade the quality and safety of products. Moreover, there is no general and standard provision which requires the use of internationally harmonised standards (see Box 6).

##### **Box 6. Japan’s standards and conformity assessment systems**

The standards and conformity assessment system in Japan has a dual structure. The government administers a variety of mandatory standards, and multiple public and private organisations manage a wide range of voluntary standards. The government is very actively involved in standards and conformity assessment.

##### ***Mandatory Standards***

Mandatory standards are enforced through legislation, and compliance is governed by a certification system. Government-designated testing laboratories inspect for conformity. Compliance with mandatory standards is required before a product can be sold in, and imported to, Japan.

A partial list of legislation defining mandatory standards (numbers of standards in brackets): Consumer Product Safety Law (6), Electrical Appliance and Material Control Law (498), Pharmaceutical Affairs Law(2014), Food Sanitation Law (377), Fertiliser Control Law (126), High Pressure Gas Control Law (2), Safety Regulations for Road Vehicles (274), Law concerning the Safety Assurance and Quality Improvement of Food (150), Building Standards Law, Industrial Safety and Health Law, Telecommunications Enterprise Law, Plant Protection Law, Measurement Law, Law concerning Screening of Chemical Substances and Regulation of their Manufacture, and Radio Law.

### ***Voluntary Standards***

Voluntary standards are used for safety, compliance, and quality assurance. Voluntary marks are required *de facto* in many cases, because of their marketing leverage. Testing and certification bodies are designated by ministries which administer each voluntary standard.

**The JIS Mark:** a widely used quality mark applicable to over 1,000 different manufacturing products and encompassing 8,161 standards. MITI administers JIS and designates qualified Japanese and foreign testing organisations. Compliance with the JIS improves marketability and is also an important element in government procurement. MITI is planning to enlarge the list of accredited foreign testing organisations.

**The JAS Mark:** a quality assurance mark for beverages, processed foods, forest products, agricultural commodities, oils and fats, and processed goods made from livestock, fishing, and forestry raw materials. The Ministry of Agriculture, Forestry, and Fisheries administers 354 JAS marks.

**Certification Marks:** additional voluntary certification marks administered by various organisations. The “SG” mark is a quality mark administered by Japan’s Consumer Product Safety Association. The “ST” mark is a safety mark administered by the Toy Safety Control Administration, a self-regulatory commission. In addition, the “ECO” mark is used for environmental standards and the “G” mark for design quality, etc.

**Quality Control:** Japan has developed a good quality control system, driven by the Japanese Industrial Standards Committee. This has made the introduction of internationally harmonised quality control standards such as ISO very slow. Now, Japan is actively introducing them and participating in international harmonisation activities.

*Sources:* WTO, *Trade Policy Review of Japan*, January 1998 and John S. Wilson, *Standards and APEC: An Action Agenda*, October 1995.

Trading partners are currently demanding the alignment of Japanese standards and certifications to international norms in numerous fields such as adoption of International Electrotechnical Committee standards for many electrical products; adoption of ISO standards and performance-based standards for various building materials and tank containers; NTT’s adaptation of international standards with regard to line connectivity i.e., standardised open interfaces; internationally-accepted labelling standards for processed foods and dairy products; adoption of international regulatory framework for food additives; adoption of global standards of financial disclosure, supervision, accountancy rules and asset valuation; harmonisation of various regulations related to motor vehicle and component with UN-ECE and EU regulations; and recognition of ISO measurement criteria for recreational craft.

The WTO paid attention to this matter, too. It reports in the 1998 Trade Policy Review that “From Japan’s perspective, ‘Japanese standards and certification systems are now comparable with those of other countries in terms of transparency and conformity with international standards’. From the perspective of some trading partners, however, ‘access to the market continued to be hindered by exclusionary business practices and various non-tariff measures. These include burdensome testing, inspection and customs clearance procedures, the use of complex standards and difficulties of access to distribution networks’.”<sup>50</sup>

In spite of these limitations, Japan has recently announced several initiatives to make progress in this regard. The 1997 Policy Actions on Market Access Issues of the OMA states that ministries and agencies are encouraged to use internationally harmonised standards and certification procedures when they take the actions proposed in the grievance resolution process of the OTO. According to the Policy Actions, they are also encouraged to actively use foreign conformity assessment bodies, to promote mutual recognition and to simplify and speed up conformity assessment procedures.

The new Three year Programme also stresses international harmonisation of regulations in order to promote fundamental reforms of Japan's economy and society to attain internationally open, free, and fair systems. In addition, Japan has the role of APEC/PASC (Pacific Area Standards Congress) chair, and in this context, four case studies are being done on the issue of alignment of national standards with international ones. These studies are contributing to deepening understanding of the issue, including quality of international standards themselves.

Besides, there has also been progress made at the individual industry level. MITI has introduced 237 international standards in the list of technical standards requested under the Electrical Appliance and Material Control Law, instead of 120 aligned standards before. Through the first Three Year Programme (1995-1997), 1,700 JIS standards out of 8,000<sup>51</sup> have been aligned to international standards. Japan introduced the OECD principle of Good Laboratory Practice (GLP) into the Law concerning the Examination and Registration of Manufacture of Chemical Substances. In addition, Japan's accession to the revised 1958 UN-ECE Agreement on automotive sector was submitted to the Diet on 3 March 1998. This is expected to have a positive impact on harmonisation in the sector (see section 3).

There have been also recent moves towards performance-based standards, notably in areas such as building materials and electricity equipment. WTO Agreements, particularly TBT & SPS agreements, have played an important role in maintaining transparency and contributing to harmonisation in standards development. Japan recognises the importance of the obligations under those agreements, including notifications of draft technical regulations and standards. It has established practices aiming to ensure them. Ministries handling technical regulations & standards have familiarised themselves to the operation of the system.

Therefore, the picture is mixed, with continuous foreign complaints and ongoing initiatives towards harmonisation. One fundamental problem lies in the lack of data in assessing progress in harmonisation in various areas. This problem is not unique in Japan. Such data collection and assessment may be a useful step for Japan making further concrete progress in this field. Concerns are raised also about the effectiveness of cross-cutting commitment. This is because the Policy Actions and Three year Programme's statements have less binding power than individual laws on which individual ministries and agencies administering their standards and conformity assessment rely much more. Based on more precise assessment, Japan may consider strengthening such cross-cutting commitment of harmonisation.

## **2.5 *Recognition of equivalence of other countries' regulatory measures***

The pursuit of internationally harmonised measures may not always be possible, necessary or even desirable. In such cases, efforts should be made in order to ensure that cross-country disparities in regulatory measures and duplicative conformity assessment systems do not act as barriers to trade. Recognising the equivalence of trading partners' regulatory measures or the results of conformity assessment performed in other countries are two promising avenues for achieving this result. In practice, both avenues are being pursued in Japan in various ways. Recognising certification given to foreign products by foreign laboratories is one example. Such recognition can be accorded unilaterally, but also through the mechanism of a Mutual Recognition Agreement (MRA) between trading partners. Another example arises when certification operates through self-declaration of conformity by manufacturers; in this case, recognition of equivalence means that declarations of conformity by foreign manufacturers are also accepted: foreign (as well as domestic) producers can assess the conformity of their product with requirements set in a given market as they deem appropriate and will be treated the same way by regulatory authorities. The latter may then test products on the market under established procedures and take necessary measures as warranted, regardless of the origin of products.

In Japan, government's involvement in conformity assessment procedures has been considerable. Ministries often designate certification bodies for particular areas. Such bodies are often given de facto monopolistic function to certify designated products or services. These procedures are often criticised by trading partners on various accounts: lack of transparency in the procedures; high costs of certification; peculiarly burdensome procedures; and reluctance to accept the data obtained through internationally accepted methods.

Many trading partners as well as Japanese domestic businesses are demanding Japan to make further progress in various fields such as acceptance of foreign standards, foreign test data, foreign testing organisations and test laboratories for construction and building materials; acceptance of foreign clinical data in the acceptance of medical devices and pharmaceuticals; generalised recognition by Japanese standards related laws of European wide accreditation bodies (European Co-operation for Accreditation: EA) or of equivalent international bodies (ILAC for laboratory accreditation and IAF for accreditation of quality systems certification); recognition of motor vehicle test results from foreign testing institutes as part of completion inspection; recognition of Dutch inspection systems for cut flowers and flower bulbs; recognition of foreign test data obtained through good practice test methods for chemical residues in meat products; acceptance of all ingredients of cosmetics on EU lists; support for the efforts of private sectors with foreign parties to resurrect the ISO for boilers and pressure vessels; recognition of the validity of the physical inspection and certification of tank containers for the carriage of dangerous goods when this is authenticated and witnessed by agencies such as Lloyds Register, Bureau Veritas and Germanischer Lloyd; recognition of Canadian fumigation treatment for hay; recognition of inspections carried out by competent foreign bodies similar to NKK (Nippon Kaisi Kokkai: fire detection); wider recognition of foreign countries' investigation data pertaining to alcoholic beverages ingredient analysis; and no re-inspection if vessel was approved abroad.

However, some progress has recently been made through new cross-cutting initiatives such as:

- The Policy Actions of the OMA encourage regulators to actively use foreign conformity assessment bodies and to promote mutual recognition;
- The Social and Economic Plan Action Plan (adopted in 1997) stipulates that Japanese standards bodies should accept foreign data, introduce mutual recognition systems, and make the transition to self-certification for appropriate items;
- The OTO 1996 report states that some foreign inspection data are authorised and administrative discretion to assess conformity should be reduced.

Related progress has recently been made in telecommunication equipment. The MPT submitted a draft law to the Diet on March 16, 1998 for the establishment of a system allowing Japan to accept certifications and test results for telecommunications terminal equipment and radio equipment from conformity assessment organisations (domestic and foreign) recognised by MPT regardless of agreements for mutual recognition. The foreign organisations do not have to be recognised by foreign governments to be recognised by MPT. The draft law was approved on April 30, 1998. This is a first in allowing foreign bodies to conduct certifications in the Japanese system for mandatory standards area.

Japan introduced an accreditation system for testing laboratories in 1997. Accreditation bodies would assess and authorize testing competence of laboratories, based on internationally accepted guidelines. In October 1998, the Asia-Pacific Laboratory Accreditation Co-operation (APLAC) approved the participation of Japanese accreditation bodies. This opens the way in Japan for recognising equivalence of wide-ranging foreign testing results under APLAC umbrella with domestic testing results.

In addition, some trading partners positively appraise Japanese efforts to recognise regulatory measures and conformity assessment results performed in their countries. Examples of positive action include acceptance of EU official tests for frontal crash tests for automobiles; and commitment to incorporate the guidelines on acceptance of foreign clinical data into national regulations for pharmaceutical products. MITI has accepted 62 foreign testing bodies for technical regulations under 9 laws in its jurisdiction. Japan has recently amended the Industrial Standardisation Law so as to enable third-party certification bodies - domestic and foreign - to issue JIS mark. The number of accepted foreign inspection bodies are 142 at the moment. MITI has also transferred 126 items of government certification of 4 standard related laws under its jurisdiction to supplier's declaration scheme. Japan's accession to UN/ECE Agreement in automotive sector also has opened the way for more positive attitude towards accepting foreign certification on safety in the sector.

Japan has also engaged in various MRA negotiations with major trading partners, even if not many have yet been concluded (see table). In addition, Japan is asked by trading partners to engage in MRA negotiations in various fields such as: 1994 joint announcement on co-operation for mutual recognition in the field of building standards with Canada; test data and certification for medical devices by the EU and Taiwan; motorised agricultural and construction machinery<sup>52</sup> by the EU.

Table 1. Japan's participation in MRA negotiations

Partner	Partner	Sector	Concluded	Effective Date	Type of Recognition
EU	Japan	telecommunications equipment (including electromagnetic compatibility) electrical equipment (including electromagnetic compatibility) machinery pressure equipment medical devices pharmaceutical GMP chemicals GLP construction materials personal protective equipment	no		ACC CERT
APEC	APEC	electrical and electronic equipment	no		ACC CERT
		food and food products	yes	97.8	
		telecommunications equipment (including electromagnetic compatibility) and electrical safety)	no	99.7 (target)	
Australia	Japan	low voltage equipment pharmaceuticals GMP medical devices pressure equipment housing and construction automotive products	no		

GMP: Good Manufacturing Practices  
ACC: Conformity assessment dealing with the acceptance of data  
CERT: Conformity assessment dealing with certification  
GLP: Good laboratory practices

Source: Information provided by the government of Japan.

In sum, Japan's announced policy goal is supportive of recognition of equivalence of other countries' regulatory measures. Recent progress is consistent with such a goal and welcomed by trading partners as contributing to market openness. Considering wide-ranging complaints made by trading partners, however, the question is speed and momentum. Are current moves going to be extended to cover all the areas where trade concerns are arising? It is difficult to assess. However, in order to better achieve the policy goal of the Japanese government, a government-wide initiative to promote, wherever possible and appropriate, acceptance of foreign certifications and/or to introduce less burdensome conformity assessment procedures such as manufacturer's declaration of conformity looks promising.

## **2.6 *Application of competition principles from an international perspective***

Foreign trading partners have claimed that not only government regulatory actions, but also practices by private firms or semi-public organisations, have posed obstacles for market openness in Japan. The lack of adequate procedures to ensure transparency, pointed out in section 2.1, may have contributed to these private practices. Such concerns have been widespread, and trading partners have recommended that Japan boost its efforts to vigorously implement the Anti-Monopoly Law.

The discussion has covered various aspects of the enforcement of competition laws and policy: strengthening the investigatory powers of the Japan Fair Trade Commission (JFTC)'s; strengthening penalties and sanctions; introducing a wider range of private remedies, including private injunctions and private damage relief; expanding the capacity of the JFTC. Complaints also point to the "grey" area where government functions, which are often regulatory, are delegated to private bodies or government regulation is seen to encourage anti-competitive behaviour by firms. In this regard, requests have arisen for more vigorous oversight by the JFTC of private practices relating to: administrative guidance; trade associations' activities, many of which are authorised by government regulation; and various "private" regulations. Trading partners have also urged further efforts to abolish exemptions to the Anti-Monopoly Law as well as more vigorous intervention by the JFTC in the regulatory decision making process primarily by strengthening its advocacy role.

The benefits of market access may be reduced by regulatory action condoning anti-competitive conduct or by failure to correct anti-competitive private actions that have the same effect. It is therefore important that regulatory institutions make it possible for both domestic and foreign firms affected by anti-competitive practices to present their positions effectively. The existence of procedures for hearing and deciding complaints about regulatory or private actions that impair market access and effective competition by foreign firms, the nature of the institutions that hear such complaints, and adherence to deadlines (if they exist) are thus key issues from an international market openness perspective.

If regulatory conduct affects the competition process impairing access to a particular Japanese market by foreign firms, the affected firms may file a complaint to the OTO. Even if the source of the market access problem arises from private conduct, then complaints may also be brought before the OTO.

Furthermore, anyone may report a suspected violation of the Anti-Monopoly Law to the JFTC and request an investigation be instituted pursuant to article 45 of the Anti-Monopoly Law. There is no discrimination on the treatment of complaints that either a foreign firm or domestic firm may raise. The JFTC has the duty to carry out a necessary investigation into relevant matters pertaining to the case in question. The JFTC does this in order to check whether the case may be relevant to the Anti-Monopoly Law or not and to determine whether there is violation or not. If the report above is done in writing and specifies concrete facts, the JFTC will send notification of the result to the person who made the report. The JFTC does not disclose any information concerning petitions because it is believed that the JFTC will face difficulty in obtaining co-operation from a complainant wishing to guard his or her identity secret. The JFTC gives explanations of its decisions to the complainant on demand, all the while taking business confidentiality into account. After a full

investigation, decisions to order elimination measures are made in writing. They include a description of the facts found, the application of law made by the JFTC and the contents of the elimination measures. All the decisions to order elimination measures are made public. An appeal for the cancellation of the decision must be brought within thirty days (three months in case of decisions on monopolistic positions) from the date on which the decision becomes effective (i.e. the date of receipt by the parties of the decision, article 77). The delay between the issuance of decisions and their publication depends on the types of decisions. In the case of and hearing decisions, the delay is a few days, i.e. the time that is deemed necessary to reach the parties concerned. On the other hand, in the case of recommendation decisions, the decisions are published annually, since each recommendation itself is made public at the time of its issuance.

The JFTC may, even when an act in violation has already ceased to exist, order the entrepreneur to take necessary measures, if it is within one year (three years in case of surcharge payment orders) since the date of discontinuation of the act. The length of time period for reaching recommendation (starting from the initiation date of the formal investigation) is generally a half to one full year, although there are frequent exceptions to this time length. There is virtually no difference in time length for reaching the verdict with regard to complaints from foreign as compared to domestic firms.

Notwithstanding the formally equivalent treatment between foreign and domestic firms, a perception still exists on the part of many foreign firms that they do not, or would not, receive equivalent treatment. It may be the case that perceived differential treatment does not arise out of anything specific to the application of competition law and policy, but rather as a result of the interaction between other regulatory schemes and the competition law. For instance, it has been suggested that restrictions on the number of Japanese lawyers (*bengoshi*), the prohibition against partnerships between Japanese lawyers and foreign legal consultants (*gaikokuho-jimu-bengoshi*) or the hiring of Japanese lawyers by foreign legal consultants, restrictions on quasi-legal professionals, and the limitations on the ability of foreign legal consultants to confer with Japanese government agencies or authorities on behalf of clients may limit the effectiveness of foreign firms in giving adequate voice to their market access concerns. This problem may be exacerbated by continuing limitations on private injunctive relief and private damage actions for alleged violations of the Anti-Monopoly Law.

In addition to these procedural concerns, it is also possible that during the period of lax antitrust enforcement by the JFTC (which is changing as documented in the background report on The Role of competition policy and enforcement of regulatory reform) certain market access problems of foreign firms under Japanese antitrust laws were hidden or ignored because the lax enforcement could affect both foreign and domestic firms. As a consequence the past weak anti-cartel enforcement (particularly with respect to bid-rigging),<sup>53</sup> combined with past copious exemptions from the application of the Anti-Monopoly Law, and the past modest resources and prestige of the JFTC might still give rise to a lingering perception that an effective means of addressing market access concerns of foreign firms relating to regulatory or private conduct still needs further development in Japan. This might be particularly true with respect to distribution channels. Market access concerns with respect to distribution channels might also be remedied by continued efforts to increase transparency in the application of the Premiums and Misrepresentations Law.

Foreign firms also continue to complain about problems in gaining market access to Japan's distribution channels in sectors such as: autos and auto parts; paper and paperboard; flat glass; and photographic film. The JFTC might consider reviewing antitrust compliance programs of influential firms in these and other "highly-oligopolistic industries" to confirm that dominant Japanese firms are fully complying with the Anti-Monopoly Law and the JFTC's Distribution Guidelines. In this regard, the JFTC might also consider initiating a survey on the relationship between vertical *keiretsu* and certain perceived market access problems with respect to distribution. In particular, the JFTC might examine the extent and form of financial inter-relationships linking manufacturers and distributors in highly oligopolistic industries. Such a survey could, on an industry to industry basis, cover equity ties, provision of loans or other capital sources and the sharing of employees, facilities and equipment.

A particular setting for concern is the exertion or extension of market power by a regulated or protected monopolist into another market. The substantive problem, sometimes called “regulatory abuse,” is addressed by laws about monopolisation, or by regulatory laws applied to particular markets. Foreign firms and traders could be implicated in two ways. First, an incumbent domestic regulated monopolist might gain an unfair advantage over foreign products or firms in an unregulated domestic market. Or, an incumbent foreign regulated monopolist might use the resources afforded by its protection at home to gain an unfair advantage in another country. These concerns might be brought to the attention of the JFTC using the procedures outlined above. The conduct of regulated firms in non-regulated market is subject to the Anti-Monopoly Law. There is no exemption in that regard. However, the JFTC is under no obligation to take any particular action beyond launching an investigation. There have been no cases of the JFTC taking action in the past three years relating to these regulatory abuse issues. One possible reason for the lack of these types of cases is that until recently, regulated monopolies in Japan required regulatory approval to engage in commerce outside of the scope of their specific grant of authority. The regulatory agency typically requires a separate accounting or the separation of companies when a regulated firm engages in unrelated business.

From the perspective of market access concerns of foreign firms, the telecommunications sector provides an interesting example of the potential for competition policy to be applied to address the anti-competitive exertion or extension of market power by a regulated monopolist. Foreign trading partners claim that the rates that telecommunications carriers must pay to connect to Japan’s local telecommunications network are so high that they represent a barrier to entry for potential domestic and foreign entrants. Pursuant to the US-Japan Enhanced Initiative on Deregulation and Competition Policy, Japan has announced to submit a bill necessary to amend the Telecommunications Business Law at the Diet in the Spring of 2000 in order to implement a long run incremental cost methodology as early as possible, and to promote certain interim reductions in interconnection rates before then.

The application of competition principles is also important to determining other issues such as cross-subsidisation by the dominant carrier to other activities of its subsidiaries. In addition, delays in implementing interconnection with a dominant carrier might also serve as a significant barrier to entry. Interconnection is, however, only one side of the market access story. Another approach to facilitating new entry would be to allow competitors to establish their own networks themselves. This will require a more pro-competitive approach to rights of way such as: poles, ducts and conduits belonging to NTT or utilities; access to privately-owned buildings; and access to roads, highways, bridges, tunnels, subways and railroads. The JFTC could play a major role - if even only from competition advocacy - in establishing a more pro-competitive approach to telecommunications regulation and limiting the anti-competitive extension and exertion of market power by dominant carriers in this sector.

Other issues that could benefit from a competition policy oversight are barriers that increase switching costs for consumers such as restrictions on to local number portability and the absence of dialling parity. Finally, it is worth considering whether new entrants or non-dominant carriers (which in many cases will be foreign owned or controlled firms) should also be subjected to less onerous tariff and licensing approval processes than dominant carriers.

As Japan continues to implement regulatory reform, it is likely that the types of issues discussed in this section will only gain in prominence. In fact many of the reforms to the administration of the Anti-Monopoly Law, and much of the strengthening of the role of the JFTC in general, and in the particular context of regulatory reform (both documented in the background report on The Role of competition policy and enforcement of regulatory reform), are rooted in bilateral trade initiatives such as the Structural Impediments Initiative (SII) in the 1980s in addition to the US-Japan Framework Agreement for a New Economic Partnership (Framework Agreement) and US-Japan Enhanced Initiative on Deregulation and Competition Policy (Enhanced Initiative) in the 1990s. As more sectors of the Japanese economy are subjected to regulatory reform, the role of competition policy as a tool in addressing market access concerns can be expected to increase in importance.

### 3. Assessing results in selected sectors

This section examines the implications for international market openness arising from Japanese regulations currently in place for four sectors (two manufacturing and two service sectors): telecommunications equipment; telecommunications services; automobiles and components; and electricity. For each sector, an attempt has been made to draw out the effects of sector-specific regulations on international trade and investment and the extent to which the six efficient regulation principles are explicitly or implicitly applied. Particular attention is paid to product standards and conformity assessment procedures, where relevant. Other issues addressed here include efforts to adopt internationally harmonised product standards, use of voluntary product standards by regulatory authorities, and openness and flexibility of conformity assessment systems. In many respects, multilateral disciplines, notably the WTO TBT Agreement, provide a sound basis for reducing trade tensions by encouraging respect for fundamental principles of efficient regulation such as transparency, non-discrimination, and avoidance of unnecessary trade restrictiveness.

#### 3.1 *Automobiles and components*

As highlighted by the process reaching to the 1995 US-Japan Automotive Agreement, the automobiles and parts sector has attracted considerable trade policy debate between Japan and its trading partners. The sector is characterised by dynamism. On the one hand, leading multinational firms have embarked on global market strategies, resulting in vigorous alliance formations involving different regions in recent years. Against this background, international trade and investment in the sector has been among the most visible and is bound to grow. Various types of trade and investment issues have been identified in the discussion among policy makers.<sup>54</sup>

On the other hand, due to high levels of safety and environment concerns relating to automobiles, regulations have been pervasive in this sector across countries. Those concerns are justified by risks arising from new technology as well as global environmental problems. Particular regulatory measures designed and implemented in order to address those concerns, however, have been often caused unnecessary burdens for business activities such as trade and investment. In some cases, they have been suspected as reflecting protectionist purposes, or as furthering national strategies for the industry. The efficiency of regulations in this sector has been examined and discussed from market openness perspectives in a number of trade fora.<sup>55</sup>

Foreign car manufactures exporting to a particular country must meet many kinds of regulations. Standards are often different among countries. Manufactures may have to adjust themselves to those standards by investing and operating different research, production and testing facilities. They also often have to present testing results for regulators in a number of countries. Differences in regulations may have arisen from natural conditions such as temperature or weather conditions. As historical development of regulations has been independent in each country, convergence is not ensured in principle. In addition, there may be different ideas among countries about how to address environmental concerns, or what level of risk is acceptable. However, there may be cases where different regulations involve unnecessary adjustment costs or duplicative costs.

Calls for regulatory systems in OECD economies to respond to globalisation have targeted this sector. The Geneva-based UN/ECE Working Party 29 has been the focus of international discussion in harmonising regulatory requirements in a number of European countries as well as promoting the reciprocal recognition of approvals granted on the basis of those prescriptions. Japan's move to enter this arrangement from November 1998 is a major development in this context. TABD (Trans-Atlantic Business Dialogue) has produced additional momentum for regulatory authorities across countries to pay explicit attention to the desirability of promoting the global harmonisation of vehicle standards.

### 3.1.1 Standards and certification

In Japan, the Road Vehicles Law stipulates that no motor vehicle may be operated on the road unless it conforms with relevant safety and environmental pollution control standards. Vehicles that have obtained type designation do not need to be individually inspected by the Ministry of Transport before they can be registered for use on the road.

The type designation system applies to mass-produced vehicles (Article 75, Road Vehicles Law). Under this system, a new car type is designated by the Ministry after it checks, *inter alia*, 1) whether the car meets regulatory specifications of the Ministry of Transport, 2) whether sufficient quality control in manufacturing process is in place and 3) whether a complete car inspection system is in place. For an imported car type of less than 2,000 in annual sales in Japan, simplified procedures for type designation called Preferential Handling Procedures (PHP) are applied: checks on 1) and 2) can be done by papers while complete car inspection is applied to each car. PHP is advantageous for the car type which is sold in small number.

There have been persistent external calls for efforts to harmonise Japanese automobile regulations, as well as to accept as equivalent, standards that are widely used in other countries, and for Japan to accept equivalence of foreign conformity assessment results such as test data. For example, the European Commission tabled in its proposals for the Deregulation Action Plan as many as 26 items in the automotive sector in October 1998 (In 1997, the number of items was 15). Among these broad range of issues raised by the EU, Japan is requested to: 1) bring Japanese regulations e.g. vehicle noise into line with international practice, and 2) recognise and accept test results from abroad. In addition, the EU requests improvements in type approval systems, such as extension of application of component type approval to more auto components, in order to reduce regulatory burdens for car makers.

The Japanese response has been rapid and encouraging. The Transportation Technology Council, advisory body to the Transport Minister, recommended that Japanese regulations be harmonised to international standards. The Japanese Diet has approved Japan's accession to the 1958 UN/ECE (United Nations Economic Commission for Europe) Agreement. This Agreement promotes harmonised technical specifications as well as reciprocal acceptance of conformity assessment in the auto sector with nearly 30 Contracting Parties, including 14 Member States of the EU as well as the European Community on its own right. Japan's entry will be in effect from November 24, 1998.

Japan has, as a first step to prepare for its accession, harmonised MOT technical regulations with UN/ECE regulations on the following 5 items:

- Reflectors (ECE Regulation No. 3);
- Lighting and signalling devices (ECE Regulation No. 7);
- Braking system (ECE Regulation No. 13H)
- Front fog lamps (ECE Regulation No. 19)
- Audible warning devices (ECE Regulation No. 28).

The Ministry of Transport is also proceeding with necessary changes to the type designation system for vehicles and vehicle equipment to accept certification by foreign bodies.<sup>56</sup>

In the medium term, Japan's entry to UN/ECE Agreement, which reflects more positive Japanese attitude towards harmonisation, will reduce technical barriers for global trade in the automobile sector. Rather than dealing with specific harmonisation/recognition issues item by item, the entry will establish a framework under which progress can be measured and remaining problems can be clarified quickly. By participating the discussion at international standardisation process, Japanese regulatory authority is going to pay explicit attention to the regulation's impact on trade, when formulating future technical regulations.

The question now is how fast and comprehensively the regulatory authority can move to achieve the announced policy goal. One European expert view holds that compared to the EU which has acceded to 78 UN/ECE regulations of the total of more than 100, Japan has still a long way to go. In considering the substantial work to be done to internationalise Japanese auto regulations, a systematic review of a broad range of current technical regulations will be needed for future regulatory reform. Such reform will bring about economic benefits, not only to exporters to Japanese market, but also to Japanese consumers who will gain from wider choice and less expensive prices without endangering safety or other social concerns.

### 3.1.2 *Avoidance of unnecessary trade restrictiveness in other areas of automobile regulation*

Another aspect of regulations in the automobile sector has attracted persistent attention by Japan's trading partners. Under the Road Vehicle Law, for the purpose of maintaining vehicle safety, only garages that are certified by the Ministry of Transport can conduct vehicle maintenance work (Article 77). Among the certified garages, only those that are designated by the Ministry of Transport can conduct vehicle inspections (Article 94-5). The United States has expressed concern that the requirements under this regulation, though applied on the basis of the non-discrimination principle, discourage establishment and operation of specialised garages more likely to deal with foreign-made automobile parts.

The response of the Ministry of Transport has been, *inter alia*, relaxation of requirements on certified garages. Reform has introduced, since February 1997, new categories of certified garages so that specialised garages can operate car maintenance services. While this reform has been welcomed as contributing to more openness in Japanese auto parts markets, the United States would like to promote further improvement by reforming qualification of mechanics: current qualification requirements for mechanics look too wide ranging while mechanics working for specialised garages may need expertise only in their specialised areas. Trading partners expect that such measures can facilitate establishment of new smaller car shops that have capacity for repair services and use more foreign-made auto parts than existing garages.

The Ministry has held public hearing in February in 1998, inviting interested parties including domestic and foreign businesses as well as foreign governments, but it is said to have been faced with difficulties to proceed due to opposition from existing garages and car makers, for the reason that the proposed change would reduce safety. The purpose of qualification system is to maintain safety quality of repair services and regulatory measures such as expertise requirement should not be more than necessary to achieve such purpose. Consideration of economic interests arising from safety regulations looks inappropriate to dominate the discussion of reform. Other concerns have been raised on unnecessary restrictiveness of existing inspection requirement. In Japan every car must be inspected by certified garages every two year. Trading partners have pointed out that the validity of inspection should be prolonged in light of technological development in the auto manufacturing since the time of the initiation of such requirement. The Japanese government promised to conclude its deliberations on this matter by March 1999. Foreign parties also claim that space and equipment requirements for garages are too restrictive.

Another example of regulations unnecessarily restricting trade are those affecting motorcycle use. Japan has a unique regulation (except for Korea) that prohibits tandem ridings on national expressways. Due to this prohibition, tandem motorcycles are unable to travel long distances in Japan. This has had a negative impact on the market for large size motorcycles which are likely to be more suitable for tandem ridings: the

market volume of big bikes in Japan is only one third that in Germany and a quarter that in the US. Because foreign motorcycles exported to Japan tend to be large sizes, the prohibition of tandem ridings on national expressways has had the effect of preventing foreign motorcycles from penetrating to the Japanese market. Major trading partners have complained that the prohibition works as a barrier to market access.

The objective of the regulation is a reduction of traffic accidents of motorcycles. This explanation is not convincing since tandem ridings on normal roads are allowed, and the driving conditions are less favourable to motorcycles than on expressways. Some argue that the real regulatory objective is the prevention of joy riding on expressways. Yet, there are alternative ways to address such concerns, such as control at the toll gates of national expressways.

In both cases mentioned above, although regulatory objectives by themselves do not include trade restrictions and are justifiable, existing measures to achieve objectives are questioned from the perspective of market openness. This supports the argument for more open regulatory procedures to take into account of the concerns of a broad range of affected parties, including foreign businesses and consumers. Such mechanisms will help focus on appropriate regulatory measures to achieve the goal without causing unnecessary trade restrictiveness.

### 3.1.3 *Transparency in regulatory procedures*

Transparency in regulatory procedures is a high priority. For automobile regulation, *MOT News*, published in English by Office of International Affairs in Road Transport Bureau of the Ministry of Transport, has helped to inform foreign firms of important regulatory changes.<sup>57</sup> There has been more frequent use of public hearings for draft regulations, such as those held on the deregulation proposal for the mechanics system and proposed modifications to the type designation system.

Foreign firms operating in Japan, however, have had difficulty in consultations on new regulatory proposals. Consultation tends to take place at late stages, resulting in a lack of understanding by foreign manufactures and stronger reactions from them. One recent example is the proposal by the Ministry to introduce recall procedures and the new certification system. A foreign expert based in Japan observed that there may be no explicit intention to exclude foreign firms from consultation, and that going to domestic players first is often simply a matter of habit. Nonetheless, such habits support the case for procedural safeguards against exclusion. Trading partners have requested that the Japanese government allow foreign manufacturers, on an equal basis with Japanese manufactures, full and timely opportunities to comment on draft regulations and standards.

Japanese Ministries have started to use the Internet, as means of communication to the public. However, use of the Internet for dissemination of detailed regulatory information seems to lag well behind the best practice countries such as the United States. In light of wide and non-discriminatory availability through information on the Internet as well as the need for more open practices by regulatory authorities, more use of the Internet is a promising avenue to impose transparency in sectors such as automobile, where regulations intervene with important business decisions. Recent use of the public comment procedures for new fuel efficiency standards is an encouraging example in this direction.

## 3.2 *Telecommunication services*

The telecommunications sector in Japan has been a major focus in trade discussions in recent years. The sector is a major part of foreign trading partners' recommendations submitted to the formulation and subsequent revisions of Deregulation Action Plan. Ongoing Japan-US trade discussions have spent

considerable time and resources on the sector. In the context of multilateral trade relationships, Japan participated in the WTO negotiations on basic telecommunications services and joined in the agreement reached in February 1998. International discussions have had substantial impact on Japanese regulatory reform to date.

Although telecommunication services cross borders easily, the prevailing feature of the industry structure in OECD countries is the existence of dominant carriers who control the nation-wide network. Vigorous international competition, where firms from different countries compete effectively against each other in a particular national market, has not been common in this sector, although such competition has become the norm in many manufacturing sectors. Competition will produce benefits in terms of consumers choice, service quality, and price. The challenge for regulatory reform in each country is how to introduce and promote competition through the most efficient measures. Specific aspects of such measures may be different across countries, since countries differ in their tradition of regulatory rules and structures. Market openness, however, will contribute to development of efficient and competitive national telecom industries and deliver the most benefits to consumers.

A general overview and assessment of future policy options in Japan's telecommunications services sector is presented in the report on regulatory reform in the telecommunications industry in this volume. This section assesses particular aspects of regulatory reform from a market openness perspective. The major policy question is how more vigorous international competition can be ensured, so that Japanese consumers, and domestic and foreign businesses can maximise benefits from reform.

### *3.2.1 Reform to date of particular interest to foreign competitors*

Since the privatisation of NTT in 1985 and subsequent liberalisation of the market, the Japanese telecommunications sector has progressively moved toward competition. A recent major step was the decision to restructure NTT under the control of a single holding company. The Deregulation Action Plan of 1998 includes the important decision to move toward introduction of interconnection rates based on LRIC (Long Run Incremental Costs) methodology (which is expected to facilitate entry of carriers by reducing the costs of interconnection to the dominant carrier NTT). This has been requested by foreign trading partners, and they are now paying careful attention to the progress.

The government has taken other steps on issues that have concerned foreign firms. For example, foreign ownership restriction of Type I carrier and KDD, as well as the "100 destination rule"<sup>58</sup> which imposed restriction on international transit services, have been abolished. International simple resale was also liberalised since the end of 1997. (On the other hand, foreign ownership restrictions on NTT and CATV still remain.) In addition, Japan's participation in the WTO agreement on basic telecommunications services, particularly its commitment with other countries to pro-competitive regulatory principles, will have positive impacts on the operation of the regulatory regime in Japan. These moves have been welcomed by trading partners.

### 3.2.2 *Foreign trading partners' concerns: uncertainty in pro-competitive approach*

While progress has been made in building a more market-based regulatory regime in this sector, observers, including foreign trading partners, see underlying and rather fundamental problems in the regulatory regime in this sector. Foreign firms in this sector are not confident that regulatory policies are committed to full-fledged competition. Foreign business operating in Japan point out that Japan's Telecommunication Business Law (TBL), and hence the market supervision by MPT, has weakness in commitment to the interests of competition and consumers in its regulating philosophy, compared to US, Germany and UK telecommunication laws: the Article 1 of the TBL states that the Law aims to protect interests of users, in parallel with other purposes including the general term of "promotion of public welfare"; it does not mention competition specifically. On the other hand, the Japanese government points out that its regulatory policies to date have been contributed to the interests of consumers through introduction of competition in the sector.

As mentioned, the key regulatory challenge is how to introduce effective competition in the market where a dominant carrier still exists. The task involves broad-range, technically complex issues such as establishing and monitoring interconnection rules, number portability and securing rights of way that are heavily controlled by incumbent interests. Without confidence that regulatory policy is aimed at resolving these issues over time in an open, non-discriminatory and pro-competitive way, incentives of firms to invest and innovate may be greatly reduced.

Such claims have been raised on: weakness in the TBL to take an explicit dominant carrier regulation approach; need of stronger competition policy; concerns on independence of the regulator. Furthermore, trading partners point out that discretionary power exercised by the regulatory authority is still too wide, giving a chilling effect to the market. Foreign firms may be the most sensitised to such risks because they know less about how discretion might work than domestic non-dominant firms including NCCs (New Common Carriers). For example, they claim that with respect to licensing of carriers, after abolition of demand-supply adjustment clauses, carriers still have to prove their business plans are "rational and certain", giving a wide range for discretion by authority. However, according to the government, the licensing procedures are based on examination standards that are clearly prescribed and publicly announced, and hence it believes that there is no room for exercising discretionary power.

As a result of the problems mentioned above, many foreign telecommunications firms believe that long-term investment has suffered in this sector in Japan. A pro-competitive regulatory regime, as recommended in the report on regulatory reform in telecommunications included in this volume, would greatly reduce uncertainty for future business activities by narrowing the scope of discretionary use of regulatory power. For example, in order to encourage innovative and vigorous business activities, positive and clear commitment by the regulatory authority to competition as well as its willingness to reduce regulations and implementation only to that purpose should be demonstrated. For this purpose, while recent revisions of TBL have been intended to increase competition, explicitly enshrined competition principles such as in 1996 US Act, or at least binding and clear statements on overall policy stance of regulation would be further useful.

### 3.2.3 *Transparency and openness of regulatory procedures*

Connection to the network and rights of way mentioned above is only a part of regulatory issues in telecommunication services which have a significant impact on competition, including international competition. There are a number of other issues that urge regulatory authorities to undertake study and to reach decisions on the daily basis. In the light of this situation as well as technical complexity and broad potential impact on the economy including its international aspects, regulatory decisions in this sector will particularly benefit from the openness and transparency of the procedures. As mentioned, authority's commitment to full

competition has not enjoyed high level of confidence by foreign businesses. Recent announcement by the Ministry of Post and Telecommunications that it would implement a notice and comment process for major regulatory changes signifies the increasing recognition of this need. Positive attitude of the Ministry is welcomed all the more because such overall commitment for procedural transparency is still under consideration by government as a whole. One trading partner particularly appreciates its publication of manual for market entry to this sector, too. However, in order for the consultation process to really work -- to contribute to the quality of regulatory decisions --, there is room for further improvement. Foreign telecommunications firms in Japan have complained that consultation periods for major regulatory changes are too short, and ask that the period be extended. They wish proceedings of the MPT's related Committee/Council/Study Group meetings to be published. Openness can be further promoted if written response is made to the comments, giving reasons for authority's actions.

In addition to a notice and comment system, the use of the Internet in disseminating detailed information on regulation would be a powerful tool to increase the level of transparency of regulations and the MPT has started to use its Home Page for the communication with the public. As described in the section on automobiles and parts, Japan can learn more from best practice countries such as the US in this context. Such reform will contribute to market openness of the sector too.

### **3.3 *Telecommunication equipment***

The size of Japanese telecommunication equipment market is the second largest in the world. It is also a rapidly growing market: domestic production of the equipment in FY 1996 was more than 4 trillion yen and it had grown by more than 36 % compared to the previous year. Foreign manufactures have come to be greatly interested in Japanese market.

Regulatory systems relating to the equipment, while aiming *inter alia* at network compatibility, have been seen as affecting further expansion of trade. Conformity assessment procedures for telecommunication equipment, especially terminal equipment including mobile phones, have been cited as one example. Furthermore NTT, the biggest procurer of the equipment, has been said to be causing difficulties for more imports. NTT has made efforts to open up its procurement to foreign manufactures. Its procurement from foreign source has been increasing under the NTT Procurement Arrangement since 1981. However, a recent JETRO (Japan External Trade Organisation) survey<sup>59</sup> has pointed out possible NTT-related problems in the market. For example: *i*) Carriers, especially NTT, play major role in sales and marketing of terminal equipment and this relatively unique structure of distribution may prevent standardised and hence low cost products from entering Japanese market; *ii*) NTT-led R & D joint project with several makers has been dominant in the development of network equipment: such "carrier design" products may have nurtured close relationship between NTT and equipment manufactures and may have discouraged new comers to work with NTT. On the other hand, the Japanese government holds the view that the procurement of NTT is a matter for the private sector and should not be regarded as government regulation. According to the government, NTT's practices, including its R&D activities, are open, fair, and non-discriminatory.

### 3.3.1 *Conformity assessment procedures*

Japan has two sets of technical standards and conformity assessment procedures accordingly for telecommunication equipment. Telecommunications Business Law mandates technical standards in order to secure connection of equipment to network. A public service corporation called JATE (Japan Approvals Institute for Telecommunications Equipment) has been authorised to certify its conformity. Radio Law mandates technical standards in order to ensure fair and efficient use of radio wave. A body called TELEC (Telecom Engineering Center, formerly called as MKK) has been designated by the Minister to certify products.

This regulatory system has been criticised as preventing optimal market competition that would finally result in wider choice and lower prices. According to the JETRO survey, the costs of certification are high in Japan, compared to some of the major OECD countries, while the MPT has pointed out that the costs in some European countries are higher than those in Japan. Several problems have been identified: *i*) Organisation that conducts certification has been a limited number, notably JATE and TELEC. These bodies can use data from testing laboratories or from the manufacturers themselves in their conformity assessment process, while some manufacturers have found it difficult to use such a system in practice. *ii*) Possible duplication arising from two types of regulations; when equipment is in both categories mentioned above, such as mobile telephone equipment, manufactures have to have their new products certified by the two bodies. *iii*) There has been no availability for manufactures' declaration of conformity which is less burdensome for manufactures.

The regulatory authority, Ministry of Posts and Telecommunications, has responded to question by introducing new legislation for rationalisation and more openness of current certification system. Passed by the Diet in April 1998, it allows foreign certification bodies (that are either foreign government bodies or those designated by the governments) can be recognised by the authority to certify products. It also allows data from testing institutions (foreign or domestic) recognised by the MPT to be used for obtaining certification. These measures, which came into force in March 1999, are to expand recognition of equivalence of foreign conformity assessment and are expected to contribute to market openness of telecommunication equipment market. In order to ensure such positive impact, the criteria to designate certification bodies and testing laboratories should be objective and according to international practice. The delegated rule-making on this should be subject to transparent and open public and notice procedures. Furthermore, the costs from complexity of the system would be reduced by the recent reform to receive "one-stop shopping" application.

Another notable development towards more open conformity assessment procedures is the ongoing negotiation on the Mutual Recognition Agreement (MRA) with the EU. Telecommunication terminal equipment is one of the items under negotiation. If successfully concluded, the MRA is expected to have a positive impact on further openness of the system. While progresses to date are encouraging, further reform efforts, such as further integrating the separate two systems as well as adoption of manufactures' declaration of conformity where possible and appropriate, will have promising benefits.

### 3.3.2 *Standards and procurement practices of NTT*

Substantial efforts have been made both by NTT and the Japanese government. The foreign products that NTT purchased amounted to 185 billion Yen in FY 1997. NTT is providing the information of its procurement at its Home page of the Internet and has announced its fundamental procurement policy based on openness, fairness and non-discrimination. However, foreign trading partners still allege that the past measures have fallen short of truly open procurement.

They claim that NTT's procurement instructions are too complex and not well documented. As a result, the manufactures, who are familiar with these practices through a close relationship nurtured under the long-held monopoly position of NTT, are claimed to have advantage over foreign suppliers. The Ministry of Post and Telecommunications argues, on the other hand, that such an allegation is not factually correct.<sup>60</sup> It has been also pointed out that NTT-led research consortia may have discouraged entry of foreign firms. Furthermore, the JETRO report raised the view that rate of return regulation may be responsible for weak incentives for cost reduction by NTT and hence weakening its purchase of low cost products on which foreign manufactures have advantage. Due to technical and detailed nature of procurement practices, the policy judgement on these issues is bound to be complex. More vigorous competition in services market, however, will have positive impact on equipment market in the sense that the best quality and the least expensive products will be chosen to contribute to economic efficiency. In this sense, price-cap regulation introduced in 1998 (which will be implemented in 1999) is expected to shift the market towards this direction, by giving stronger incentives to NTT to seek more vigorously low-cost equipment.

It has been also pointed out that standards development of telecommunication equipment has often been heavily influenced by NTT. It has overwhelming technological advantage and has tended to produce Japan-specific standards. More open and internationally-oriented standards development, it is said, can enhance more vigorous competition, wider choice for consumers and innovation. NTT recognises that its technical specifications should be based on international standards, including *de facto* ones, where they exist. Again, this is not a simple question. Considering technology-driven nature of the telecommunication equipment, NTT's technological capacity can be seen as the assets for the future, not only in Japan. But at the same time, such potential benefits should be balanced by Japanese consumers' interests in having the least expensive equipment which has connection to the broadest part of the world.

### 3.4 *Electricity*

There are ten electricity utilities in Japan, who have enjoyed regional monopoly status for a long time. They are firms of large size and regarded as important representatives of Japanese business. During five decades in the post-war period, the electricity sector has been the major and stable establishment in Japanese industrial structure and its main concerns have been, understandable, domestically focused.

However, Japanese electricity prices, the highest in the OECD are affecting industrial competitiveness. Concerns about international competitiveness is the main driver of recent reform in this sector. The Ministry of International Trade and Industry (MITI) has established the target to reduce electricity price to "internationally comparable levels" by 2001. Recent reform introduced competition at the whole sale level from 1996 and made other several important changes (including easing some technical requirements for pre-inspection of new facilities). Further reforms, to introduce partial liberalisation of retail supply of electricity, are expected next year. The background report on Regulatory reform in the electricity industry makes the overview and assessment of this development.

The focus on international competitiveness in electricity prices, and the trend to market liberalisation, is putting pressure on the utilities to reduce costs. A focus on costs of investment in new electrical generating equipment, currently the highest in the OECD, is a logical starting point. The volume of annual investment by utilities in generation, transmission, transformation and distribution equipment of 4.4 trillion yen (this consists of approximately 1.6 trillion in generation, 1.5 trillion in networks (transmission transformation and distribution), and 1.3 trillion in plant improvements), makes a highly attractive market to foreign electrical equipment manufacturers. In recent years, as the share of foreign equipment sales in Japan has been at the level of around 9%, the potential for trade still looks significant.

Market openness perspectives can strengthen benefits from the ongoing reform in electricity. It would help to expand opportunities for less expensive input price, and hence can make a concrete contribution to the objective of reducing costs to internationally comparable levels. It may further bring benefits from innovative

technology widely available in the world, such as that in metering. Such benefits would enhance broad consumer interests as well as the foreign trade and investment. The following analyses how market openness perspectives work to contribute to regulatory reform in Japan.

### *3.4.1 Technical regulations and conformity assessment of electricity equipment*

MITI is mandated by the Electricity Utilities Industry Law (EUI Law) to set technical standards to ensure safety of electricity supply. Utility companies have to submit plan for construction work to MITI for its approval when they install or change electricity facilities such as turbines and boilers. MITI conduct mandatory inspection before the operation of the facilities (Article 48). Periodical inspection by MITI is also mandated for pressure-resistant facilities (Article 54).

Most of the technical standards set by MITI are said to have originated from ASME standards, which are used globally by electricity businesses. Until recently, technical safety standards by MITI were highly prescriptive, which left equipment manufacturers little flexibility in design of equipment. In reviewing electricity safety regulation, it was recommended that technical regulations should adopt performance-based standards that would provide performance needed to be achieved by equipment for safety purpose but allow manufactures flexibility in achieving it. Subsequently, in June 1997, performance standards was introduced by revision of related MITI internal order. Although some specifications remained in the form of "interpretation of technical standards", it was made clear that such interpretation is not mandatory.

This move reflects in part the concerns from trade perspectives that difference in standards across countries can become unnecessary trade obstacles. The current measure is expected to contribute to market openness in electricity equipment market and contribute to harmonisation process across countries. However, expert views are that there are obstacles in addition to technical regulations: for example, specifications set by utility companies may pose more serious difficulties (as discussed below); the upgrading of existing power generation facilities in Japan meets too burdensome procedures due to various regulatory restrictions.

Furthermore, they point out that there are unnecessary burdens in inspection procedures. Such burdens, while non-discriminatory in nature, may be excessive for the purpose of safety and they are likely to discourage trade in equipment in this area. While the periodical inspection has been recently prolonged from 24 months to 30 months, foreign businesses have seen this only marginal improvement.

Foreign trading partners have also expressed their concerns on the requirement from the High Pressure Gas Law (HPG Law) applied to electricity equipment. This regulation applies to the equipment that are not used directly for power generation, such as pollution control facilities. Inspection under the HPG Law is said to be complex and costly, imposing unnecessary burdens for foreign producers. Technical standards under the Law, it is said, should be brought in line with internationally accepted standards. According to MITI, the similar measure taken under the EIU Law, namely the reform of regulatory specifications towards performance-based standards, is under way to be implemented next March. Enforcers of the HPG Law regulations include 47 local prefectural governments and that has added to the complexity of regulations.

While MITI has addressed the particular concerns of exporters to Japanese market i.e. by lifting part of inspection requirement by the EUI Law or HPG Law for pressure-resistant facilities for imported equipment, more systematic review of safety regulations with a view to avoiding unnecessary trade restrictiveness would contribute to market openness: under such reform, economic gains can be shared with consumers without sacrificing safety concerns.

### 3.4.2 *Procurement practices by utilities*

Procurement of electricity equipment by utilities has been dominated by domestic manufactures. However, recent drive for lowering electricity price has given strong pressures to Japanese utility firms to change their practices, opening up their procurement process to wider range of businesses, including foreign ones. TEPCO (Tokyo Electricity Power Company) and other utilities have set up Internet sites to provide information on their procurement items and procedures, both in Japanese and in English. Utilities have shown increased interest for purchasing abroad by sending mission to foreign trade shows. These reflect utilities' growing concerns for cost saving as a result of introduction of competition to the sector. Foreign manufacturers clearly welcomed this move.

However, the specifications of utilities in procuring equipment have been frequently raised as fundamental problem. Technical specifications (standards) set by Japanese utilities are often said to be tailored to each company (ten "general" utilities exist in Japan), and too high for the purpose of maintaining an optimal level of safety or reliability. (An economist mentioned that Japanese electricity grid system is "Rolls Royce" among other countries.) Utilities also require stringent conditions for prompt deliveries and periodical inspection as well. While concerns for high quality is understandable and justified to some extent, the standards must be balanced against the impact on economic efficiency. If standards are set so high, the number of potential suppliers will be limited, reducing competition and raising costs.

More open equipment procurement practices will be encouraged by further promotion of competition in the electricity sector by future reform, through more pressures on electricity companies to search and purchase less expensive equipment. A central issue here is how quickly such reform will be implemented and its impact will be translated into equipment market. There may be a danger of a policy vacuum, since MITI has been reluctant to intervene directly in procurement practices of utilities. More focused attention on this issue, probably looking at the role of standardisation for example, will likely to contribute to consumer interests as well as to help ease potential trade tensions.

Furthermore, market liberalisation can be expected to affect only the cost for generation equipment, which is currently only about two-thirds of all utility investment. Investment in electrical networks (transmission, transformation and distribution) will not be subject to competition. Intensive policy efforts to ensure openness of procurement practices is even more necessary in this area. One possibility for the regulator to consider is to require utilities to tender for construction of major new network facilities (e.g., transmission lines).

### 3.4.3 *Openness and transparency in the regulatory procedures*

Regulatory procedures in the electricity sector have been in the traditional style: the key discussion is based on informal consultation with major players; decisions are often formalised in advisory councils in closed session, while members of such councils have been selected from utilities, user industries, consumers and academics. Public comment and notice procedures has not been the norm. As foreign companies have not been very active in the Japanese electricity sector, their views have not been sought.

That attitude has to change in order to adapt to a more liberalised, and at the same time a more internationalised, electricity sector. Potential participants in the market may be more numerous than major players, including regulators, think. Exposing the discussion to public and even international view would increase confidence in decisions made and would ensure their quality. The current efforts to enhance openness are in the right direction and should be pursued further.

The commitment to a public notice and comment system in major regulatory decisions, made in telecommunication services area for example, is worthwhile to be pursued. MITI announced in August 1998 its intention to adopt public comment procedures to policy council deliberations. The coverage of such measure, however, has not been explicitly spelled out and the impact on significant regulatory decisions, which are expected to be made in electricity areas in future remains to be seen. If broadly and effectively implemented, it would ensure all the interested parties, including foreign firms, to make input to the decision making and help reach pro-competitive results. Publication of Study Group/Council proceedings are also useful for enhancing transparency. Furthermore, the use of the Internet would contribute to higher level of transparency as is seen in leading countries such as the US and should be pursued further.

#### **4. Conclusions and policy options for reform**

##### **4.1 *General assessment of current strengths and weaknesses***

Recent Japanese regulatory reform programs have been launched to implement fundamental reforms in Japan's socio-economic structure and have also responded to concerns voiced by major trading partners (including foreign business communities) and suggestions made in international fora such as the WTO and the OECD. Even though the current programs have been largely based on Japan's own initiatives, the Japanese public still seems to relate them to foreign pressures. In fact, the image related with foreign pressures was one of main weaknesses of previous programs. While this image helped promote reform against strong domestic opposition, it also helped to make Japanese regulatory reform programs incremental, defensive and conservative. It did not help the Japanese general public to accept reform and understand how reform was in its interests.

Japanese bureaucrats have had tendencies to keep regulated sectors at the close sight and to manage competition. Many trading partners have expressed their concerns about the demand supply adjustment clauses of individual sectors which give regulatory authorities the right to intervene, as this usually results in controlling the number of firms and limiting the entry of new competitors, domestic and foreign.<sup>61</sup>

Even when bureaucrats agree with the request to change the system i.e., to introduce more market mechanisms at the expense of direct control or regulations, they are usually reluctant to do so radically. This is partly due to their perception of responsibility with regard to specific sectors. But, it is also largely due to traditional inertia vis-à-vis change.<sup>62</sup> Sometimes, traditional values of regulations which have existed so long make bureaucrats hesitate to change. This stance of Japanese bureaucrats was one of the most important obstacles to the launching of government-wide regulatory reform. It has been continuously criticised by trading partners as a major obstacle to improving market openness. It has also been the main reason why Japanese deregulation measures have been incremental in nature. Despite requests from the prime minister's office and strong pressure from domestic and foreign businesses, bureaucrats still take the incremental approach by, for example, reducing some administrative procedures, or by allowing additional licences, (see the background report on Government capacity to assure high quality regulation for a more detailed discussion on "incrementalism" in Japanese deregulation programmes).

Although the Japanese government considers consultation with councils as a good method to hear public opinion and make administrative conduct more open and transparent, many trading partners have expressed their concerns about the council system. According to them, consultation with councils makes the decision making process more closed (in the sense that vested interests are reflected and not new competitors' views) and very slow.

One of the main strengths in the Japanese regulatory reform process is the desire of Japan to integrate in the globalised world.<sup>63</sup> Despite all the obstacles to enhancing market openness and to launching effective structural reforms, the efforts which have been made until now owe a lot to this desire. The Japanese general public seems to accept the necessity of the integration of the Japanese economy in the globalised world. One of the Three year Programme's guidelines requires Japanese regulations to be aligned with international norms and is a notable example.

A second strength is closely related to the first one. The establishment of the OTO and the OMA is also perhaps the result of the desire of the integration in the world economy. The OTO has the right vocation to enhance market openness and consequently to contribute to regulatory reform in this regard. It has also a well established mechanism, multi-layer inter-ministerial co-ordinating meetings and special committee, to solve specific market access problems. In addition, the establishment of the OMA Cabinet level meeting has made the OTO more powerful at least at the institutional level. Japan may need, however, to reinforce its co-ordinating authorities over other ministries and agencies, since some trading partners seem to be losing interest in bringing complaints to OTO, due to disappointment with its lack of authority.

A third strength is the contribution made by foreign business communities. They are active in every phase of Japanese regulatory reforms. They are bringing forth the most current issues because they are very close to the market, playing the intermediary role between the Japanese government and governments of their home countries, and monitoring the implementation of Japan's commitments in deregulatory plans and in various level trade talks. However, their role is not very well received by the Japanese public. They may be playing a role which is missing but necessary in Japan, catalyst for change. However, their role is limited because they fragment reform, and focus change on trade disputes rather than deepen change.

Many weaknesses can be found in the Japanese regulatory reform process. First, one should mention the lack of serious support for regulatory reform and market openness. It is notable that supposed beneficiaries from reform, market openness and competition, consumers, are not very eager to support those initiatives but are sometimes opposed to so-called radical change. This is because consumers are not well informed about the potential benefits of reforms and market openness, and reforms have been often initiated to respond to the demand of producers, domestic and foreign. Political support seems to be not always strong enough to promote concrete regulatory reform programs in specific sectors especially when related to market openness. Consequently, the struggle is taking place among bureaucrats, between those who are convinced of the necessity of change and those who are eager to stick to their traditional way to govern. Since the actual power to decide something at the concrete level remains at the hand of the latter, it is still difficult to launch effective regulatory reform programmes, even if there are good guidelines for the programmes which are usually defined by the former. It seems essential for the former to develop a stronger constituency among the general public and politicians in order to effectively pursue further reform programmes.

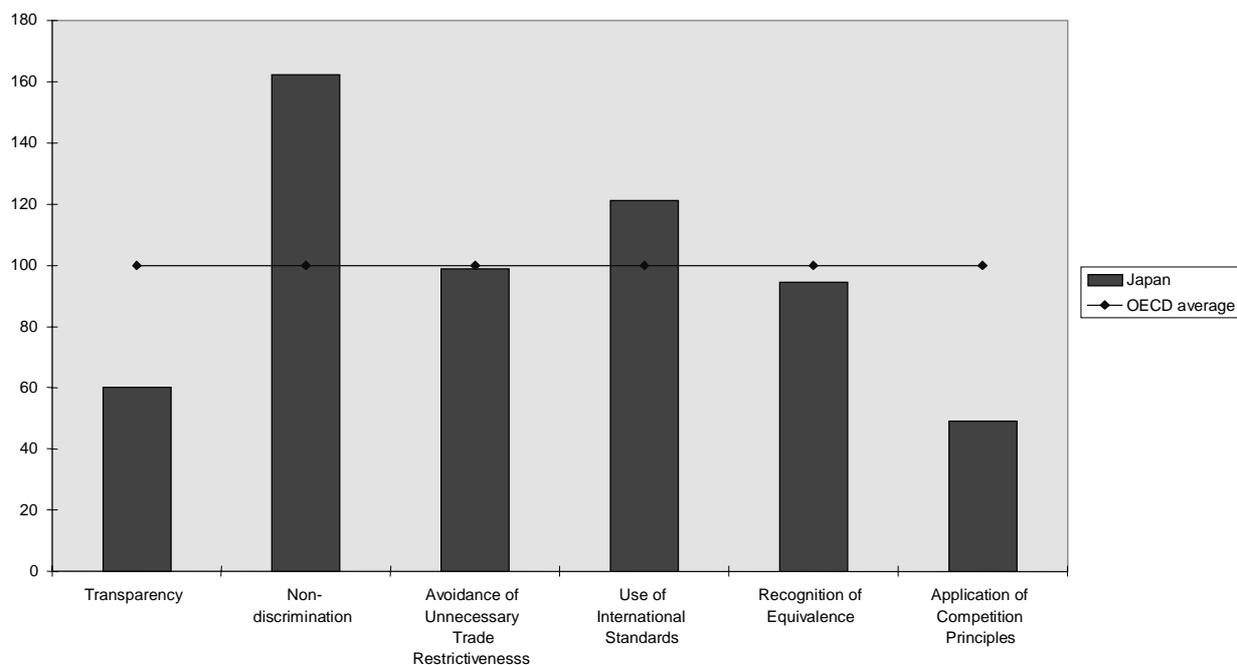
Secondly, the distinction between the sectors traditionally open to international competition and the sectors protected from it is too prominent. The former sectors are generally competitive on the world market. Businesses active in these sectors are generally favourable to enhancing regulatory reform and market openness in the protected sectors, because they think that only further reforms in these sectors can help their own sectors to remain competitive. However, those protected sectors are still regulated and relatively well protected from foreign competition. Those involved in these sectors (regulators and regulated firms) even when conscious of the necessity to change, are eager to maintain the current situation. When sectors are represented by small business such as distribution firms, they are often politically strong enough to resist reform. Since ministries and agencies in charge of the two groups of sectors are well separated and independent from each other, effective government-wide initiatives for regulatory reform in view of enhancing market openness become difficult to launch.

Thirdly, the lack of strong competition policy enforcement is an important obstacle to market openness in the Japanese regulatory system. The JFTC seems to have difficulty taking vigorous enforcement actions against the sectors regulated by “major” ministries. In these sectors, anti-competitive business practices of either monopolising companies or exclusionary industry associations may not be appropriately treated by the competition policy authority (see the background report on The Role of competition policy and enforcement of regulatory reform for more detailed discussion). In addition, the Japanese business tradition of long-term close relationships between manufacturers and distributors remains a major obstacle to foreign access to the Japanese market.

Fourthly, there are no established methods to monitor adverse trade and investment effects of some administrative conduct. Informal communications such as administrative guidance still form a part of the “effective” regulatory structure in Japan. Government bodies in charge of monitoring regulatory processes do not have strong authority vis-à-vis individual ministries and agencies. Their monitoring role does not fully reach regulations such as ministerial orders or administrative conduct of other ministries and agencies, except at the inter-ministerial deliberation process of laws and cabinet orders. The advocacy role of MITI and MOFA for enhancing market openness (e.g. training) is also limited.

According to the self-assessed response by governments to the OECD indicators questionnaire on the six efficient regulatory principles with a market openness perspective, the Japanese regulatory system is relatively advanced in its application of the principles of non-discrimination and use of internationally harmonised regulations compared to OECD averages (see Figure 2). On the other hand, the Japanese regulatory system has a relatively wide scope for further improvement in the principles of transparency, openness of decision making and of appeals procedures; and application of competition principles from an international perspective. However, even regarding non-discrimination and international standards, more efforts are required, taking account of concerns of trading partners mentioned in Section 2.

Figure 2. Japan's trade friendly index by principle (OECD averages = 100)



## 4.2 *The dynamic view: the pace and direction of change*

Globalisation has dramatically altered the world paradigm for the conduct of international trade and investment, creating new competitive pressures in Japan and elsewhere. At the same time, the progressive dismantling or lowering of traditional barriers to trade and the increased relevance of “behind the border” measures to effective market access and presence has exposed national regulatory regimes to a degree of unprecedented international scrutiny by trade and investment partners, with the result that regulation is no longer (if ever it was) a purely “domestic” affair. Trade and investment policy communities have generally kept pace with these twin phenomena. However, a degree of regulatory catch-up is required. Concrete steps to increase awareness of and effective adherence to the efficient regulation principles and to deepen international co-operation on regulatory issues are encouraging trends in this context. Overcoming systemic intransigence and fostering a new regulatory culture will be pivotal to these efforts.

Currently, the US and the EU are engaged in dialogue with the Government of Japan on regulatory matters. These dialogues include the identification and canvassing of regulatory issues and suggestions for reform. Current reform policies emphasise the openness of reform authorities to external viewpoints, both domestic and foreign, suggesting that these dialogues will continue to be an important one for future regulatory reform. The quantity of international comments and requests has been large. The Commission of the European Communities provided, in August 1998, a 105 page List of EU Deregulation Proposals for Japan. Similarly, the United States government, in October 1998, submitted 52 pages of US proposals to the Japanese government for promoting further reform in the areas of telecommunications, housing, medical and pharmaceuticals, financial services, energy, legal services, and automotive and motorcycles as well as institutional reforms such as distribution, competition authority and Anti-Monopoly Law, and transparency and other government practices.

Some of the recent Japanese deregulation programmes such as the Big Bang in financial sectors and the abolishment of the LSRS (Large Scale Retail Store Law), seem to be relatively well received by major trading partners.<sup>64</sup> Moreover, the “Three year Programme for the Promotion of Deregulation” decided by Cabinet on March 31, 1998 sets conformity to international standards as one of six main guiding principles of the Programme (see the background report on Government capacity to assure high quality regulation for more detailed discussion of the Programme). Trading partners recognise the progress achieved in many Japanese deregulation initiatives, although they are keeping pressure for further action.

However, Japan’s reactions to direct bilateral trade pressures have been quite mixed. On the one hand, for the purpose of reducing trade conflicts, Japan appears to have taken a serious approach to those negotiations, but on the other hand, it has kept a somewhat defensive attitude regarding the requests of trading partners. As a result, deregulation and/or reforming programmes have been incremental in nature, giving away minimum concessions which touch on potentially vast areas but which result in very little change of the Japanese regulatory system. Their reforming efforts are generally neither adequate to efficiently enhance competition and market openness and to change the Japanese economic system nor sufficiently rapid to produce notable results.

Moreover, the deregulation initiatives reveal that the impediments to imports have not been well assessed. The measures have been concentrated on import procedures rather than the market structure. To date, promotion programmes have been more concerned about adjusting existing procedures than removing major obstacles of market access. The SEP, one of the Japanese economic reform initiatives, envisages the following steps “to promote imports and market opening measures: the creation of import-promotion zones, enhancement of import-related infrastructure, and provision of import incentives in taxation and financial assistance areas”.<sup>65</sup> All the steps relate to border access. Hence, market openness at the border level has been enhanced. However, market openness obstacles include behind the border measures and conditions, such as distribution and access to consumers, where further progress is still needed (see Box 1).

### 4.3 *Potential benefits and costs of further regulatory reform*

Japanese consumers, who are not well informed by market information and are served by highly regulated service sectors and an inefficient distribution system, are losing substantial wealth because of the higher prices they pay compared to their counterparts in the OECD countries. In 1997 on the average, citizens of Tokyo pay 18% more for their purchases than citizens in New York, 8% than those in London, 23% than those in Paris, and 30% than those in Berlin. They also generally pay higher prices for most services. They also generally pay higher prices for most services. Because of protection and inefficiency in the distribution sector, they pay much higher prices for foods & beverages and clothes & footwear as well. As Kato said, "Japanese consumers are living miserably in spite of the abundant wealth they are creating".<sup>66</sup> According to Sazanami (1995), "Japanese tariff and non-tariff barriers inflicted a cost on Japanese consumers of 10 to 15 trillion yen in 1989 (75 to 110 billion US dollars at the 1989 exchange rate). At the expense of consumers, Japanese producers pocketed perhaps 7 to 9.6 trillion yen."<sup>67</sup>

Table 2. Tokyo's price level compared to those of other international cities

Products	New York	London	Paris	Berlin	Geneva
Total	1.18	1.08	1.23	1.30	0.99
Foods and beverages	1.41	1.44	1.56	1.72	1.18
Durable goods	1.24	0.78	0.85	0.86	0.85
Clothes and footwear	1.33	1.37	1.36	1.16	0.97
Energy	1.54	1.41	1.15	1.12	1.01
Water and sewage	1.67	0.78	0.61	0.33	0.87
Transport	1.17	0.94	1.12	1.06	0.96
Telecommunications	1.00	1.16	1.03	0.85	0.94
Health services	0.82	1.55	1.72	4.02	0.36
Education	0.55	0.56	1.20	1.09	0.51
Household services	1.55	1.12	1.55	1.22	1.64
Other services	0.90	0.87	0.93	1.16	0.83

Source: EPA, 1998 Price Report, October 1998.

Many Japanese manufacturing industries which used to be very competitive in the international markets seem to be suffering from declining competitiveness because of expensive domestic intermediary inputs in service sectors. According to MITI's survey report, Japanese industries are paying almost twice as high for non-manufacturing intermediary inputs compared to their competitors of Germany, almost three or four times higher compared to those of other Asian emerging economies, and more than eight times higher compared to their Chinese competitors. The price difference appears to be a bit moderated for manufacturing inputs.

Table 3. **International price difference for intermediary inputs**

	Japan	US	Germany	Korea	Taiwan	Hong Kong	Singapore	China
Total inputs	100	88	70	39	33	53	46	20
Manufacturing	100	91	101	55	65	67	66	45
Non-manufacturing	100	85	51	28	21	43	33	12

Source: MITI, *Survey on Price Differentials between Domestic and International Markets for Intermediary Inputs*, 1998.

The loss of consumer welfare and economic efficiency resulting from regulations not consistent with market openness principles has been very large in Japan. Potential benefits of further reform in this direction are very large as well. The gain which Japanese producers have pocketed thanks to the protection, will be lost if market opening reforms are fully implemented. However, Japanese producers can expect the supplementary efficient gain in terms of competitiveness from those reforms, in exchange of the loss of “protection rent” which has been anyway smaller than consumers’ welfare gain, as Sazanami estimated above.

#### 4.4 *Policy options for consideration*

Considering the potential benefits of further regulatory reform from the market openness perspective, and the assessments of the Japanese regulatory system made above regarding its integration of the six efficient regulatory principles, the Japanese government is encouraged to consider the following six policy options and subsequent detailed recommendations in its further regulatory reform initiatives.

- Enhance transparency from the international perspective in the regulatory process through concrete and wide-ranging steps;
- Heighten government capacity to promote market openness perspectives in regulatory reform;
- Establish a systematic approach to cope with recurring themes in the trade debate, such as lack of openness of procedures, unnecessary trade restrictiveness as well as harmonisation of standards and recognition of foreign conformity assessment;
- Engage pro-actively in public efforts to enlighten the Japanese public, including consumers, of the economy-wide benefits of regulatory reform;
- Enhance regulatory co-operation with other countries; and
- Strengthen competition policy enforcement recognising its increasing importance in promoting market openness.

Enhance transparency from the international perspective in the regulatory process through concrete and wide-ranging steps.

- Following on the announcement of October 1998 that so-called Public Comment Procedures will be adopted for new regulations, implement those procedures in a way that allows foreign firms to participate easily.
- Ensure that all regulations, including information relating to the decision making process, are accessible to foreign parties.
- Enhance the efforts to publish the proceedings (or video recordings) of deliberations or open sessions on regulatory decisions for all advisory council meetings.

- Enhance the efforts to include participants from variety of interests including foreign participants in all decision making process, including participation in advisory councils, that substantially affect the trade and investment openness of the Japanese regulatory system.

Although Japan has made progress in exposing reform discussions more frequently to foreign trading partners, there are still concerns that proceedings are not transparent and vulnerable to bias in their operations. More cross-cutting commitment to open regulatory procedures will raise the level of reform discussions as well as reduce the risk of capture by incumbent interests. The benefits will be shared by consumers and new businesses, both domestic and foreign. Although initial progress was made in the early 1990s, the impact has been limited. A more open approach now seems to be emerging, as shown in the area of telecommunications, and it should be expanded.

- Expand the dissemination of detailed and updated regulatory information such as administrative conduct that may have regulatory effects, ongoing proposals put for comment procedures, and business formalities to ensure its maximum public availability, such as via the Internet

Considering the persistent concerns from abroad about lack of openness of regulatory procedures, the use of the Internet for dissemination of detailed and updated information has great potential. Although such use has started in Japan, it remains under-exploited, particularly when compared to practices in some other countries. The expansion of the Internet for this purpose will particularly benefit new or potential entrants for markets, especially foreign firms. This will go far toward strengthening confidence in Japanese regulation in the eyes of all the market players, domestic or foreign.

- Explicitly limit the discretionary power of ministries and agencies through concrete and effective measures such as limits provided by revised basic laws of ministries.

A fundamental concern of trading partners is that Japanese regulations in practice allow too wide-ranging discretion for regulators in many areas, which results in general uncertainty for future business activities and investment. The limitation of such discretion is crucial not only for raising the growth potential of Japanese economy but also for achieving a clear policy statement favouring foreign direct investment. Transparent and effective remedies should be provided for those aggrieved by administrative actions under broad range of discretion, including foreign parties; explicit limits on discretionary power should be imposed through revision of the ministry's basic laws as well as well-defined and clear policy commitment made under laws delegating regulatory authorities.

Heighten government capacity to promote market openness perspectives in regulatory reform.

- Create a capacity in government, in co-ordination with the economy-wide regulatory reform programme 1) to recommend reform measures from a market openness perspective and 2) to monitor vigorously implementation of those reform measures through strengthened power vis-à-vis other ministries and agencies.
- Heighten the capacity of government officials to cope with the market openness issues by strengthening training programme on international rules for all regulatory officials.

Domestic regulations will continue to be a focus of trade discussions concerning Japan. Foreign voices will have an important role in Japanese regulatory reform as in the past. The current link between market openness perspectives and regulations mainly comes from

translating foreign complaints or requests for consideration by regulatory authorities on an item by item basis. There is no governmental function to work with regulators to systematically improve regulations for market openness, with a view to benefiting both Japanese consumers and foreign trading partners. In order to better achieve the announced Japanese policy stance in favour of international harmonisation of regulations, Japan needs to install a more effective mechanism as well as capacity to plan and implement reform from a market openness perspective. This would support Japan's own regulatory reform initiatives and reduce incremental approach that results in reactions to foreign pressures.

Establish a systematic approach to cope with recurring themes in the trade debate, such as lack of openness of procedures, unnecessary trade restrictiveness as well as harmonisation of standards and recognition of foreign conformity assessment.

- The RIA (regulatory impact analysis) programme recommended in the background report on Government capacity to assure high quality regulation should include assessment of trade and investment impacts. Individual ministries and agencies should be required to report this analysis to Cabinet meeting when they propose new regulations or modifications of existing regulations.
- Require that drafts or discussions of ministerial orders and administrative conduct having regulatory effect which are not scrutinised in Cabinet level meetings should be checked by trade policy bodies, through establishment of more effective consultation process between government bodies.
- Launch government-wide measures to accept the equivalence of foreign conformity assessment, and establish sectoral programmes of reviewing and harmonising technical regulations and standards.

Japan's efforts to date on market openness aspects of regulations have centred on addressing specifically defined issues arising from the requests from its trading partners. This means that although concrete progress has been constantly made, similar concerns in different areas, have been repeated and fundamental problems have not been adequately addressed. By utilising the strengthened mechanisms recommended above, the Japanese government should take a more fundamental approach to address cross-cutting issues as well as establishing the framework under which future progress can be measured.

Engage pro-actively in public efforts to enlighten the Japanese public, including consumers, of the economy-wide benefits of regulatory reform and market openness.

- Promote current and future studies to identify the net benefits for Japan from regulatory reform and market openness.
- Disseminate the research findings widely to the public.

Some of the Japanese public have had a negative impression of continuous external pressures on Japan to reform. In order to maximise benefits of regulatory reform from a market openness perspective in Japan, it would be useful to recognise its own interests in such reform with concrete evidence. Such studies have been undertaken more and more in Japan, at the OECD and elsewhere.

*Enhance regulatory co-operation with other countries.*

- Engage more vigorously in work with trading partners to promote harmonisation and recognition of foreign conformity assessment.

Considering the weight it represents for the global economy, Japan's actions to harmonise regulations and promote recognition of conformity assessment across countries are increasingly crucial for the success of international co-operation. Japan's recent accession to international harmonisation agreement in automobile sector as well as its leadership in APEC standards area have been promising examples in this regard. Recent progress towards MRAs with the EU in several sectors is also a positive point for international regulatory co-operation. By engaging in such co-operation vigorously, Japanese regulators will have more chances to get acquainted with the impact of their regulations on international trade and investment. As regulators are involved more and more in international co-operation, they will face the new challenge to translate its implications to domestic regulatory measures more frequently and quickly. Current efforts should be strengthened and accelerated.

Strengthen competition policy enforcement recognising its increasing importance in promoting market openness.

- Reinforce the role of the JFTC in resolving market access problems.<sup>68</sup>

Meaningful private injunctive relief and private damage actions, combined with reformed rules on Japanese lawyers and foreign legal consultants are important means of redressing some of these problems. Similarly, an expanded role for the JFTC in reviewing regulations that might pose market access concerns is also important.

- Apply competition policy more effectively to private anti-competitive practices by adopting the measures recommended in the background report on The Role of competition policy and enforcement of regulatory reform.

In addition, many of the market access concerns directly related to regulation and regulatory reform appear to be linked, in part, to lingering perceptions about Japanese enforcement of competition policy applied to private anti-competitive practices. Accordingly, strengthened anti-cartel enforcement (particularly with respect to bid-rigging and other "hard core" cartels) and monitoring of potential anti-competitive abuses with respect to distribution channels are also important tools in redressing the market access concerns that arise in the particular context of regulatory reform.

## NOTES

1. MITI (1998), *White Paper on Trade and Industry*.
2. See among others Sazanami, Yoko and others (1995), *Measuring Costs of Protection in Japan*, Institute for International Economics, January 1995; Daiwa Economic Research Institute (1994), *Deregulation Impact on Business*, (in Japanese) January 1994; and Kato, Masashi (ed. 1995), *Economics of Deregulation*, (in Japanese) Toyokeizaishimbunsha, July 1995.
3. EPA (1997), *1997 Price Report*, October 1997 and MITI (1996), *Survey on Price Differentials between Domestic and International Markets for Intermediary Inputs*.
4. Simple mean of post Uruguay Round Bound Tariffs. See OECD (1998), *Review of Tariffs and Non-Tariff Barriers, Tariff Regimes of the Quad Countries*, February 1998.
5. For example, Japan currently does not apply any kind of quantitative trade restriction measures, except the import licencings applied to Chinese and Korean silk and silk products and MFA quotas for some textile products.
6. As one of the special measures to promote imports and inward investment, the Japanese government has established several special zones in the vicinity of main ports and airports. Those who want to establish infrastructure for the purpose of import facilitation in these zones can get various financial and tax incentives from the government.
7. Japanese Government (1998), *Measures for Promoting Foreign Direct Investment in Japan*, August 1998.
8. OECD (1998), *Financial Market Trends - 70*, June, pp. 96-100.
9. In this process, foreign business associations are playing an important role in providing their negotiators with information about certain Japanese regulations which are considered to be major obstacles to effective market access in Japan.
10. One should not omit other important factors which have made the establishment of new large scale stores difficult in Japan. Apart from the Large Scale Retail Store Act, there are high land prices and an inadequate road system. *International Economic Review*, Retail Distribution in Japan, September/October 1997, p 9. See also Motoshige, Itoh, "Regulatory Reform: An Experience of the Japanese Distribution System" in *Regulatory Reform in International Market Openness*, 1996, OECD.
11. OECD (1991), *Economic Survey on Japan*.
12. Frank Gibney (ed.: 1998), *Unlocking the Bureaucrat's Kingdom*, Brookings.
13. The Housewives Association was one of strong opponents to rice market liberalisation. The main reason cited for opposition was lack of confidence in the quality of foreign rice.
14. OECD (1998), *1997-1998 Annual Review - Japan*, ECO/EDR(98)14.
15. See, in particular OECD (1998), "*Open Markets Matter. The benefits of Trade and Investment Liberalisation*", Paris, OECD (1994), "*The environmental effects of Trade*", Paris; and the 1995 Report on Trade and Environment to the OECD Council at Ministerial level.

16. See related discussion in Chapter 2, “Regulatory Quality and Public Sector Reform”, in *The OECD Report on Regulatory Reform, Volume II: Thematic Studies*, OECD, 1997, Paris.
17. According to the Japanese response to the indicators questionnaire on market openness, Japan showed a relatively low score for the questions related with transparency principle compared to OECD average. See the figure of comparative analysis among principles in section 4.
18. US (1998), *Submission by the Government of the United States to the Government of Japan regarding Deregulation, Competition Policy, and Transparency and Other Government Practices in Japan*, October 7 1998.
19. EU (1998: Commission of the European Communities), *Indicative list of EU Deregulation Proposals for Japan*, October 12 1998.
20. US (1998), EU (1998), and Australian Government, *Submission of the Australian Government to the Japanese Government on the Deregulation Promotion Program*, November 6 1998.
21. The problem is that firms often do not know which ministry requests should be submitted to and how these requests are handled.
22. MOF press release, June 8 1998.
23. Interview by the OECD secretariat.
24. The JFTC has carried out a survey of foreign firms in Japan, asking these firms questions about Japanese industry associations. It shows that foreign firms believe that industry associations tend to be used for information dissemination and informal consultation by regulatory authorities. See JFTC (1996), *Report based on the survey on foreign firms about industry associations* (in Japanese).
25. In this report, the term “other administrative conduct” is used to designate such administrative conduct as internal orders and communications notes which does not bind the public directly but may have an indirect regulatory effect on the public through bureaucrats’ administrative actions directed by that kind of conduct.
26. These ad hoc meetings are not limited to those specially convened for once in a purely ad hoc basis, but include those convened in a semi-regular basis, which can last for a certain period of time.
27. According to the Japanese government, all advisory councils (*shingikai*) are now publishing at least summaries of discussions. However, there are still many ad hoc meetings which do not publish anything at all.
28. Unless entrusted by the relevant laws, it shall not have provisions creating penalties, imposing obligations or limiting nationals rights.
29. *Kokka Gyosei Soshiki Ho* (National Government Organisation Law) Art 12(1).
30. A definition is introduced in the background report on Government capacities to assure high quality regulation.
31. WTO (1998), *Notifications under article 6.2 of the TRIMs Agreement on publications in which TRIMs may be found*, G/TRIMS/2/Rev.4, 5 August 1998.
32. According to the strict definition of the Japanese legal system, internal orders and communication notes are not defined as “types of regulations”, because they are deemed to regulate not directly “private sectors” but “bureaucrats” themselves. However, as bureaucrats administer policies and programs in accordance with them, sometimes with administrative guidance, they may have regulatory effect in the practical sense. Furthermore, regulated firms seem to usually consider internal orders and communication notes as another form of regulations,

because these have regulatory effect on their relations with regulatory authorities by binding the decision of regulatory bureaucrats.

33. It seems that the OTO is recently receiving some collected packages of complaints directly from foreign chambers of commerce in Japan and foreign embassies, apart from the complaints directly addressed to the OTO at the individual company level. However, the fact that foreign companies are taking the option to pass through their representatives and not to lodge them directly to the OTO may show the disappointment of foreign companies on the effectiveness of the OTO.
34. The EU has continuously raised this kind of concern, when important trade talks have been held between the US and Japan. Some of market access improvements achieved by these talks seem to have benefited other trading partners. For example, Korea obtained more market access for Japan's semiconductor market after an accord to improve market openness in the sector had been reached between the US and Japan.
35. For telecommunications services, Japan has recently lifted restrictions for most of Type I carriers. It has also decided to abolish foreign ownership restrictions concerning KDD.
36. On the basis of reviews and submissions by member countries, the OECD maintains a list of reservations to the *OECD Code of Liberalisation of Capital Movements*, and *OECD Code of Liberalisation of Current Invisible Operations* (both of which are binding codes containing provisions on non-discrimination), as well as exceptions reported under the *National Treatment Instrument*. The Japanese reservations and exceptions to these instruments, last updated in January 1997, are available through: <http://www.oecd.org/daf/cm/country/japan.htm#n>.
37. See Japan's Exceptions to National Treatment: <http://www.oecd.org/daf/cm/country/japan.htm#n>.
38. Article 27 of the Foreign Exchange and Foreign Trade Law.
39. EU (1998).
40. See OECD (1997), *OECD Report on Regulatory Reform Volume I : Sectoral Studies*, Paris.
41. EU (1998).
42. See Frank Gibney (ed.: 1998), *Unlocking the Bureaucrat's Kingdom*, pp. 2-3.
43. US (1998), EU (1998), and Web Site of Canadian Ministry of Foreign Affairs and Trade.
44. EU (1998).
45. EPA(1997), *Policy Actions on Market Access Issues as Concerns Standards, Certification and Others*, July 1997.
46. The Japanese government gave priority to resolving trade obstacles over investment obstacles at the outset of the OTO. At that time, the OTO was called the Office of Trade Ombudsman. That is why the OTO omits the letter "I" even after it changed its name to include investment as well.
47. Remaining 158 cases are classified in the group for which the situation remains unchanged. In these cases, related ministries explained the reason why they do not change the current situation, and complainants understood the reason.
48. The Japanese Fiscal Year (FY) starts from the first April and ends in 31st March of the next year.

49. Meetings with the American Chamber of Commerce in Japan (ACCJ) and the European Business Council (EBC), July 23, 1998.
50. WTO (1998), *Trade Policy Review of Japan*, January 1998.
51. According to the Japanese government, the number of JIS standards which can be aligned to international ones is limited to 3,000 out of total number of 8,000 and remaining 1,300 (3,000-1,700) JIS standards are already equivalent to international standards.
52. According to the Japanese classification, these machines are categorised into motor vehicles and regulated by Road Transportation Law.
53. Jiro Ushio (1996), chairman of the Japan Association of Corporate Executives, originally in the article "Spread the Gospel of the Market Economy", *Japan Times*, December 1996 1&4 and quoted in "Implications of Competition Policy for International Trade: How Different is Japan From Germany and Does it Matter?" by Mark Tilton of Purdue University at [http://www.nmjc.org/jiap/specrpts/reports/sp2\\_1998.htm](http://www.nmjc.org/jiap/specrpts/reports/sp2_1998.htm), states, "Compared to [the] Anglo-Saxon model, the traditional market rules in Japan and Europe are closed by nature.... Three Japanese practices go against [the liberal] Asia-Pacific model: market rigging within an industry, excessive government control, and a tendency not to throw bad eggs out of the market. Old-fashioned Japanese businesses tend to avoid competing in open markets. some industries condone restrictive business practices and they gang up to shut out new entries. True, rigging the market is a highly efficient way to do business, no one gets hurt through government mediation, and everyone can keep the cost of sales low. The upshot is higher prices, and it is the consumer who ends up holding the bill. compared to other countries (Germany 2.25%, US 6.96%, France 8.94%, and UK 20.65%).".
54. OECD (1997), *Market Access Issues in the Automobile Sector*, Paris.
55. See OECD (1997), "Product Standards, Conformity Assessment and Regulatory Reform" , *OECD Report on Regulatory Reform Volume I : Sectoral Studies*, Paris.
56. *MOT NEWS*, May 20, 1998, Ministry of Transport.
57. For example, *MOT News* No. 88 published on May 20, 1998 explained on a number of revisions of the safety regulations for road vehicles, both for in accordance to Deregulation Action Plan as well as for responding to the need from Japan's entry into the UN/ECE 1958 Agreement.
58. The Ministry of Post and Telecommunications prohibits international Type I carriers from entering into agreements with foreign carriers to terminate international traffic until the Type I carrier has established one hundred or more destinations.
59. JETRO (1998), *The Survey on Actual Conditions Regarding Market Access -- Telecommunication Equipment*, Tokyo.
60. Ministry of Post and Telecommunications' Internet Home Page.
61. The current three-year deregulation programme plans to lift the demand supply adjustment clauses.
62. This inertia to change does not seem to be an unique phenomenon among Japanese bureaucrats. In fact, Japanese firms are very reluctant to shed their employees and/or to abandon their over-invested business, even when they are in great difficulty as they are now. See *The Economist*, "Corporate Japan goes to waste", August 29, 1998.
63. This desire can be found in various government documents. For example, the Maekawa Report (1986) which opened the avenue to of reform in Japan underlined the necessity of internationalisation of the Japanese economy. Various government White Papers have pronounced this desire as well.

64. Meetings with ACCJ and EBC, July 23, 1998.
65. WTO (1998), *Trade Policy Review of Japan*, January 1998 p. 60.
66. Kato (1995).
67. Sazanami and others (1995), p. 2. Because they compared the level of CIF price of imported goods and the level of producer prices for similar goods, the welfare loss might have been underestimated. In fact, in their studies, the supplementary adverse effect of inefficient distribution system was ignored.
68. Many market access concerns reviewed in this report might be remedied to some extent by the general recommendations made in Chapter 3.