

The Report on Compliance by Major Trading Partners with Trade Agreements (WTO, FTA/EPA and IIA) (hereinafter referred to as the “Report”) is a series of annual reports published by the Subcommittee on Unfair Trade Policies and Measures, a division of the Trade Committee of the Industrial Structure Council. The Industrial Structure Council is an official advisory body to the Minister of Economy, Trade and Industry of Japan. The first Report was released in 1992, and this is the 30th volume.

1. Introduction

The Report is the only report in Japan that analyzes, in light of WTO Agreements as well as EPAs, FTAs and IIAs (hereinafter collectively referred to as “EPAs and similar agreements” in the Preface), the status of trade policies and measures of the respective countries and regions (hereinafter sometimes simply referred to as “country(ies)”).

The origin lies in the experience Japan had in the course of its rapid economic growth as a trading nation that it was “unilaterally” blamed as implementing unfair trade measures based only on the “results” of trade surplus, etc. and requested to correct economic imbalance. Against such “result-oriented approach” and “unilateral sanctions”, the Report has consistently been asking what “fairness” means to pursue dispassionate and constructive solutions to trade friction and insisting on “rule-oriented approach”.

In other words, “result-oriented approach,” which allows a country to regard the trade policies and measures of its trading partner as unfair only because there are any unfavorable “results,” lacks objectivity and may evolve into managed trade and produce anti-competitive effects. “Fairness” of each country’s trade policies and measures should be assessed not based on results but on internationally agreed-upon rules. International are no appropriate international rules, the establishment of new rule should be pursued first, and fairness or unfairness should not be discussed without international discipline. This approach, or “rule-oriented approach,” is the “fairness” that the Report has insisted and the (principle) we have to be based on.

These efforts have been successful, and “rule-oriented approach” is now prevailing globally. The fact that many trade measures have to date been addressed at bilateral and multilateral talks as being suspected of violations of international rules and the number of cases using the WTO dispute settlement procedures reached 600 can be viewed as the evidence.

The origin of the multilateral free-trade system that supports global trade rules can be traced back to the Havana Charter, an agreement concluded to establish an International Trade Organization (ITO) for reconstructing the international trade system after World War II. The Charter failed because it was not ratified by the necessary number of signatory countries. However, the spirit has been inherited by the General Agreement on Tariffs and Trade (GATT), coming into effect over 70 years ago, and then the World Trade Organization (WTO), inaugurated a quarter of a century ago. WTO members, 164 countries and regions, substantially cover the entire world economy.

Meanwhile, since the first publication of the Report in 1992, the global trade environment has change enormously. Countries have struggled to establish a multilateral free-trade system

supported by effective, rule-based dispute settlement procedures, and it has facilitated the remarkable growth of emerging economies, the deepening of global value chains, and the progress of the Fourth Industrial Revolution, and thus a profound contribution to the global economy in its astonishingly rapid development. Many bilateral or regional EPAs and FTAs have been concluded, and so-called “mega-FTAs/EPAs” have progressed significantly as the RCEP was signed last year in addition to the enactment of the CPTPP and Japan-EU EPA. The number of International Investment Agreements (IIAs) concluded is also growing.

In recent years, in the face of behaviors of some emerging economies - market-distorting subsidies, forced transfer of technology, infringement of intellectual property rights, and expansion of business activities under the influence of public-sector entities, such as governments and state-owned enterprises (SOE), a concern is spreading that they might distort the base of competition and the function of the market which are the foundation of the multilateral free-trade system. The significance of evaluating these measures based on the “rule-oriented approach” and addressing them in the Report is becoming more and more important than ever.

Policy makers often refer “fair competitive conditions” and “equal-footing of competitive conditions” as level playing field¹. What should be regarded as “fair competitive conditions” may differ depending on the standpoint from which one talks about the issue. However, it can be said that a broad consensus has been achieved for the idea that such conditions should have an accumulation of internationally agreed-upon rules as an integral part foundation. We highly think of the government of Japan in keeping away from any market-distorting measures that take advantage of loopholes in the rules or any unilateral measures designed from a “result-oriented” way of thinking, and instead holding fast to the “rule-oriented approach” as basic approach. In the first volume of the Report, we cited a phrase, “All are sinners.” It implies what is important is humble attitudes of asking all the parties concerned to work together and solve problems. We expect the government of Japan to give thought again to the importance of the concept and make significant contribution for securing the base of competition that underpins the multilateral free-trade system.

Furthermore, the spread of COVID-19 since last year has also been greatly impacting the trade environment. Although international cooperation has been promoted, “national priority” and “protectionism” trade-restrictive measures such as export restrictions on medical-related products have also been taken. Therefore, it is necessary to pay attention not to allow the base of competition and the function of the market which are the foundation of the multilateral free-trade system to be distorted by excessive measures taken behind critical situations. In addition, during the COVID-19 crisis, digitalization is accelerating in all areas of the society and efforts to establish new international rules are increasing. Furthermore, also coupled with geopolitical environmental changes, economic security efforts of the respective countries, including the strengthening of supply chains, are progressing.

The Report, while referring to the environmental changes mentioned thus far, describes the

¹For instance, discussions at the Japan, US, and EU Trade Ministers Meeting (since December 2017).

topics related to recent trends. We hope that it will help readers understand the Japanese trade environment.

2. Objectives of the Report

The Report has three main objectives: (1) Securing of Compliance with International Rules (WTO Agreements, EPAs, etc.); (2) Presentation of “Rule-oriented Approach” as Basic Approach; and (3) Promotion of Further Understanding of International Rules.

(1) Securing of Compliance with International Rules (WTO Agreements and EPAs and similar agreements)

The first objective of the Report lies in making sure that countries will comply with international rules in their trade policies and measures by analyzing consistency between them.

So far, the Report, in light of internationally agreed-upon rules such as WTO Agreements, EPAs and similar agreements, has identified problems in trade policies and measures adopted by Japan's major trading partner countries and regions to urge them to remove or otherwise remedy them.

With changes observed in the Japanese industry community in their trade and investment activities, both in quality and scale, and increased weight of new players in the order of global trade, the Report has increasingly important roles to play in analyzing consistency of their trade policies and measures with international rules and offering perspectives from which solutions should be designed.

(2) Presentation of “Rule-oriented Approach” as Basic Approach

The second objective is presentation of “rule-oriented Approach” as basic approach.

In early 1990s, when the first volume of the Report was produced, countries, inclined to evaluate trade policies and measures of their trading partners using “result-oriented approach,” often found themselves in all the greater difficulty in solving diverse and complex problems of the international economy. After the inauguration of the WTO in 1995, they more often take up the issue of consistency of trade policies and measures adopted by their counterparts with international rules. Such changes may be viewed as evidence that “rule-oriented approach,” the basic approach of the Report, has got widely accepted.

The Report has also pointed out the importance of using the dispute settlement procedures under the WTO as specific measures for solving international economic problems. Major trading countries around the world have come to recognize any trade policies or measures questionable under the WTO Agreements should be referred to the WTO dispute settlement procedures to ask for fair and objective judgment. Cases have also been accumulated of disputes settled through the arbitration procedures provided by an IIA or an FTA and those settled by an international arbitration body. Here, we would like to point out again the fact that practice of “rule-oriented approach,” under which governments and businesses actively make use of dispute settlement procedures, has laid the foundation for the stability of the multilateral trade system.

(3) Promotion of Further Understanding of International Rules

The third objective is promotion of further understanding of international rules (WTO Agreements, EPAs and similar agreements).

Having come into force in 1995, the WTO Agreements serve as a fundamental framework that sets multilateral rules for international trade. EPAs and similar agreements concluded by many countries are also important as new international rules that complement the WTO Agreements. However, it would be too early to say that these international rules have been broadly recognized or fully understood by businesses and people. Accordingly, the Report explains again the current rules, together with and basic principles lying behind them. We hope that these explanations, coupled with the analyses of the trade policies and measures of different countries under particular examples, will promote further understanding by various parties of the significance and potential of the WTO Agreements and other international rules.

3. “Rule-oriented approach” as Basic Approach

(1) Significance of “Rule-oriented Approach”

Since first published, the Report has been holding up the “rule-oriented approach,” an approach of evaluating trade policies and measures of countries based on internationally agreed-upon rules.

When mentioning the “rules” under the “rule-oriented approach,” the Report deals with three categories of rules below.

The first category is the WTO Agreements. The WTO Agreements go beyond the scope of its predecessor (GATT, which covered only trade in goods) to provide rules for new areas such as trade in services and protection of intellectual property rights. These are the most comprehensive international rules regarding international trade.

The second set of rules we employ is found in international treaties other than the WTO Agreements, basic principles of international law and customary international law. These disciplines, international agreements concluded in the areas covered or not covered by the WTO Agreements and other standards supporting the international law system, are considered supplements to the WTO Agreements. Examples of international treaties other than WTO agreements include: EPAs/FTAs; IIAs; bilateral agreements governing bilateral economic and trade issues; and multilateral agreements other than the WTO Agreement.

The general principles of international law and other international customary law may not be codified in treaties, but they nevertheless constitute rules which Japan and all other countries are supposed to observe.

Trade policies and measures of countries should be evaluated according to “rule-oriented approach” for three reasons.

Maintenance of the base of internationally agreed-upon rules

Issues of fairness in market competition should not be focused on the results of competition, but on the rules under which competition takes place. As long as fair competition takes place under agreed-upon rules, challenging the fairness of results (result-based criteria) might destruct the base of agreed-upon rules.

Securing of effectiveness of international agreement

When countries reach agreement in international negotiations and commit to the fulfillment of mutual obligations, they should cite and seek remedies for the breach of those obligations. Such an approach is both justified and necessary to secure the effectiveness of agreements.

Avoidance of turning trade problems into political issues

An indispensable means of avoiding needless misunderstandings and emotionalism over trade concerns, as well as of preventing trade friction from becoming a political issue, is to evaluate objectively whether criticism and complaints about a country's trade policies and practices in fact have any basis under internationally agreed-upon rules. The WTO prohibits its members from unilaterally recognizing other countries' behaviors as violating the WTO Agreements and resorting to sanctions or countermeasures before any decision is made through its dispute settlement procedures. Also, under many of Japan's EPAs, forums have been established for discussing improvements to the business environment, enabling the parties to discuss the trade and investment-related systems and the implementation status of partner countries. Moreover, rules of dispute settlement under many EPAs and similar agreements provide the procedures through which investors can obtain remedies based on international law by submitting a case to arbitration against the host state, in the case of problems arising between investors and states, which function as a useful tool to secure the implementation of rules. With Japan getting more closely linked with countries around the world in their economic relationships, the government of Japan must select effective tools and channels depending on types and characteristics of different trade issues to solve them in a dispassionate and constructive manner according to rules.

(2) Problems with “Result-oriented Approach”

The Report has so far pointed out problems of “result-oriented approach,” a contrary concept for “rule-oriented approach.” The “result-oriented approach” allows a country to brand as “unfair” or “unreasonable” the trade policies or measures of another country only because there are any “results” the country does not like, such as trade imbalance or poor export performance of specific products. There are many problems associated with this approach as described below.

Lack of Objectivity

The result-oriented approach has the most serious problem in its lack of objectivity as it allows a country to unilaterally evaluate trade policies and measures of other countries. The evaluation itself is not necessarily based on any internationally agreed-upon rules. The country may wrongly regard the “results” of trade as a consequence of any policies or measures adopted by its trading partner, and determine them “unfair” even when they are in fact not responsible.

Danger of Turning into “Managed Trade” (Anti-Competitive Effect)

The result-oriented approach may easily turn into “managed trade” as the approach often comes together with a policy that demands trading partners to achieve specific results (numerical targets), such as market share or import value of products imported from a specific country. Such demand involves risk that it may hinder functions of genuine competition, what should be called engine of the market economy. That would represent an abrogation of the basic principles of the WTO Agreements to develop the world economy according to market disciplines.

(3) Economic Perspectives that Supplement “Rule-Oriented Approach”

The Report, placing the legal analysis of trade policies and measures of countries at the core, also refers briefly to their “economic implications” to complement the analysis for three reasons.

The first reason is that trade policies and measures that depart from international trade rules and dispute settlement mechanisms that have been agreed upon generally have negative economic implications. They reduce the predictability and transparency of international trade and distort the smooth flow of goods and services, thereby exerting a substantially detrimental influence on the economic welfare of each country. Complementary analysis of these economic effects should assist the better understanding of the importance of international trading rules and dispute-settlement mechanisms.

Second, the existing international trading rules and dispute settlement mechanisms serve as institutional frameworks for the economic activities of national governments, producers, and consumers and have a significant effect on the level of economic welfare that is achieved thereunder. Understanding the economic implications of the rules and mechanisms is of importance to understanding the meaning and significance of the current system.

Third, international trade rules and dispute-settlement mechanisms are not set in stone. They are merely institutional frameworks that can be changed at any time if there is an international consensus to do so. In searching for new international disciplines, we must have an accurate understanding of the implications that possible alternative rules and mechanisms will have on countries’ economic welfare, and we must make a choice regarding the systems that we prefer.

4. Structure of the Report

Main parts and their objectives

The Report consists of three main parts.

Part I deals with Japan’s major trade partners’ policies and measures that are problematic under the WTO Agreements and other international rules. (In principle, this Report is described based on the information as of the end of February 2021.)

Part II contains an overview of what Part I starts from, namely, the WTO Agreements and other international rules. (In this regard, Part II does not offer the whole picture of the WTO Agreements.)

Part III provides analysis and explanations concerning rules of EPAs and similar agreements, sector by sector. Also, there are several columns which discuss special topics every year with the focus on current issues, etc.

Furthermore, in general terms, in order to seek to improve another country's policy/measure based on international rules, it is necessary for the private citizens including the industries and experts, and governments to function together. Again, in this volume, we try to provide information on developments of the WTO Agreements and EPAs and similar agreements in an active manner.

In Part I, we have described a three-step framework in principle, namely, i) outline of the measure, ii) problems under international rules, and iii) recent developments. These descriptions indicate how a country's measures could be problems under the WTO Agreements and will lead to a better understanding of the WTO Agreements for readers. Moreover, we have tried to describe the reactions of the Japanese government specifically. We hope that these feedbacks of our policy information will lead to understanding of trade policies in general and help promote public-private cooperation. For this purpose, before preparing this report, the Secretariat announced a list of topics to be included for this volume of the Report and invited public comments on these and any other topics.

Criteria for Selecting Trading Partners

We have made it a rule to cover in Part I of the Report a dozen or so economies important to Japan, based on the amount of bilateral trade with each (total exports and imports). In this 2021 volume of the Report, we covered the economies of China, ASEAN^(Note 1), the United States, EU/UK^(Note 2), Republic of Korea, Taiwan, Australia, Canada, Russian Federation, India, and Brazil in accordance with the said criteria.

(Note 1) Although ASEAN did not accede to the WTO as an independent customs territory, it is collectively dealt with in one chapter because there are problems addressed that are common to ASEAN countries.

(Note 2) The UK has withdrawn from the EU on January 31, 2020, and the transition period has expired on December 31 of the same year, achieving complete withdrawal from EU laws. Therefore, in the Report, measures concerning the UK are collectively addressed in the same Chapter 4 with the EU for convenience.

Figure P-1 Amount of Trade with Japan

China	32.6
ASEAN	20.5
United States	20.0
EU/UK	14.2
Korea	7.6
Taiwan	7.6

Australia	5.1
Canada	1.9
Russian Federation	1.8
India	1.5
Brazil	1.1
World Total	136.2

(Remarks) Prepared from Ministry of Finance “Trade Statistics for 2020” (confirmed). In trillion yen.

Policies and Measures Discussed

In Part I, the trade and investment policies and measures of the covered economies are discussed. Business practices and such that have nothing to do with the policies and measures taken by a particular government are not discussed here. Among the policies and measures of each, Part I conducts examinations on those that may be problematic in terms of consistency with the WTO Agreements and other international rules with a focus on those that are considered to be important to Japan’s economic and trade activities.

There also are some trade and investment policies and measures that do not expressly violate the WTO Agreements or other international rules, but that contravene the spirit of the WTO and should be liberated or controlled under new rules. These areas generally include high tariffs, non-concession, service and government procurement, etc. They are included with the statement “this particular case was included in light of the following concerns despite it being a trade or investment policy or measure that does not expressly violate the WTO Agreements or other international rules” at the beginning of each case.

Other Matters

Unless otherwise stated, this Report indicates the state of affairs as of the end of February 2021. However, additions shall be made in case of noteworthy progress thereafter.

The Report is available on the METI website.

https://www.meti.go.jp/policy/trade_policy/wto/3_dispute_settlement/32_wto_rules_and_compliance_report/321_past_report/compliance_report.html