

## **Section 2 Promotion of the multilateral free trade system and creation of strategic external economic relations**

While it is undeniable that the Great East Japan Earthquake has caused tremendous damage to Japan, we need to launch initiatives to revitalize our country so that we can secure the reconstruction of East Japan and deal with the challenges that had been facing us since prior to the earthquake. To this end, this section explains our initiatives for promoting a multilateral free trade system and building strategic external economic relations, which are necessary to improve Japanese companies' competitiveness, expand exports from Japan, increase employment, and create an environment facilitating Japanese companies' strength overseas.

### **1. FTAs/EPAs and active promotion of regional economic integration**

#### **(1) Movements related to FTAs/EPAs in recent years**

As mentioned in Section 3 of Chapter 1, the number of FTAs/EPAs has been increasing year after year, as a result of the accelerated movements toward regional integration, driven by the changes in the global economic environment and development strategies around the world, since the 1990s. The reasons for such an increase in FTAs/EPAs include the following: [1] Moves have accelerated in the United States and Europe toward economic partnerships with their economically-linked neighboring countries through liberalization and the promotion of trade and investment, illustrated by the accelerated efforts by the U.S. and the EC for NAFTA (in effect since 1994) and the EU (established in 1993), respectively; [2] While NIEs and ASEAN have achieved high economic growth by opening up their markets ahead of other countries, emerging economies, such as Chile, Mexico and Peru, have changed their economic policies, liberalizing trade and investment and introducing market mechanisms. In doing so, they have adopted the strategy of utilizing FTAs /EPAs; and [3] East Asian countries, including Japan, have changed their stances in favor of EPAs/FTAs, etc. The number of regional trade agreements reported to the WTO reached 474 as of July 31, 2010.

With regard to this expanding network of FTAs/EPAs, their two characteristics in recent years are signing of high-quality agreements on top of the increase in the number, and increasingly active initiatives for broader regional economic partnerships in the Asia Pacific.<sup>1</sup>

#### **(A) The spread of high-quality FTAs/EPAs**

One of the major objectives of FTAs/EPAs is to promote trade by reducing tariffs among signatory nations, and it is customary to show the extent of tariff elimination as liberalization rates of FTAs/EPAs. Under international economic rules, FTAs/EPAs are treated as an exception

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<sup>1</sup> With regard to the individual FTAs of the U.S., Europe and other major countries/regions, see the Ministry of Economy, Trade and Industry, Japan, (2011), FUKOUSEI BOUEKI HOUKOKUSHO 2011 edition, p.474 onwards.

to the GATT (General Agreement on Tariffs and Trade) /WTO (World Trade Organization) regime, and GATT signatories are allowed to conclude preferential free trade agreements with other member nations on the condition that “within a reasonable length of time” the duties and other restrictive regulations are eliminated on “substantially all the trade between the constituent territories in products originating in such territories”.<sup>2</sup> Although there is no established interpretation concerning the conditions for concluding FTAs under these GATT rules, the general understanding is that tariffs should be eliminated on at least 90% of trade (in terms of trade value or tariff lines) within 10 years, and each agreement’s tariff elimination within the 10-year time frame is used for comparison as representing the liberalization rate.

With regard to the FTAs concluded among developed nations/major countries in recent years, an increasing number of them achieved the liberalization rate of no less than 95% on a tariff line basis. For example, in the case of the FTAs signed by the U.S., the rates for the U.S.-Chile FTA (effective January 2004) are the U.S.’s 97.6% and Chile’s 97.7%, while those for the U.S.-Australia FTA (effective January 2005) are the U.S.’s 96.0% and Australia’s 99.9%. The liberalization rates for the U.S.-South Korea FTA (signed June 2007) are the U.S.’s 99.2% and South Korea’s 98.2% (those for the revised 2010 agreement are even higher). The rates for the U.S.-Peru FTA (effective February 2009) are the U.S.’s 98.2% and Peru’s 99.3%.<sup>3</sup> In the case of the EU-South Korea FTA signed in October 2010, the liberalization rates are the EU’s 99.6% and South Korea’s 98.1%

The high liberalization rates mean that economic actors in the signatory nations can trade without tariff barriers on a larger number of items, and such high-quality FTAs are expected to make considerable contributions to the signatory nations' trade expansion and economic growth.

## **(B) Movements toward broader regional economic partnerships in the Asia Pacific**

Along with the spread of high-quality FTAs, another noteworthy movement in recent years is the increasingly active initiatives aimed at broader regional economic partnerships in the Asia Pacific.

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<sup>2</sup> GATT Article XXIV 5 (excerpt) Accordingly, the provisions of this Agreement shall not prevent, as between the territories of contracting parties, the formation of a customs union or of a free-trade area or the adoption of an interim agreement necessary for the formation of a customs union or of a free-trade area; Provided that:

(c) Any interim agreement referred to in sub-paragraphs (a) and (b) shall include a plan and schedule for the formation of such a customs union or of such a free-trade area within a reasonable length of time.

GATT Article XXIV 8 (excerpt) For the purposes of this Agreement: (b) A free-trade area shall be understood to mean a group of two or more customs territories in which the duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated on substantially all the trade between the constituent territories in products originating in such territories.

<sup>3</sup> Cabinet Secretariat, “HOUKATSUTEKI KEIZAI RENKEI NI KANSURU KIHON HOUSHIN NI TSUITE” (January, 2011). Figures on a tariff line basis.

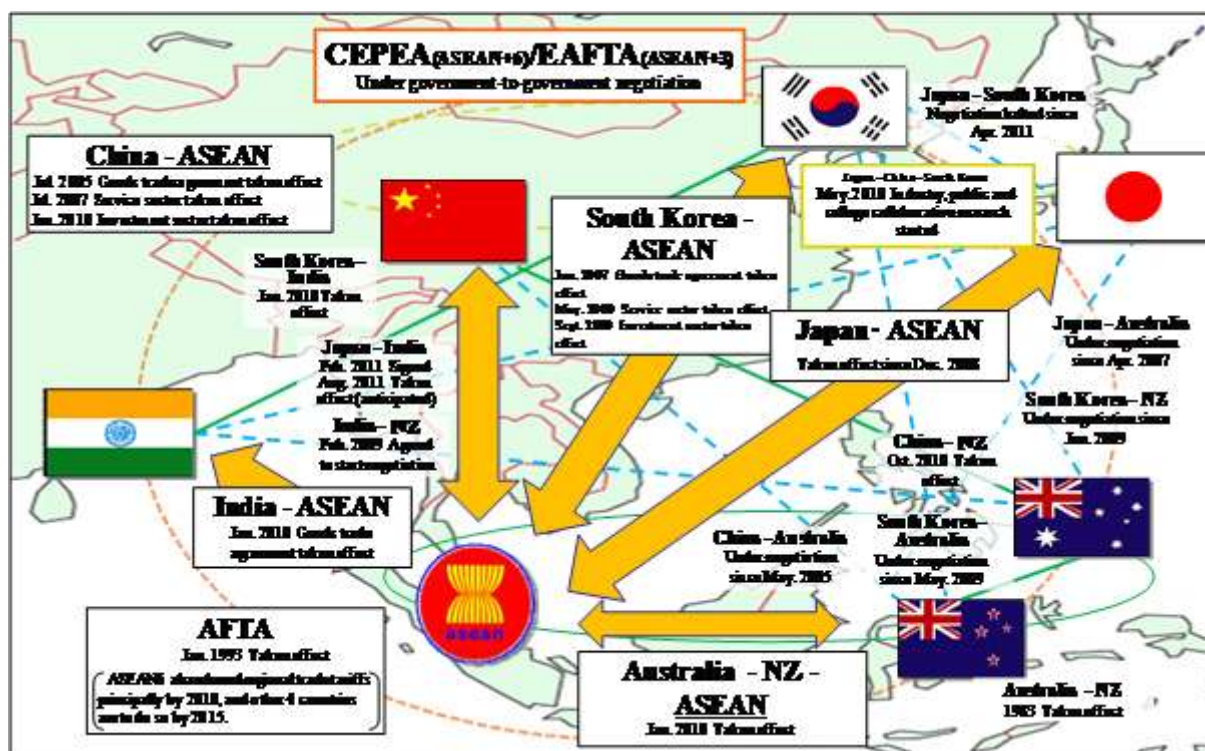
In 2010, the tariffs among the six original ASEAN Member Countries (Indonesia, Singapore, Thailand, Philippines, Malaysia and Brunei) were eliminated in principle, and in the goods sector, all of the “ASEAN plus 1” FTAs came into effect, causing observers to say that the FTAs in East Asia have entered a new stage.<sup>4</sup> The “ASEAN + 1” FTA is a FTA that ASEAN signed with each one of the six countries in the ASEAN neighborhood (Japan, China, South Korea, India, Australia, NZ) separately. As a result, an East Asian-wide FTA network emerged, with ASEAN serving as its hub. Specifically, the Japan-ASEAN EPA (AJCEP) (negotiations ongoing for investment and services) went into effect in 2008.<sup>5</sup> With regard to the China-ASEAN FTA, the agreement for the goods sector went into effect in 2005, followed by that for the services in 2007, and then in 2010, that for the investment sector came into force as well. The South Korea-ASEAN FTA went into effect in 2007 for the goods sector, followed by that for services and investment in 2009. With regard to the India-ASEAN FTA, that for the goods sector came into force in January 2010, while the ASEAN-Australia/New Zealand FTA, a comprehensive one covering goods, services and investment, went into effect also in January 2010. And, with regard to the bilateral FTAs among the countries in the ASEAN neighborhood as well, there has been steady progress (see Figure 5-2-1-1).

**Figure 5-2-1-1 Movements of economic partnerships in East Asia**

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<sup>4</sup> With regard to Australia and New Zealand, it's a tripartite FTA between these two countries and ASEAN.

<sup>5</sup> The EPA came into effect on December 1, 2008 between Japan and the ASEAN countries of Singapore, Laos, Vietnam and Myanmar, followed by Japan-Brunei on January 1, 2009, Japan-Malaysia on February 1, 2009, Japan-Thailand on June 1, 2009, Japan-Cambodia on December 1, 2009, and Japan-the Philippines on July 1, 2010.



Source: Ministry of Economy, Trade and Industry.

Following the spread of these FTA networks in the East Asia/Asia Pacific region, the next important step would be to launch initiatives for a broader regional economic partnership. Partly as a result of the building of the FTA networks, there has been a considerable development of the cross-border production sharing as well as the concentration/optimal allocation of production resources. Companies' initiatives to upgrade their supply chains all over Asia would be encouraged even further, if, through a broader regional economic partnership, tariffs are cut under a more unified market access schedule, the Cumulative Rules of Origin (CRO) are enabled, and various rules concerning business activities are unified. Under such an environment, companies would be able to optimize their business processes, while individual countries can realize the combinatorial optimization of comparative advantages and even more efficient economies, enabling the region as a whole to grow more.

As for the movements for broader regional economic partnerships in East Asia, there is an initiative to create a trilateral FTA among Japan, China and South Korea, and joint study meetings by these countries' representatives of industry, the government and academia have been held four times since May 2010 (as of April 2011). And at present, inter-governmental discussions have been underway also with respect to the East Asia Free Trade Area (EAFTA) by the "ASEAN plus 3" embracing ASEAN 10 and the three countries of Japan, China and South Korea, as well as concerning the Comprehensive Economic Partnership in East Asia (CEPEA) by the "ASEAN plus 6" comprising the "ASEAN plus 3", Australia, New Zealand and India, by

identifying specific fields for the talks. There have been also initiatives which are not limited to East Asia but extend to the Asia Pacific as a whole, such as the Free Trade Area of the Asia-Pacific (FTAAP) proposed in November 2006 by the U.S. (under then-president George W. Bush), and the Trans-Pacific Partnership (TPP) Agreement which initially entered into force in 2006 as the Trans-Pacific Strategic Economic Partnership Agreement (the so-called P4 agreement) between Singapore, New Zealand, Chile and Brunei, and is now being renegotiated as part of the expansion in membership to include the U.S., Australia, Peru, Vietnam, and Malaysia. The FTAAP is an initiative which aims at free trade in the Asia Pacific, and at the APEC Economic Leaders' Meeting held in Yokohama in November 2010, it was confirmed that an “FTAAP should be pursued as a comprehensive free trade agreement by developing and building on ongoing regional undertakings, such as ASEAN+3, ASEAN+6, and the Trans-Pacific Partnership, among others”, and it was declared that concrete steps would be taken toward its realization.<sup>6</sup>

Thus, in East Asia and the Asia Pacific, various initiatives aimed at broader regional partnerships are in progress in a multilayered manner, with a synergistic effect to promote them. Details of each initiative's specific situation would be explained in “(3) Japan’s efforts for economic partnerships based on the ‘Basic Policy’ ”.

## **(2) Japan's efforts thus far and formulation of the “Basic Policy on Comprehensive Economic Partnerships”**

### **(A) Efforts thus far and Japan falling behind**

Since our first EPA, with Singapore, came into effect in November 2002, Japan has concluded EPAs with 10 countries and one economy. (There are also agreements with two other countries which were already signed but have yet to go into effect) (see Table 5-2-1-2).

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<sup>6</sup> Pathways To A Free Trade Area Of The Asia Pacific (FTAAP) (APEC Leaders' Meeting on November 13-14, 2010)

**Table 5-2-1-2 EPAs that Japan has thus far concluded or signed**

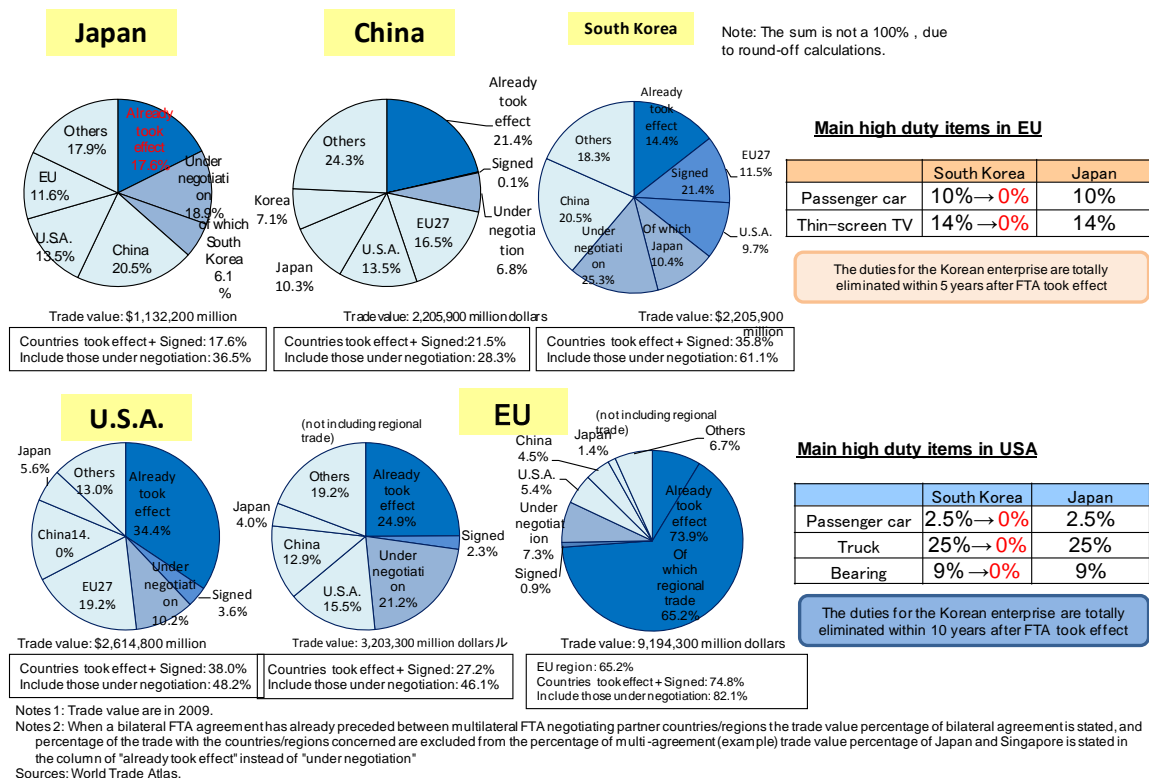
Partner countries/regions	Date of Effect
Singapore	November, 2002
Mexico	April, 2005
Malaysia	July, 2006
Chile	September, 2007
Thailand	November, 2007
Indonesia	July, 2008
Brunei	July, 2008
ASEAN	December, 2008 -
The Philippines	December, 2008
Switzerland	September, 2009
Vietnam	October, 2009
India	February, 2011 (Signed / not having taken effect)*
Peru	May, 2011 (Signed / not having taken effect)

Note: EPA between Japan and India will become effective on August 1, 2011.

Source: Compiled from the data of Ministry of Economy, Trade and Industry.

But the ratio of trade covered by the signed and effective FTAs/EPAs to the country's total trade value is mere 17.6% in the case of Japan, compared with 38.0% for the U.S., 35.8% for South Korea and 21.5% for China, showing a delay in the Japanese efforts (see Figure 5-2-1-3).

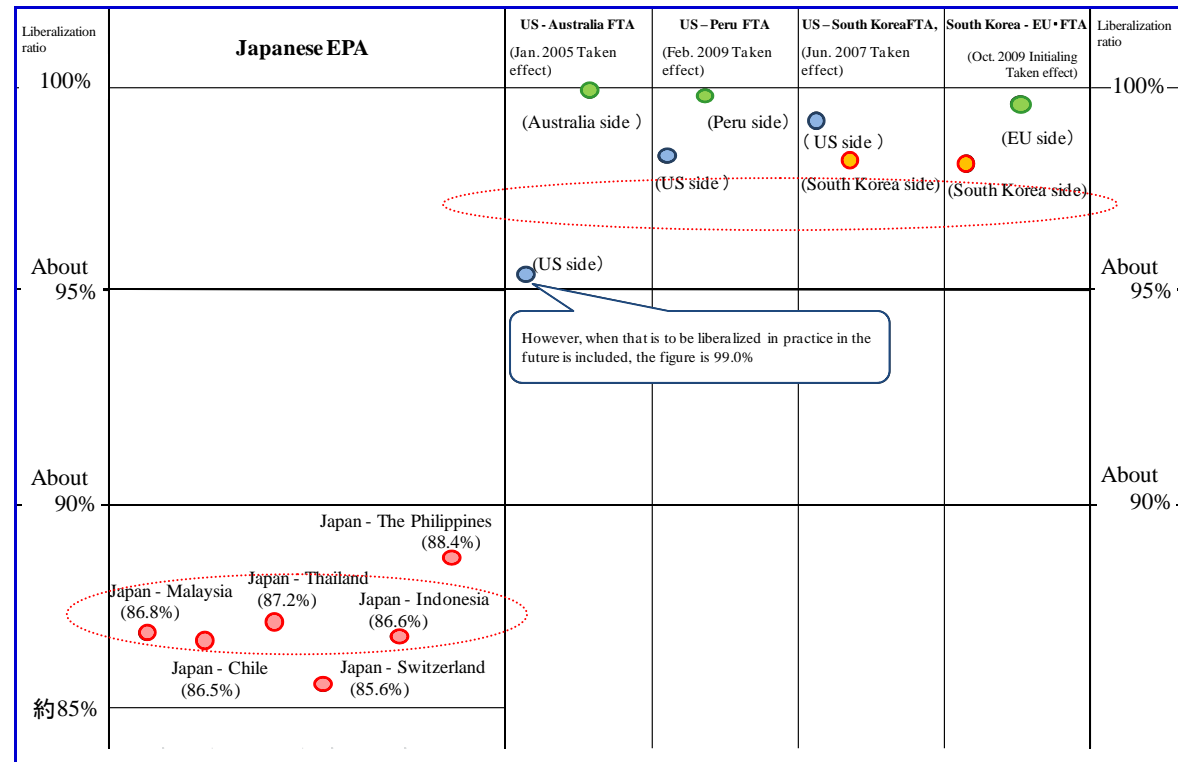
**Figure 5-2-1-3 Proportion of FTA/EPA in the trade value of the major country, and major high tariff rate items of the EU, U.S. (as at June, 2011)**



What is thought to be a major cause of such a delay is the Japanese EPAs' low liberalization rate in comparison to international standards. The liberalization rate of the EPAs concluded by Japan stands at no less than 90% on a trade value basis, but it is about 86-87% on a tariff line basis. This reflects the fact that Japan has set up many exceptions to the liberalization. As mentioned before, an increasing number of FTAs, especially those between developed countries, have achieved liberalization rates of no less than 95%, and almost 100% on a tariff line basis. In view of this fact, there is no denying that the liberalization rate of the FTAs concluded by Japan thus far has been low (see Figure 5-2-1-4). The more the number of items treated as exceptions to liberalization, the more it would become difficult for us to seek our trading partners' liberalization with regard to the items of interest to us. And, resultant limitations on the room for negotiations cause an impasse in the trade talks itself.

In a sense, to this day Japan has selected/concluded the EPAs which allow many exceptions to the liberalization principle in a bid to start with what it can do. But, now that the EPAs with the ASEAN and South American countries, which are positive towards them, have been basically settled, Japan would need to accept a higher level of liberalization commitments in view of the sort of countries/regions with which Japan should actively promote the EPAs from now on. Thus, Japan's efforts for significantly reducing the exceptions to the liberalization principle become essential so that Japan can catch up with other countries in the promotion of EPAs.

**Figure 5-2-1-4 Comparison of liberalization rate between EPAs of Japan and FTAs of U.S.A., etc.<sup>7</sup>**



Notes: This table shows liberalization ratio on item basis (ratio of items to be abolished duty within ten years in proportion of all items).

However, when it comes to Japanese EPA, liberalization ratios on trade value basis are generally achieved more than 90% (ratio of items to be abolished duty within ten years in proportion of import-value).

More than 99% in Japan-Brunei EPA and Japan-Switzerland one, and more than 95% in Japan-Singapore EPA, Japan-Malaysia and Japan-Vietnam ones.

Material: Compiled from “Opening the Country Forum”, Cabinet Secretariat

## **(B) The need for high-level EPAs and formulation of the “Basic Policy on Comprehensive Economic Partnerships”**

If Japan's trade and investment environment becomes less attractive than in other countries as a result of the delay in taking the initiative for EPAs, there is a possibility that future employment opportunities will be lost because of the impaired locational/export competitiveness. These adverse effects on Japanese companies' competitiveness are particularly significant in relation to South Korea. While South Korea has already surpassed Japan in the overseas market share of some products in sectors such as electric machinery and electronics, some Japanese items will be forced to bear the burden of EU and/or U.S. import tariffs, estimated to be higher by as much as 10% or more compared with those imposed on South Korean products in these huge markets

<sup>7</sup> Source: Cabinet Secretariat-sponsored “KAIKOKU FORUM: HEISEI NO KAIKOKU TO WATASHITACHI NO KURASHI”



if South Korea's already-signed FTAs with the EU and the U.S. come into effect (see Figure 5-2-1-3 Reprint). In a global marketplace where companies (especially manufacturers) are engaged in intense cost-conscious competition, such percentage differences in the level of tariffs are significant.

Japan's manufacturing sector is already shrinking, with the number of production bases and employment both decreasing. The shrinkage of Japan's domestic manufacturing industry can be attributed to non-EPA factors such as a change in the industrial structure itself, exchange rates, the cheap labor cost overseas and corporate taxes, but the delay in making efforts for EPAs is also considered one of the causes of hollowing-out.

If we wish to overcome this situation and achieve sustained growth amid the expectation of a shrinkage of the domestic market, we need to rebuild the infrastructure for future growth and development by capturing the potential for growth in Asian and emerging countries, the U.S., Europe, and resource-rich countries, etc. through the cultivation of deeper economic ties with them.

Based on such understanding, on November 9, 2010, the Japanese Cabinet approved a "Basic Policy on Comprehensive Economic Partnerships" (hereafter referred to as the "Basic Policy"). It expressed the firm resolve to open up the country, stating that the government of Japan "will take major steps forward from its present posture and promote high-level economic partnerships with major trading powers that will withstand comparison with the trends of other such relationships". It says: "With regard to EPAs or broader regional economic partnerships that are politically and economically important and will be of especially great benefit to Japan, the Government of Japan, while taking into consideration the sensitivity of trade in certain products, will subject all goods to negotiations for trade liberalization and, through such negotiations, pursue high-level economic partnerships." Meanwhile, there is necessity for "fundamental domestic reforms in order to strengthen the competitiveness it will need for economic partnerships of this kind." In particular, agriculture is a field where "considering Japan's aging farming population, the difficulty farmers have in finding people to take over their farms when they are ready to retire, and the low rate of profit, there is a risk that sustainable agriculture will not be possible in the future." The "Basic Policy" stipulates that with a view to "opening the country" as well as pursuing high-level economic partnerships, the Japanese government will first promote appropriate domestic reforms with respect to areas of the agricultural industry, movement of natural persons, and regulatory reforms.

With regard to specific efforts for economic partnerships, it says that in the Asia Pacific region Japan will increase its efforts to conclude the ongoing EPA negotiations, start talks for broader regional economic partnerships which have been studied, and promote EPAs with major countries/regions with which Japan has not yet started negotiations. Concerning the TPP

Agreement, it states that “it is necessary to act through gathering further information, and Japan, while moving expeditiously to improve domestic environment, will commence consultations with the TPP member countries.” It is also stipulated that Japan will make efforts with regard to major countries/regions<sup>8</sup> outside the Asia-Pacific such as EU and GCC (Gulf Cooperation Council) countries, and other countries/regions, especially newly emerging nations and resource-rich countries (see Table 5-2-1-5).

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<sup>8</sup> Bahrain, Kuwait, Qatar, Oman, Saudi Arabia, and the United Arab Emirates.

**Table 5-2-1-5 Basic policy on comprehensive economic cooperation (excerpt)<sup>9</sup>**

**Basic Policy on Comprehensive Economic Cooperation (approved by Cabinet meeting on Dec. 9, 2010)**

**1. The environment surrounding Japan, and promotion of high level economic cooperation**

Japan now faces a big change that could be called a watershed. When it comes to the global economy, structural change is ongoing in that the relative position of Japan is decreasing while emerging economies rapidly develop. In addition, although the reinforcement of international trade rules through the agreement of the WTO Doha Development Agenda negotiations remains important, high level FTA/EPA networks among major trading countries are expanding while the prospect of negotiations is unclear. However, Japan's response has been rather slow.

Under such conditions, When Japan's trade and investment environment is unfavorable to other countries, future employment opportunities could be lost. In order to realize a "strong economy" shown in the "New Growth Strategy" (approved by Cabinet meeting on Jun. 18, 2010), it is necessary to deepen economic relations between Asian countries and emerging countries, and, where can be expected, European countries and resource-rich countries, and to reconstruct bases for growth and development toward building a better future for Japan.

Under such recognition, we make solid decisions for the sake of "opening the country" and "opening the future", making a big step away from our past position, and promote high-level economic cooperation between the world's major trading countries that keep pace with global trends. At the same time, we will promote radical domestic reforms such as strengthening the competitive edge that is necessary for high-level economic cooperation and so on.

Especially, since the agricultural sector is not only the most likely to be affected by the liberalization of trade but also, taking the aging of Japan's agricultural work force, the shortage of successors, and low profitability into consideration, the future sustainability of the sector is a major concern, and a bold measurable response that boosts the potential domestic agricultural sector such as strengthening its competitive edge and expanding of overseas demand is needed.

Especially, the Asia-Pacific region is the most critical region for the politics, economy and security of Japan, and this region's stability and prosperity is a life and death issue. The Free Trade Area of Asia Pacific (FTAAP) is important in forming a seamless Asia-Pacific region with Japan, and it is necessary to show leadership for its realization.

Therefore, we will take a leading role in the aggressive promotion in bilateral EPAs in the Asia-Pacific region, and promoting broad regional economic cooperation and tackling according to each sector in APEC, and work toward forming trade and investment rules in the Asia-Pacific region fit for the 21<sup>st</sup> century.

**2. Concrete actions strengthening comprehensive economic cooperation**

Based on the international and regional environment surrounding Japan, we will execute the following concrete actions to reinforce comprehensive economic cooperation with the major trading partner countries and regions for Japan. Particularly politically, concerning EPAs and broad regional economic cooperation that are important politically and economically that bring big benefits to Japan, paying consideration to sensitive items, making all items to be subject of liberalization negotiation, we intend to high level economic cooperation via negotiation.

- (1) Action in the Asia-Pacific region
- (2) Action with major countries and regions other than the Asia-Pacific region
- (3) Action with other countries and regions

**3. Integral execution of economic cooperation negotiations and domestic measures**

- (1) Agriculture

<sup>9</sup> For the full text, see <http://www.npu.go.jp/pdf/20101109/20101109.pdf> (National Policy Unit)

- |   |
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| (2) Movement of human resources<br>(3) Reforms of the regulatory system |
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Following the adoption of the “Basic Policy”, the “Ministerial Meeting for FTAAP/EPA”, “Headquarters for the Revitalization of Food, Agriculture, Forestry, and Fisheries” (established within the Cabinet) and the “Working Group on the Movement of Natural Persons” (established under the Minister of State for National Policy) were established, with the aim of considering the specifics of how to promote economic partnerships and domestic reforms. Through these and their subsidiary meetings, discussions, including those at the ministerial level, have been ongoing. In addition, with regard to some of the related reforms of regulations and systems, discussions were conducted under the Government Revitalization Unit.

For the purpose of explaining the government’s thinking on “Opening of Japan in our modern Heisei era” advanced by Prime Minister Naoto Kan, and hearing firsthand opinions of the people from a wide variety of fields for future reference, a plan was made after the formulation of the “Basic Policy” that the Cabinet Secretariat tried to sponsor the “Opening-of-the-country forum: Heisei Opening and our Lives” from February to March of 2011 in a total of nine cities across Japan. Although the forums except for those in Saitama, Kanazawa and Sendai cities were cancelled as a result of the effects of the March 11 Great East Japan Earthquake, the three forums were attended by the Minister for National Policy Koichiro Genba, Minister of Economy, Trade and Industry Banri Kaieda, Senior Vice Minister of Cabinet Office Tatsuo Hirano, and Senior Vice Minister of Finance Fumihiko Igarashi, as well as by expert panelists from fields such as the agriculture, forestry and fisheries, and the business, labor and consumer sectors. They, together with participants recruited from the general public, were engaged in the discussions.

Furthermore, on May 17, 2011, the Japanese Cabinet approved the “Guideline on Policy Promotion” which set out principles on the occasion of re-launching efforts to revitalize Japan following the March 2011 Great East Japan Earthquake. As one of the “Seven Basic Principles for Restarting”, this guideline spells out the need to “revitalize the economy in an open manner by strengthening ‘Kizuna’ (the bonds of friendship)”, and, with regard to FTAs/EPAs, it says “the Minister-level Meeting on FTAAP/EPA will consider the basic policy for strengthening “Kizuna” (the bonds of friendship) with other countries, such as promoting high-level economic partnerships based on the “Basic Policy on Comprehensive Economic Partnership” and establishing economic security, taking into consideration factors such as the sentiments of the farmers and fishing industry personnel who have suffered enormous damage by the earthquake and the nuclear incident, the progresses in the international negotiations, and concerns of de-industrialization.” At the same time, it was confirmed that the basic thinking and direction of the “Basic Policy” would be maintained.



**Figure 5-2-1-6 Policy Promotion Guidance -- for Revival of Japan -- (excerpt)<sup>10</sup>**

- 2. Restart for Japan's revival
  - (1) Basic 7 principles for revival
    - 6) Opened economic revival via strengthening of bond between state and state
  - (2) Ways to promote each major policies
    - II. Redesigning and re-strengthening of national strategy for new growth
      - Strategy to strengthen interstate bonds
        - In FTAAP and EPA-related ministerial meetings taking into account the needs of farmers and fishing industry workers hit by the Great East Japan Earthquake, the progress of international negotiation and concerns about industrial hollowing out, we are considering our basic stance about strengthening interstate bonds such as the promotion of high level economic cooperation and economic security and so on.
        - We are considering when to participate in TPP agreement negotiations.
      - Revival strategy for agriculture and fisheries
        - In the “realization of the revival of the food and agriculture, forestry and fisheries meeting”, we are considering measures to meet requirement for new problems regarding the revival of East Japan's agriculture, forestry and fishery industries, and promoting a recovery in confidence of the agricultural and marine products of Japan.
        - When it comes to new basic policy settled in the “Basic Policy on Comprehensive Economic Cooperation” and new processes instead of the October Action Plan, we will consider them based on conditions of the progress of Japan’s revival as a whole.

<sup>10</sup> For the full text, see <http://www.npu.go.jp/policy/pdf/001.pdf> (National Policy Unit)

## **Column 6 Significance of FTAs/ EPAs**

The primary significance of Free Trade Agreements/ Economic Partnership Agreements (FTAs/ EPAs) is supposed to be expansion of trade promoted by tariff reductions among member countries. However, FTAs/ EPAs usually stipulate matters in various areas including services, investment, intellectual property, government procurement and others. Establishment of new rules covering a whole region is especially meaningful in the regional economic partnership for which efforts for accomplishment are supposed to be accelerated in the future. Therefore, the significance of FTAs/ EPAs is discussed in the light of tariffs and rules focusing on examples of the existing FTAs/ EPAs<sup>11</sup>.

### **<Merits of tariff reduction>**

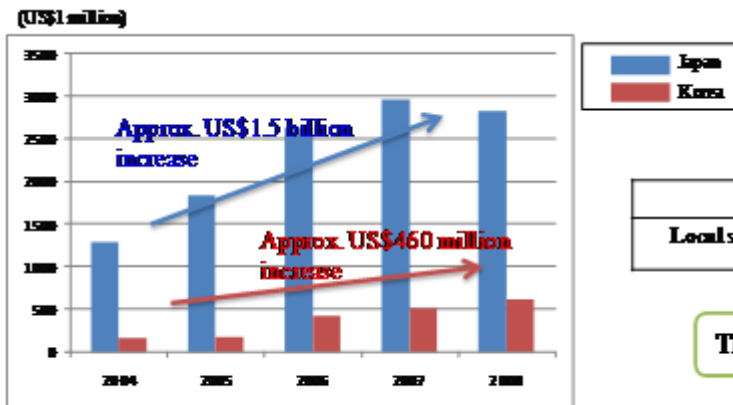
Trade of commodities that gained price competitiveness caused by tariff reduction of an FTA/ EPA may increase between contracting countries. For example, examining the transition of export volumes of Japan to the EPA partner countries after the EPA became effective, exports to Mexico (effective in April 2005) increased 1.8-fold between 2004 and 2008; exports to Malaysia (effective in July 2006) increased 1.5-fold between 2005 and 2008.<sup>12</sup> Such merits as increased trade can be effectively achieved by contracting FTAs/ EPAs ahead of other countries. The EPA between Japan and Mexico which had gone ahead of Korea, resulted in a significant increase in Japanese automobile exports to Mexico compared to those of Korea's. The share of Japan's automobile sales in Mexico showed a substantial expansion and reached 38.1% in 2009 from 27.3% in 2004 (Figure 6-1). With the accelerating hollowing-out of manufacturing industry, it may possible that equalizing production conditions via tariffs between Japan and the partner countries may prevent the hollowing out of industry and maintain the job opportunities in Japan.

## **Column Figure 6-1 Exports to Mexico and local sales shares before and after the Mexico EPA**

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<sup>11</sup> Addition to the increased trade and investment by the tariff reduction and unification of rules, it is expected that companies' production methods, technology and skills can be improved to enhance productivity and profitability in the course of deepening economic unification and bring positive impact to the entire economy.

<sup>12</sup> For details, refer to White Paper on International Economy and Trade 2010, page 383 and below.



Source: Global Trade Atlas

(US\$1 million)

	FY 2004	FY 2009
Local sales share	27.5%	38.1%

The share increased approximately 10%

Source: White paper on trade and investment 2009 edition, ETRIO

Adversely, when Japan is behind the third countries, as already described in Chapter 5, Section 2, 1 (2) (B), it may possible to escalate exporting production. Japan's manufacturing industry accelerated its transfer of production bases to Thailand due to the Thailand-Australia FTA, which became effective in January 2005, while the Japan-Australia EPA has not been signed yet. A flow has been established that Japanese automobiles have been manufactured in Thailand and exported to Australia. This caused a significant decline in the share of Japanese automobiles imported to Australia. (Figure 6-2). It has a great merit as Japanese manufacturing industry can its operations overseas aiming at optimum locations; a part of the profit yielded by expansion of local production returns to Japan; exports of parts that can be manufactured only in Japan are increased. On the other hand, it may cause a substantial negative impact on domestic employment and administration of local governments due to the overseas transfer of core production bases. Especially small and medium enterprises are severely affected by the shift due to difficulties locating abroad. The equalizing competitiveness which can be partially achieved through FTAs/ EPAs is strongly required.

**Column Figure 6-2 Effect of the Thailand-Australia FTA and movement of commercial car imports to Australia**



Movement of commercial cars import to Australia

			2004	2009	(ratio to 2004)
Commercial cars	Total import amount		2,556	3,484	
	Share	Japan	43.8	23.4	-20.4
		Thailand	25.3	50.4	+25.0

(Unit: US\$1 million, %)

Effect of Thailand Australia FTA (January 2005)

Sources: Australia Trade Statistics




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#### <Merits of rule formulation>

The importance of FTAs/ EPAs other than tariff reduction included the improvement of business activities by the formulation of rules. It is really effective to establish common rules for global business activities to reduce various transaction costs, maintain the equality of Japanese companies' exports and investments in other countries and to make Japan more desirable for inward FDI.

(Table 6-3 column).

**Table 6-3 column Composition of chapters in the Japan-Switzerland EPA, Japan-India EPA and Japan-Peru EPA**

	 Japan-Switzerland EPA (Took effect in September, 2009)	 Japan-India EPA (Signed in February, 2011)	 Japan-Peru EPA (Signed in May, 2011)
Ch. 1	General	General	General
Ch. 2	Trade of goods	Trade of goods	Trade of goods
Ch. 3	Customs procedures and smoothing trade	Country of origin rules	Country of origin rules
Ch. 4	Sanitary and plants quarantine measure	Customs procedures	Customs procedures and smoothing trade
Ch. 5	Compulsory standards, adoptive standards and adequacy assessment procedures	Compulsory standards, adoptive standards and adequacy assessment procedures and sanitary and plants quarantine measure	Plants quarantine measure
Ch. 6	Trade of services	Trade of services	Compulsory standards, adoptive standards and

			adequacy assessment procedures
Ch. 7	Movement of natural person	Movement of natural person	Trade of services across border
Ch. 8	Electronics commercial transaction	Investment	Electric and communication services stay for commercial purpose
Ch. 9	Investment	Intellectual property	Immigration and temporary
Ch. 10	Competition	Government procurement	Government procurement
Ch. 11	Intellectual property	Competition	Intellectual property
Ch. 12	Government procurement	Preparation of business environment	Competition
Ch. 13	Closeness of economic relationship	Cooperation	Preparation of business environment
Ch. 14	Dispute settlement	Dispute settlement	Cooperation
Ch. 15	Administration of the agreement	Final regulations	Dispute settlement
Ch. 16	Final regulations		Final regulations

Source: Ministry of Economy, Trade and Industry

Unlike tariff reductions, effects provided by the formulation of rules are difficult to measure with figures, but, for example, the formulation of the government procurement rules in the Japan-Mexico EPA stipulated that “the government procurement is principally carried out by the domestic bidding”. This stipulation enabled Japanese companies to enter the Mexican government procurement market and to receive orders along with the Mexican and FTA countries’ companies on equal terms, though international bidding had been opened only for Mexican and FTA countries’ companies. In addition, the “Sub-committee on Improvement of the Business Environment”, stipulated in the chapter of the business environment improvement of EPAs with Asian countries, Chile and Mexico, is very useful to solve companies’ specific issues on partner countries’ business environment such as improvement of customs clearance, infrastructure, maintaining public safety, measures against faked products and improvement of authentication standards<sup>13</sup>.

Moreover, recently Japanese companies especially in the service industry increasingly have deployed shops and stores and have operated the business in ASEAN countries utilizing advantage of know-how on retail sales, distribution and service to customers which have been cultivated in the domestic market for years. Preparation of rules for chapters of service and investment may facilitate matters such as the easing of regulations and enhancing the transparency for Japanese companies operating in the partner countries, the elimination of conditioning to business activities, dialogue and dispute settlement for problems when they

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<sup>13</sup> For details, refer to “Unfair trade report 2011” (Ministry of Economy, Trade and Industry) page 727 and below.

happen.

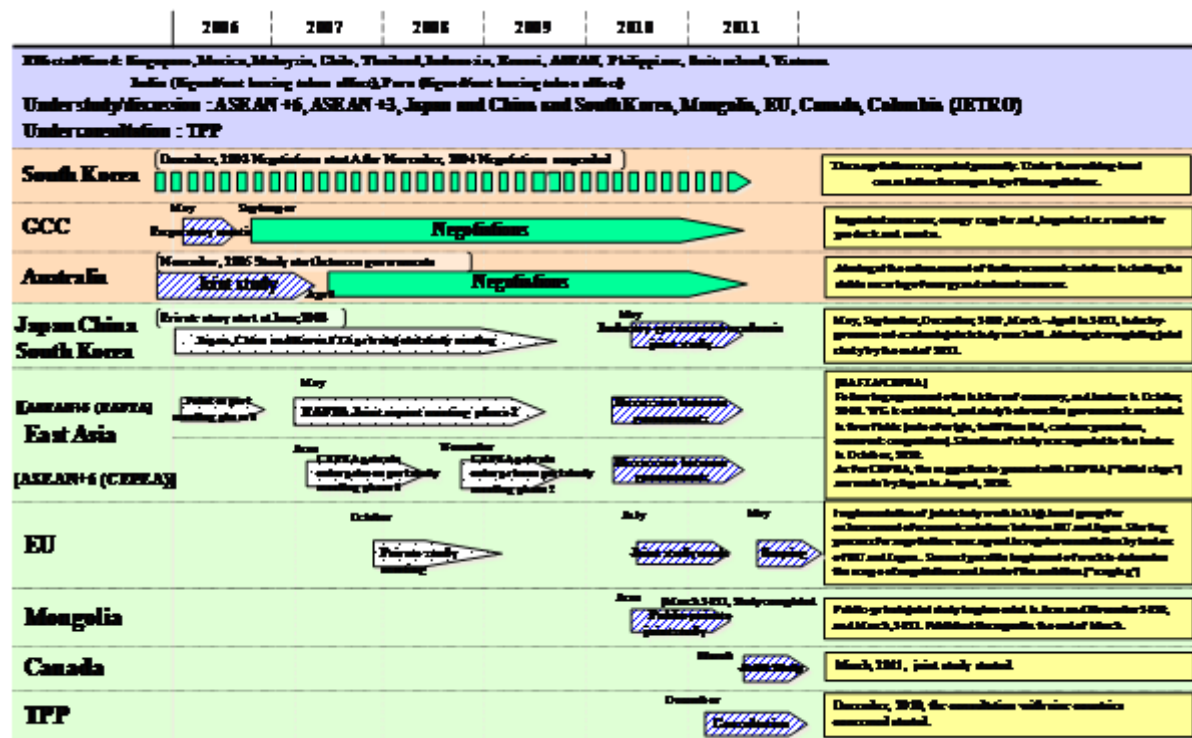
Establishment of rules for economic partnership is effective to promote business activities of Japanese companies operating in foreign countries to reduce risks and local costs.

### (3) Japan's efforts toward economic partnerships based on the “Basic Policy”

#### (A) FTAs/EPAs under negotiation, discussion or study

As mentioned at the beginning, countries are increasingly active in their efforts for FTAs/EPAs. With a view to helping Japanese companies expand their global reach, our country will continue to be active in promoting FTA/EPA negotiations while taking into consideration factors such as the sentiments of the farmers and fishing industry workers who have suffered enormous damage by the earthquake and the nuclear incident, progress in the international negotiations, and concerns about de-industrialization. Here we will explain our current efforts by classifying them into those in (a) the Asia-Pacific region, (b) major countries and regions outside the Asia-Pacific, and (c) other countries and regions (see Figure 5-2-1-7).

Figure 5-2-1-7 Conditions of Japanese actions toward EPAs



Source: Ministry of Economy, Trade and Industry.

#### (a) Efforts in the Asia Pacific region

The Asia Pacific region is important for Japan from the political, economic and security

points of view, and it is very beneficial for the prosperity of Japan to deepen its partnership with the region. FTAs/EPAs could become an important tool to create a seamless market in the Asia Pacific and capture the vitality of the region. Japan has already concluded an EPA with ASEAN as a whole, in addition to seven bilateral EPAs with ASEAN countries (Singapore, Malaysia, Thailand, Indonesia, Brunei, Philippines, and Vietnam). With regard to the efforts for EPAs in the Asia Pacific region other than the ASEAN, Japan concluded the negotiations successfully with India and Peru (the EPA with India was signed in February 2011, and is scheduled to go into effect on August 1, while that with Peru was signed in May 2011). Furthermore, the EPA with Australia is under negotiation, while that with South Korea has been suspended. The EPAs with Mongolia and Canada are under consideration.

Negotiations with India were launched in January 2007, signed in February 2011, and scheduled to go into effect on August 1. India has a population of more than 1 billion people and is the third-largest economy in Asia, enjoying considerable economic growth in recent years. By joining hands with India towards trade liberalization/facilitation, investment promotion and improvement of rules/systems in related fields, we can expect further expansion of business opportunities, even stronger bilateral economic ties, and thus a closer Japan-India relationship as a whole. At present, the Japan-India economic relationship is not necessarily reflective of the two countries' economic size. For example, Japan's exports to India (791.7 billion yen in 2010) account for only 1.1% of our total exports, while the ratio of imports from India to total Japanese imports is as low as 0.8% (496.7 billion yen in 2010). With the Japan-India EPA coming into effect, it is hoped that the bilateral trade/economic relations will be strengthened.

EPA negotiations with Peru started in May 2009, leading to the signing of an agreement in May 2011. Peru has achieved high economic growth in recent years (maintaining growth for 11 consecutive years till 2009). Through measures such as reduction of the 44% tariff (in 2009 on a trade value basis), Japan can hope to strengthen its economic partnership with this growing market. In recent years Peru has been active in promoting FTA talks. Peru's FTAs with countries such as the U.S., China and Canada have been already in effect, while those with the EU, South Korea, Panama, Costa Rica and Mexico have been signed (yet to go into effect). Thus, the EPA with Peru has become all the more important for Japan so that Japanese companies do not lose their competitive edge in the Peruvian market. Furthermore, Peru is one of the major sources of Japan's mineral resource imports (zinc: 3rd, copper: 3rd in 2009), so it's also important from the perspective of securing a stable supply of natural resources for Japan. The Japan-Peru EPA, signed in May 2011, will eliminate tariffs on goods accounting for more than 99% (albeit excluding used goods) of two-way trade value between the two countries in ten years after coming into effect, so its early implementation is desirable.

The EPA negotiations with Australia were launched in April 2007. The EPA with Australia is

expected to help strengthen the “comprehensive strategic relationship” with the country, which shares fundamental values and strategic interests with us, and also boost bilateral trade and investment through such measures as tariff elimination. Furthermore, Japan relies on Australia heavily for iron ore, coal and other raw materials. So, the EPA with Australia is also expected to be helpful from the viewpoint of securing a stable supply source of natural resources, energy and food.

The EPA negotiations with South Korea, which began in December 2003, were suspended after the 6th meeting in November 2004. Since 2008, both countries have started moving towards resuming negotiations. Under the agreement made between the top leaders in April 2008, working-level meetings to build up an environment for discussion and study were held four times by the end of 2009 in order to work towards resuming negotiations. And, at the May 2010 summit talks, Japanese and South Korean leaders agreed to launch a high-level prior consultation towards resuming negotiations, and in September 2010 and May 2011 the prior consultation meetings were held at the level of director-generals. As of June 2011, the negotiations have not yet resumed. But the EPA is supposed to symbolize a “new era” in Japan-South Korea relations which was agreed upon at the summit meeting of February 2008, and it is also significant from multifaceted perspectives like the expansion of bilateral trade/investment and the two countries’ international competitiveness. Therefore, an early resumption of negotiations is hoped for.

The EPAs with Mongolia and Canada have been also under consideration. With regard to Mongolia, the governments of Japan and Mongolia held the joint public-private study meetings on a bilateral EPA in June 2010, November 2010 and March 2011, with the participation of representatives from government, industrial and academic sectors of the two countries. As a result, they finalized a joint study group report recommending to the leaders of both countries that they should launch negotiations on the Japan-Mongolia EPA immediately. Mongolia, a country endowed with rich mineral resources, has not yet concluded any FTA or EPA with foreign countries. If Japan becomes Mongolia’s first EPA partner, it would be of great significance not only from the standpoint of securing a stable supply source of natural resources but also for strengthening our friendly relationship with Mongolia.

With regard to Canada, the joint study on the overall economic relations between the two countries under the “Japan-Canada Economic Framework” was completed in October 2007, with the two countries agreeing to revisit the possibility of an EPA to follow up the study through appropriate channels. Following the November 2010 summit meeting where the two countries’ leaders agree to positively consider promotion of economic partnership, the two sides discussed the issue at a vice-minister level economic meeting in February 2011 and agreed to launch a joint study. The first joint study meeting was held in March in Toronto, followed by the

second one in April in Vancouver. Canada, a country endowed with abundant energy and mineral resources, holds the world's second-largest reserves of oil (including oil sands) behind Saudi Arabia, and ranks second in the production of uranium, third in nickel, and fourth in zinc, etc. With a view to securing a stable supply of these natural resources, it would be of great significance to deepen economic ties with Canada.

Among efforts covering large areas are a proposed FTA among Japan, China and South Korea, CEPEA and EAFTA. (TPP will be discussed in (B))

Japan, China, and South Korea had conducted joint research at the private-sector level about an FTA among these three countries since 2003. It was decided at the 6th Japan-China-Republic of Korea Trilateral Economic & Trade Ministers' Meeting to start joint research involving government, business, and academia in the first half of 2010. This decision was made based on the talks at the 2nd Japan-China-Republic of Korea Trilateral Summit Meeting held earlier in October 2009. The first joint study meeting on the FTA, involving the three countries' government officials and experts from industrial and academic sectors, was held in May 2010. By April 2011 this meeting had been held four times in total. And, at the Japan-China-ROK Trilateral Summit held on May 21/22, 2011, the three countries' leaders agreed to accelerate the Joint Study on a trilateral FTA so that the study will be concluded within this year, moving up the initial goal of completing it before the trilateral summit of 2012.<sup>14</sup> To this end, we intend to continue vigorous discussions hereafter.

The East Asia Free Trade Area (EAFTA) initiative of "ASEAN+3", which consists of ASEAN 10 countries and the three countries of Japan, China and South Korea, has been under study by the joint expert group since 2005, while the Comprehensive Economic Partnership for East Asia (CEPEA) initiative of "ASEAN+6" (Japan, China, South Korea, India, Australia and New Zealand), proposed by Japan in 2006, has been studied by experts from the private sector since 2007. The final reports on these two proposals were submitted to economic ministers and top leaders in 2009, and it was agreed that they would launch intergovernmental discussions on the contents of the reports. For the intergovernmental discussions, four working groups in charge of rules of origin, tariff nomenclature, customs procedures, and economic cooperation were set up, and the rules/management of five "ASEAN+1" FTAs have been compared/analyzed within each group.

At the meeting of ASEAN+6 Economic Ministers in August 2010, Japan put forward its concept paper titled "Initial Steps towards Regional Integration in East Asia: A Gradual

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<sup>14</sup> Japan-China-ROK Trilateral Summit Declaration (excerpt) "Taking into account the current circumstances in Japan and their implications and noting the progress of the Joint Study on a trilateral Free Trade Agreement (FTA) and the recommendation from the Economic and Trade Ministers as well as Foreign Ministers, we decided to accelerate the Joint Study on a trilateral FTA so that the study will be concluded within this year and follow-ups will be taken thereafter."

Approach” which depicts the medium- to long-term direction of economic integration of ASEAN+6. This is a comprehensive proposal designed to promote the discussions within aforementioned working groups in the four fields and help move towards a greater economic integration based on a two-axis approach promoting liberalization on the one hand and facilitating development on the other. It also expressed expectation for intellectual contributions by the Economic Research Institute for ASEAN and East Asia (ERIA) (see Column 7). Also in August in 2010 at the ASEAN+3 Economic Ministers Meeting, China proposed a EAFTA-related roadmap on trade facilitation which aims to reduce the trade cost within ASEAN+3 by at least 5% by 2015.

At the ASEAN Plus Three Summit held in October 2010, the current status of examination by working groups was reported. And the leaders welcomed the Japanese and Chinese proposals, and tasked relevant officials to recommend specific targets and timelines with regard to the efforts for regional economic integration.

With regard to CEPEA and EAFTA, two of the “ASEAN plus” moves for broader regional economic partnerships, the Chair’s Statement of the May 2011 ASEAN Summit noted that the leaders tasked the officials to intensify efforts with a view to making a recommendation for a possible modality using the existing five “ASEAN Plus One” FTAs as the building blocks and the basis for the evolving architecture of regional economic integration.<sup>15</sup> This is a new movement with regard to this matter. Through such efforts for broader regional economic integration in East Asia, we can expect to promote cross-border production sharing as well as the concentration/optimal allocation of production bases, thus boosting the efficiency of the economy as a whole and international competitiveness of the industries in East Asia.

Along with efforts for broader regional economic partnerships, Japan would be able to support the realization of the “Master Plan on ASEAN Connectivity” adopted at the ASEAN Summit Meeting as well as the “Comprehensive Asia Development Plan” proposed by ERIA (Economic Research Institute for ASEAN and East Asia) at the East Asia Summit in 2010, thus helping promote the broader regional infrastructure development and strengthen regional connectivity in both hard and soft aspects. A study made by ERIA after the Great East Japan

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<sup>15</sup> Paragraph 43 of Chair's Statement of the ASEAN Summit: “We took note of the progress on the work of the four ASEAN Plus Working Groups that were tasked to look into the recommendations in the Studies on the East Asia Free Trade Area (EAFTA) and the Comprehensive Economic Partnership in East Asia (CEPEA) in parallel. To ensure and strengthen ASEAN centrality in its objectives to promote partnership with wider region, we tasked the officials to intensify efforts to accelerate the process of consolidating ASEAN’s Plus One FTAs by identifying the gaps and making a recommendation for a possible modality, using the ASEAN Plus One FTAs as the building blocks and the basis for the evolving ASEAN-centered regional architecture.” With regard to the specifics of the ASEAN-related economic ministers meetings of 2010, including Japanese proposals, see the METI website:

([http://www.meti.go.jp/policy/trade\\_policy/ASEAN/html/ASEAN1008.html](http://www.meti.go.jp/policy/trade_policy/ASEAN/html/ASEAN1008.html)).

Earthquake<sup>16</sup> also shows that strengthening of intra-Asian connectivity will bring about the recovery of the Japanese economy. For example, construction of bridges and highways in Asia, infrastructure development of the Mekong-India Economic Corridor (MIEC)<sup>17</sup> including opening of a new port, and strengthening of partnerships between Japan and MIEC-related countries in “soft” aspects such as reinforcement of air and sea routes and reduction of non-tariff barriers will not only bring high economic growth to Asian nations but is also expected to boost Japanese GDP by 4.14%, according to the ERIA study (see Figures 5-2-1-8, 9, 10).

Thus, strengthening links between Japan and Asian countries and reinforcing intra-regional connectivity would bring growth not only for the economies of Asian nations but also for that of Japan as well.

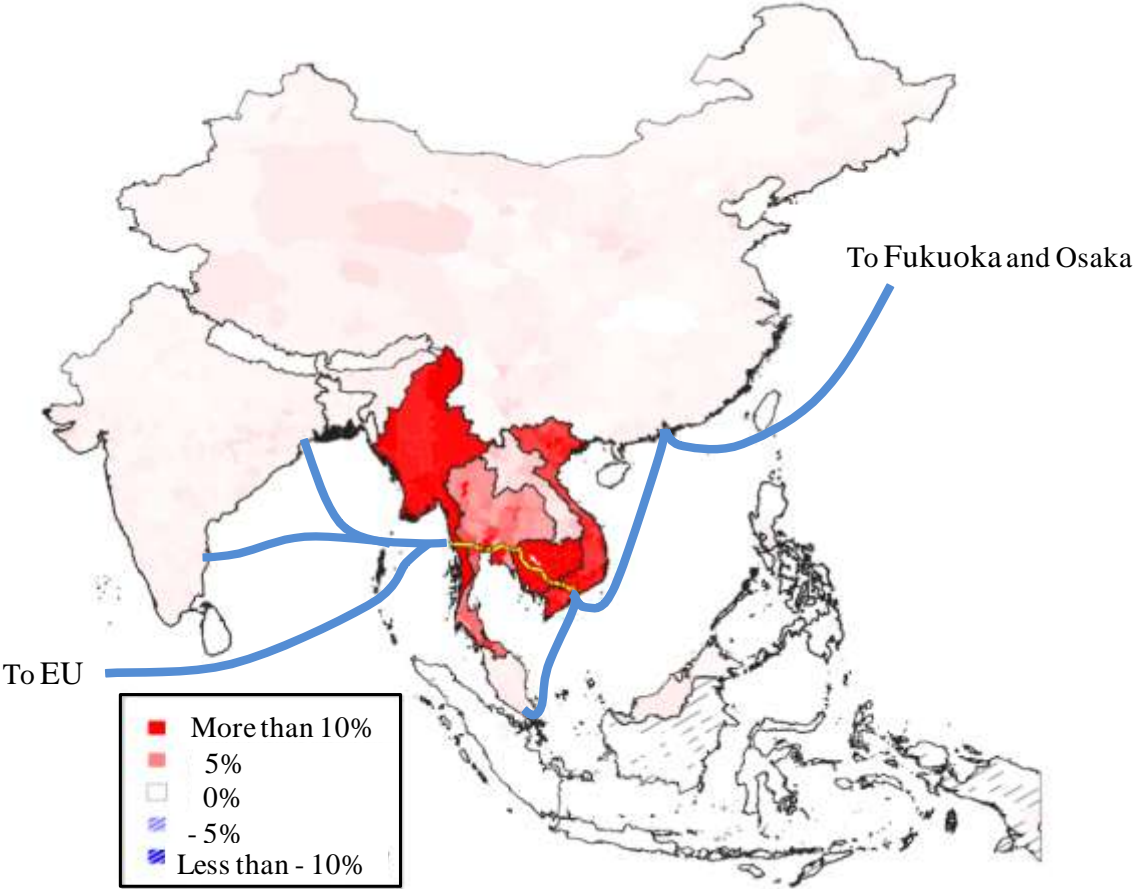
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<sup>16</sup> This research uses the Geographical Simulation Model (GSM) to analyze the earthquake disaster’s long-term effects on the economies of Japan and Asian nations, as well as the effects of the measures taken by Japan after the earthquake. GSM is a model utilizing detailed data of Japanese and Asian industries/population based on theories of spatial economics.

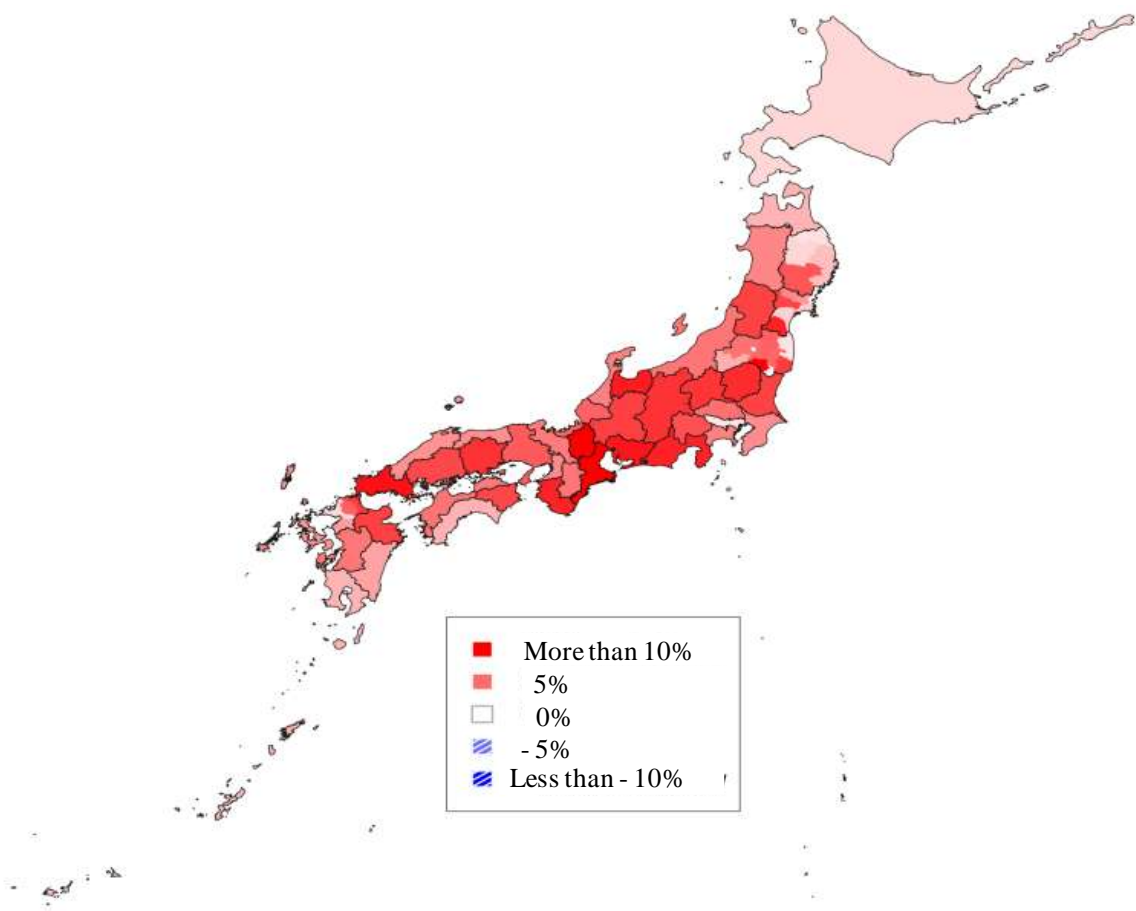
<sup>17</sup> Mekong-India Economic Corridor (MIEC) connects Vietnam, Cambodia, Thailand and Myanmar by land route, and link it to India by sea route.



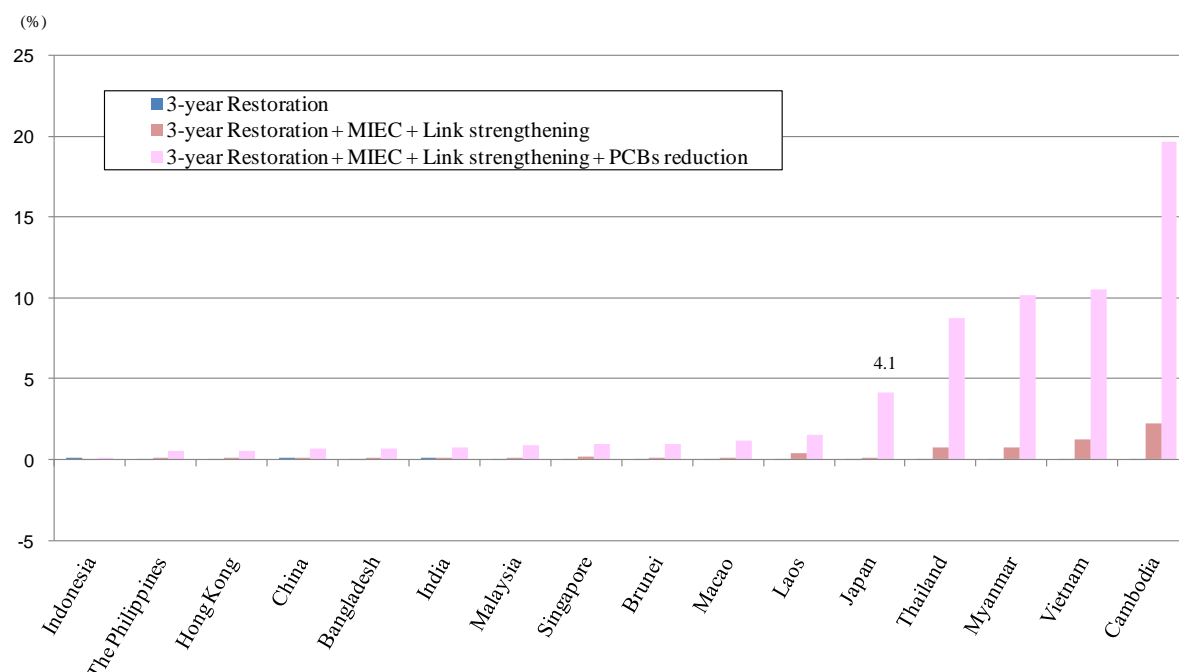
Figures 5-2-1-8 Economic effect to Asia by ERIA simulation (2030, base line ratio)



**Figures 5-2-1-9 Economic effect inside Japan by ERIA simulation (according to each prefecture, base line ratio)**



**Figures 5-2-1-10 Economic effect to each country by ERIA simulation (according to each country, base line ratio)**



Note: Simulation by ERIA (GSM Asia-Japan linkage model)

Source: Compiled from ERIA

### **Column 7 Undertaking of Economic Research Institute for East Asia and ASEAN (ERIA)**

ERIA is an international organization intending to promote the economic unification of East Asia, which is constructed by the 16 member countries of the East Asia summit (10 countries of ASEAN, Japan, China, Korea, India, Australia and New Zealand). ERIA is carrying out research to solve common regional problems and to accomplish an affluent society in Asia as a world growth center and results of the research are submitted as recommendations to policy to the leaders and ministers of the countries.

ERIA started its history in August 2006 at the ASEAN Finance Ministers Meeting when the ministers discussed and proposed the framework of an “East Asian edition of the OECD”. After discussion by leaders and ministers at several meetings, the inaugural meeting was held on June 3, 2008 based on the Chairman’s Statement at the 3rd East Asia Summit meeting in November 2007. Surin Pitsuwan, Secretary General of ASEAN and representatives of 16 East Asian countries attended the meeting and formally declared the establishment of ERIA.

ERIA set the three pillars as its main tasks of policy research projects, i.e. “promotion of East Asia economic unification”, “correction of disparities of economic development within the

region” and “accomplishing of sustainable growth”. In 2010, ERIA proposed an “Overall Asian Development Plan” to comprehensively integrate the infrastructure development and growth strategy and other several formulas to accomplish the sustainable development in the East Asia region. In addition, as ERIA places ASEAN economic unification aiming at construction of the ASEAN Community by 2015 as the most important task for the research, it conducted the research projects including an “ASEAN Connectivity Master Plan”, and the “ASEAN Strategic Traffic Plan” and “ASEAN economic community score cards”.

Other ERIA undertakings include capacity building projects to enhance the policy research capacity of developing countries and symposiums and seminar projects to facilitate exchanges of opinion and information among a wide range of industry, academic and government personnel in the region. As one of important symposium projects, ERIA, with the cooperation of Harvard University and the Vietnam Central Institute of Economy and Management, conducted a symposium with the theme of “The Establishment of a Developing ASEAN Society and a Sustainable Social Security System”, which was held in Hanoi on October 26, 2010. About 250 participants, mainly policymakers from East Asian summit member countries, academic experts and business representatives attended the symposium. The symposium confirmed that ASEAN and the Asia region as a whole play an important role to accelerate both global and regional economic growth. For the capacity building project, ERIA continued to conduct the “ERIA/JENESYS next generation leaders program” as one of “21st Century East Asia Youth Intercommunication Plan (JENESYS programme). The program provides scholarships to students from ASEAN countries who study social and human sciences at designated Japanese universities and graduate schools and it also provides opportunity of internship at ERIA secretariat to those students during their summer holidays.

Moreover, ERIA has been recommending the results of policy research projects to the member countries’ decision-makers including leaders and ministers at the East Asia summit meetings and other opportunities to facilitate the unified policy planning in the East Asian region. For example, ERIA’s contribution to promote connectivity among ASEAN and East Asian countries was highly appreciated by leaders of participated countries at the 5th East Asia Summit Meeting on October 30, 2020. The “Asia Overall Development Plan”, which had been prepared by ERIA under cooperation with the Asian Development Bank and ASEAN Secretariat, was also given high praise. Additionally, the Chairman’s Statement at the 17th ASEAN Summit meeting on October 28 2010 highly praised the ERIA’s contribution to completion of the “Asian Connectivity Master Plan”. ERIA will continue to offer practical recommendations to leaders and ministers of East Asian countries at the East Asia summit and ASEAN summit meetings.

ERIA, as an international research center to recommend specific policies to the East Asian countries’ policy forum such as East Asia Summit, is expected to conduct the implementation of

the “Asia Overall Development Plan” and the “ASEAN Connectivity Master Plan” and to offer practical recommendations to policies also in the future under the close relationship with the ASEAN Secretariat, East Asian countries’ governments and cooperation with research bodies both in and outside the region (Column Figure 7-1).

## Column Figure 7-1 Performance and results of Economic Research Institute for East Asia and ASEAN (ERIA)

### Blueprint for ASEAN community

ASEAN countries, aiming at construction of ASEAN community by 2015, have different culture, social systems and diversity in their development stages and there are various difficulties to connect these countries (difficulty in connectivity). ERIA intellectually contributes to clarify the problems and provides formula to solve them.

Implementation of core work for ASEAN including formulation of strategy and process sheet to construct the ASEAN community (ASEAN Connectivity Master Plan), checking the progress (preparation of AEC score cards) and comparison analysis of various economic partnership agreements

### < Meanings of ASEAN economic community >

China intensively implemented the accession to WTO, easing foreign currency restriction and opening the domestic distribution markets in the 2000s. As a result, the GDP was drastically increased.

US\$1,832 billion in 1999



US\$4,984.7 billion in 2009

When the ASEAN community (single market and production base; economic zone with competitiveness; equal economic development; integration to the world economy) is accomplished by 2015, the GDP in 2020 will be equivalent to that of China.

US\$2,312 billion in 2009



US\$4,514.9 billion in 2020

### Asia Overall Development Plan

The plan is one of the integrated achievements of Economic Research Institute for ASEAN and East Asia (ERIA) research projects. In order to seek the “deepening economic unification” and “correction of development gaps” at the same time, a space design to connect the infrastructure development and industrial location is formulated by using economic theory. In these conditions, the investment effects of specific projects are verified and the projects are prioritized. When those are realized, it may have great benefits to private companies. A part of the research projects has been adopted by President Yudhoyono, Indonesia as a priority measures (Indonesia Economic Development Corridor (IEDC)).

Economic effects of the infrastructure projects in the region are analyzed with the newest model.

(Ten years accumulated economic effects to GDP)

### General list of CADP future projects (long list)

### Business opportunity in the infrastructure development markets

ERIA rated about 700 projects. The investment will be approximately US\$400 billion in total.

Business opportunity by the expanding middle-income group  
GDP per capita in the region will be doubled by 2020.

Approximately US\$4,270 in 2008



Approximately US\$8,540 in 2020

**(b) Efforts with regard to major countries and regions outside the Asia Pacific**

Foremost among Japan's efforts toward economic partnerships with major countries and regions outside the Asia-Pacific is those related to the EU. The EU is Japan's largest trading partner outside the Asia-Pacific region. The total trade value between Japan and the EU is about 13 trillion yen (2010). The EU is Japan's third largest trading partner in the world, while Japan is the EU's sixth largest trading partner. The total outstanding amount of Japanese investment in the EU is about 16 trillion yen (2009), which makes Japan the third largest investment source for the EU. The outstanding amount of the EU investment in Japan totals 7 trillion yen (2009), and it's the second largest for Japan. Within the EU about 3,300 Japanese companies have been operating, creating more than 400,000 jobs. Further strengthening of our economic relations through the Japan-EU Economic Integration Agreement (EIA) will contribute to both sides' economic growth, and also enhance the possibility of strengthening more comprehensive relations including the political and security fields by deepening our interdependence and mutual trust. There's a growing voice among Japanese businesses seeking the realization of the Japan-EU EIA, as is shown by the Japan Business Federation's move to request an early start of the EIA negotiations, against the backdrop of the concern that they would be put in a disadvantageous position, with the EU-South Korea FTA coming into force in July 2011.

At the regular Japan-EU Summit Meeting held in April 2010, the leaders decided to establish a "Joint High-Level Group" to conduct a "joint examination" of the ways to comprehensively strengthen and integrate the Japan-EU economic relationship. The "Joint High-Level Group" has met five times in total at the vice-ministerial level, discussing issues of interest to both sides including tariffs, non-tariff measures, intellectual property rights and government procurement. The Basic Policy on Comprehensive Economic Partnerships, approved by the Cabinet in November 2010, stipulates that the Japanese government will expedite arrangements to enter into negotiations with the EU at an early date, and that for this purpose, it will accelerate efforts to reform its domestic non-tariff measures. And, in December 2010, the two sides reached an agreement on concrete measures with regard to the technical guideline on the Advanced Safety Vehicle, government procurement websites, wood product standards and medical equipment, which were cited as some specific non-tariff measures. Although there exist some negative opinions toward the Japan-EU EIA on the EU side, especially in its industrial sector, the European Council referred to the possibility of the EIA negotiations in its meeting in March 2011, adopting the conclusions which state that "the forthcoming summit must be used to strengthen this relationship and bring forward our common agenda, including through the potential launch of negotiations for a free trade agreement on the basis that Japan is willing to tackle inter alia the issue of non-tariff barriers and restrictions on public procurement."

Following these moves, the leaders of Japan and the EU agreed at their summit meeting in

May 2011 that they would start the process towards EIA negotiations. It was agreed that the two sides would start discussions with a view to defining the scope and level of ambition of negotiations as soon as possible, and that in parallel with this, the European Commission will seek the necessary authorization for the negotiation of the agreements on the basis of a successful scoping.

With regard to the GCC countries, the negotiations were launched in September 2006. This region accounts for more than 70% (2010) of Japanese crude oil imports, while Japanese exports to them total as much as 1.7 trillion yen (2010). Furthermore, there exists a huge demand for large-scale infrastructure development resulting from the population growth, so the governments and private sectors of individual countries have been aggressively engaged in joint sales offensive there. It is important for Japan to build/maintain friendly relationships with GCC countries with a view to expanding trade/investment and ensuring energy security.

### **(c) Efforts with regard to other countries and regions**

The “Basic Policy” stipulates that “taking into account of the progress in the negotiations on the Doha Development Agenda, efforts for regional integration in the Asia Pacific region, and efforts for the strengthening of economic partnerships with major countries, the Government of Japan will work actively to strengthen economic partnerships, including conclusion of EPAs, with other Asian countries, newly emerging powers, and resource-rich countries, based on a comprehensive assessment from economic as well as diplomatic and strategic viewpoint.”

Thus far, we have discussed the EPAs, which are currently under negotiation, discussion or study, based on the classification of the “Basic Policy”.

In order for us to meet the needs of globally-engaged businesses, it is also important to facilitate the smooth utilization of existing EPAs and improve (renegotiate) them apart from making efforts for new ones.

As of May 2011 the number of EPAs which was signed by Japan and is already in force is 11, (Singapore, Mexico, Malaysia, Chile, Thailand, Indonesia, Philippines, Brunei, ASEAN, Switzerland and Vietnam). And the growing utilization of these EPAs by the corporate sector shows that they have reached a stage of utilization/operation. In order for us to help Japanese companies’ international business activities in the EPAs’ utilization/operation phase, we need to make all the more efforts to acknowledge the importance of EPAs’ “life cycles” and improve their quality; specifically (i) steadily implement the EPAs, (ii) improve the business environment so that the government and private sector can actively utilize EPAs and enjoy tariff merits, and (iii) grasp the actual condition of EPAs in order to understand problems and new needs, and improve them.



### **(B) Efforts toward signing the TPP**

The TPP negotiations, which currently involve nine countries (Australia, Brunei, Chile, Malaysia, NZ, Peru, Singapore, the U.S., and Vietnam), have been underway, aiming to reach broad outlines of agreement by the November 2011 APEC summit in Honolulu.

The original agreement between the P4 countries of Brunei, Chile, New Zealand and Singapore entered into force in 2006, and then in 2008 the U.S., Australia, and Peru announced that they would begin negotiations with the P4 countries, and joined them. Further, in March 2010, Vietnam joined them, and formal rounds of TPP negotiations started. (In October 2010, Malaysia joined the talks.) So far (as of April 2011), six formal rounds of TPP negotiations have been held, first in March 2010, followed by those in June 2010, October 2010, December 2010, February 2011, and March 2011, making steady progress. The TPP has been open to accession by countries other than original members, and it's envisaged to be expanded across the whole of the Asia-Pacific region in the future. Among potential pathways leading to the establishment of the Free Trade Area of the Asia-Pacific (FTAAP), the TPP is the only initiative for which the negotiations have been actually launched. At a breakfast meeting for the TPP member nations held on May 19, 2011 on the sidelines of the APEC Trade Ministers' Meeting, the ministers agreed that they would try to reach the broad outlines of an agreement on the TPP by the APEC Leaders' Meeting due to be held in November 2011, and that they continue to work bilaterally with interested countries and to consider the membership of any APEC members if and when they are ready to meet the high standards of the TPP agreement. Member countries have already begun to propose draft texts for various fields of the TPP<sup>18</sup>, promoting substantive negotiations on a request/offer basis with regard to the access to each others' markets for various goods, investment, services, and government procurement, among others (see Figure 5-2-1-11).

### **Figure 5-2-1-11 Process of TPP Agreement negotiations: progress steadily**

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<sup>18</sup> Based on such information as Singaporean government's announcement after the sixth round of TPP negotiations on March 27-April 11, 2011.



Aiming at the extensive rough agreement:  
November, 2011 APEC leaders conference (Hawaii)



Source: Ministry of Economy, Trade and Industry.

Among the areas discussed in the TPP negotiations are: Market access (industrial products, textiles/clothing and agriculture), rules of origin, trade facilitation, SPS (sanitary/phytosanitary measures), TBT (technical barriers to trade), trade remedies (safeguards and others), government procurement, intellectual property, competition policy, services (cross-border flows of services, financial services, telecommunications and the movement of business people), e-commerce, investment, environment, labor, institutional issues, dispute settlement, cooperation, and “cross-cutting issues” that cut across the boundaries of various fields<sup>19</sup>. They are trying to craft a comprehensive, high-quality “21st-century” agreement, characterized by maximum tariff elimination and a broader regional membership covering both developed and developing countries, with the aim of making it a building block for making common trade and investment rules for the Asia Pacific as a whole. Meanwhile, the “cross-cutting issues”, which have not been covered in more traditional FTAs/EPAs, deal with regulatory coherence, competitiveness (including the question of supply chain connectivity) and support for small and medium-sized enterprises, among others. Its main feature is to enable discussants to cut across the boundaries of various individual fields such as rules of origin, investment and services, with

<sup>19</sup> Some call them 24 working groups/fields by adding the chief negotiators' meeting to them. But it is not yet determined how to calculate them, and differs depending on the negotiation meetings. There is no guarantee that the agreement's final structure will be as framed here.

the aim of establishing a more liberalized environment for trade and investment by eliminating regulatory differences and solving various supply chain-related problems faced by companies which invest and supply goods/services within the Asia-Pacific region.<sup>20</sup>

The U.S. and other countries joining the TPP negotiations aim not only to achieve high levels of tariff elimination but also to make new rules to help solve various problems faced by the companies doing business within the Asia Pacific, the growth center of the global economy. For example, while many of the countries participating in the TPP talks are not a party to the WTO Government Procurement Agreement, in order to ensure the fair treatment of signatory countries' companies and their products in the markets of TPP participants the TPP negotiators have been discussing adoption of government procurement rules at the WTO level. With regard to the protection of intellectual property, discussions have been underway to strengthen a framework to prevent the proliferation of counterfeit goods and pirated copyright protected works. And, with a view to facilitating the businesses of globally operating companies, discussions have been underway to establish regional rules covering entire supply chains, including those to simplify customs procedures and improve logistic services. They aim to promote a rulemaking in a manner considerate of small and medium-sized enterprises for whom the burden of trade-related information gathering and customs procedures is heavier than for big companies. In the fields of investment and services, discussions have been underway to enhance the transparency of restrictions on foreign investment and to ease/eliminate the regulations concerning investment and services, with the aim of facilitating companies' overseas operations. With regard to the fields of labor and environment, they are discussing prohibiting member countries to ease labor and environmental regulations for the purpose of trade/investment promotion, as well as the issue of compliance with multilateral rules such as those of the ILO.

The TPP is still under negotiation, so we cannot predict for sure what kind of rules would be finalized. But we can guess that they would make common rules covering a broad region as a whole, which would be unattainable if they are merely piling up bilateral EPAs.

Concerning the TPP, the “Basic Policy” says that “it is necessary to act through gathering further information, and Japan, while moving expeditiously to improve domestic environment, will commence consultations with the TPP member countries.” In December 2010 we started gathering information from each of the nine TPP member countries, and by February 2011 we have heard from all of them. We will continue our efforts for information gathering/analysis with regard to the TPP.

## **In conclusion**

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<sup>20</sup> For details, see the Ministry of Economy, Trade and Industry, Japan, FUKOUSEI BOUEKI HOUKOKUSHO 2011 edition, pp.495-49

The Guideline on Policy Promotion, adopted after the Great East Japan Earthquake, states that “the timing of a decision on whether to join negotiations for the Trans-Pacific Partnership (TPP) Agreement will be considered from an overall perspective.” It was decided that the Minister-level Meeting on FTAAP/EPA would consider how to proceed with the question of comprehensive economic partnerships, including the timing of a decision on the TPP. Amid growing concerns about the hollowing-out of industry following the Great East Japan Earthquake, we need to maintain the basic thinking of the “Basic Policy”, and pursue both reconstruction of East Japan and revitalization of the Japanese economy as a whole in an integrated manner.

## **2. Improvement of the business environment by investment agreements and the development of international standards**

For Japanese companies to operate globally in Asia and other regions, cross-border investment, trade and improved business environment in other countries are important. For the improvement of the business environment it's necessary to tackle various issues, such as the improvement of investment rules, development of industrial infrastructure, simplification/facilitation of administrative procedures and protection of intellectual property rights. Japan's economic EPAs set a framework in which the government and the private sector discuss the issues of business environment in a comprehensive manner. Apart from the EPAs, other types of bilateral agreements and international standardization are also useful in coping with these issues. Among such bilateral arrangements are investment treaties, tax treaties and social security agreements. Here, we take up (1) bilateral investment agreements, (2) tax treaties, and (3) social security agreements, and present an overview of their roles and current situations. We also discuss the importance of improving the business environment for promoting overseas business operations.

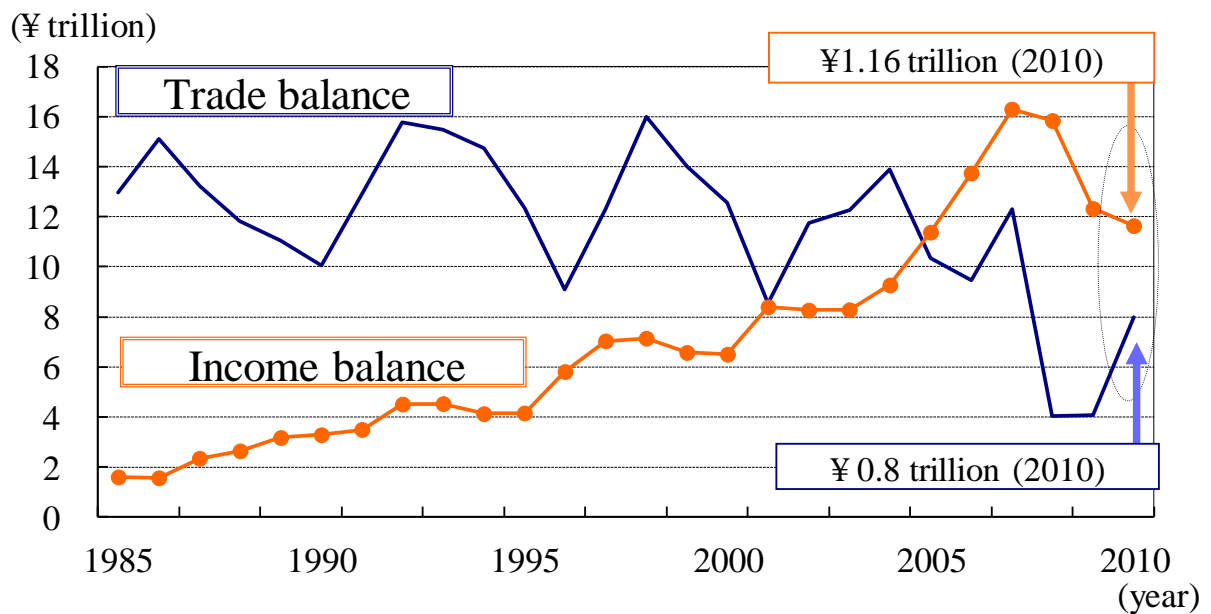
### **(1) Bilateral Investment Agreements**

#### **(A) Trends of Japan's direct investment abroad**

The world's direct investment abroad expanded rapidly since the 1980s, playing an important role as a driver of the world's economic growth, together with trade. According to the World Investment Report 2010 issued by the United Nations Conference on Trade and Development (UNCTAD), in 1990 foreign direct investment as a percentage of GDP was 8.5% in the value of direct investment abroad and 9.1% in the value of inward direct investment, but in 2009, they grew to 33.3% and 30.7%, respectively. Japan's international balance of payments indicates that Japan has constantly recorded a surplus in balance of trade since the latter half of the 1980s and the volume of overseas investment gradually expanded. In recent years, income receivable generated by such overseas investment has increased, with the surplus in the balance of income

reaching about 12.3 trillion yen in 2009. It is much larger than the surplus in the balance of trade which was about 4.0 trillion yen in the same year. The surplus in the balance of income has exceeded that in the balance of trade for the fifth consecutive year (see Figure 5-2-2-1). In 2009, the return on direct investment amounted to 4.2806 trillion yen (preliminary estimate), showing steady performance.

**Figure 5-2-2-1 Change of Japan's trade balance and income balance**



Source: Compiled from “Balance of Payments Statistics”, MOF / BOJ

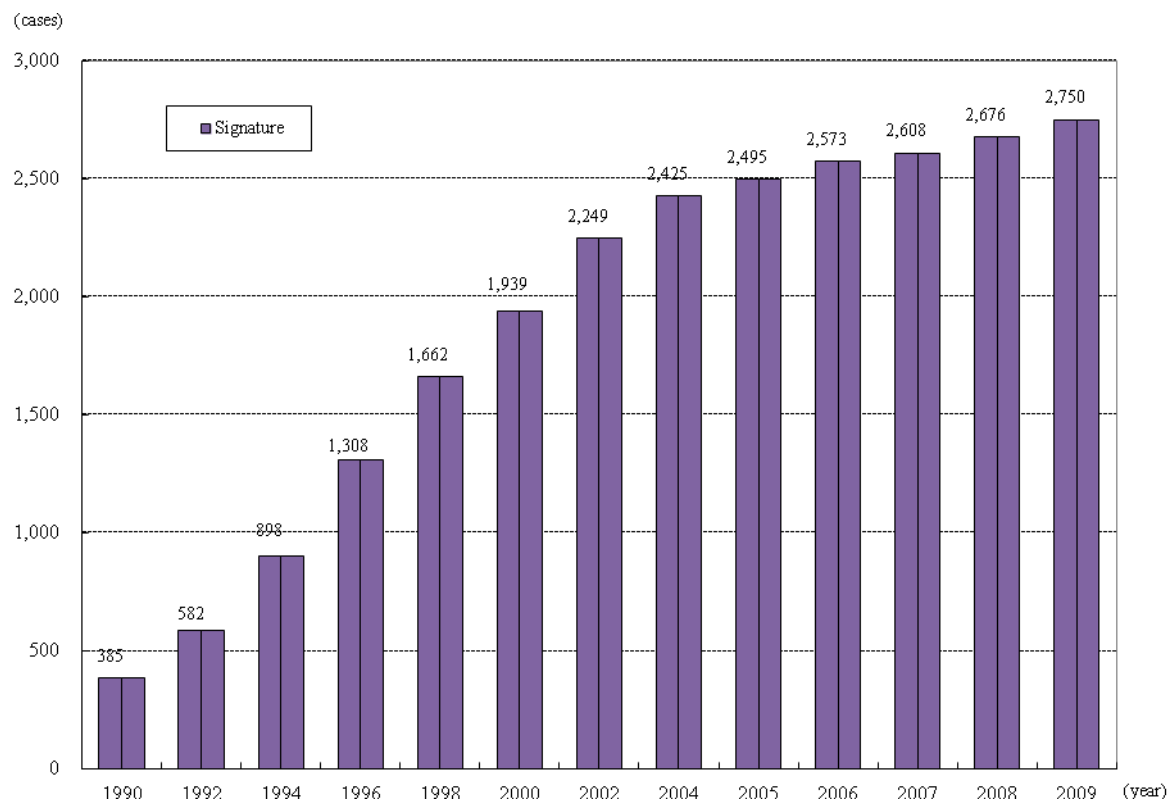
### **(B) Signing of bilateral investment treaties around the world**

In light of the expansion of direct investment abroad, countries have signed bilateral investment treaties in order to protect investors and their invested assets from various risks, such as discriminatory treatment or expropriation (including nationalization) in invested countries.

The number of bilateral investment treaties in the world has increased considerably in recent years, reaching 2,750 as of 2009 (see Figure 5-2-2-2). While countries like Germany China, the UK and France have concluded around 100 bilateral investment treaties, Japan has concluded merely 26 including economic partnership agreements<sup>21</sup> (see Table 5-2-2-3).

<sup>21</sup> As of May 2011.

**Figure 5-2-2-2 Change of the number of bilateral investment agreements in the world**



Source: Compiled from "IIA MONITOR No.3 (2009)", UNCTAD

**Table 5-2-2-3 Conditions of conclusion of Japan's bilateral investment-related agreements.**

Counterparty country (including region) of concluded agreement	Signed	Enacted
Egypt	January 28, 1977	January 14, 1978
Sri Lanka	March 1, 1982	August 7, 1982
China	August 2, 1988	May 14, 1989
Turkey	February 12, 1992	March 12, 1993
Hong Kong	May 15, 1997	June 18, 1997
Pakistan	March 10, 1998	May 29, 2002
Bangladesh	November 10, 1998	August 25, 1999
Russia	November 13, 1998	May 27, 2000
Mongolia	February 15, 2001	March 24, 2002
Singapore (Economic Partnership Agreement)	January 13, 2002	November 30, 2002
South Korea	March 22, 2002	January 1, 2003
Vietnam	November 14, 2003	December 19, 2004
Mexico (Economic Partnership Agreement)	September 14, 2004	September 17, 2005
Malaysia (Economic Partnership Agreement)	December 13, 2005	July 13, 2006
Philippines (Economic Partnership Agreement)	September 9, 2006	December 11, 2008
Chile (Economic Partnership Agreement)	March 27, 2007	September 3, 2007
Thailand (Economic Partnership Agreement)	April 3, 2007	November 1, 2007
Cambodia	June 14, 2007	July 31, 2008
Brunei (Economic Partnership Agreement)	June 18, 2007	July 31, 2008
Indonesia (Economic Partnership Agreement)	August 20, 2007	July 1, 2008
Laos	January 16, 2008	August 3, 2008
Uzbekistan	August 15, 2008	September 24, 2009
Peru	November 21, 2008	December 10, 2009
Vietnam (Economic Partnership Agreement)*1	December 25, 2008	October 1, 2009
Switzerland (Economic Partnership Agreement)	February 19, 2009	September 1, 2009
India (Economic Partnership Agreement)	February 16, 2011	Undecided
Papua New Guinea	April 26, 2011	Undecided
Peru (Economic Partnership Agreement)*2	May 31, 2011	Undecided

**Notes**

1: Contents of Japan-Vietnam Investment Agreement taken effect on Dec. 19, 2004 is included.

2: Contents of Japan-Peru Investment Agreement taken effect on Dec. 10, 2009 is included.

3: Compiled from the information as of Apr. 2011.

Source: Compiled by METI

Many of the bilateral investment treaties provide for dispute settlement procedures in cases where investors (companies) suffer disadvantages. When there is no bilateral investment treaty equipped with such dispute settlement procedures, it is not easy for an investor to have the legal



grounds to appeal to an investment arbitration body about remedying them. According to the UNCTAD, the number of cases of arbitration of investor-state disputes arising from investment treaties (the number of filed arbitrations to the arbitration body) remained at 14 in cumulative total until 1998<sup>22</sup>, since the first case<sup>23</sup> was filed in 1987, but such cases have increased dramatically since the latter half of the 1990s<sup>24</sup>, adding up to a cumulative total of 390 as of March 2011. On the other hand, the number of Japanese-owned companies using the investment arbitration system is only one, which had been filed by an overseas subsidiary<sup>25</sup>.

### **(C) Bilateral investment treaties as a tool to promote protection/facilitation of investment**

Bilateral investment treaties have long been concluded with the aim of protecting investors from such risks as expropriation of invested assets and arbitrary interpretation of laws by the host countries. These are called “investment protection treaties”, and their main features are national treatment/most-favored nation treatment, requirements for expropriation/formula of compensation, free transfer of money, dispute settlement procedures between contracting countries, and dispute settlement between investors and host countries. In addition to such framework to protect invested assets, the 1990s saw an emergence of a new type of bilateral investment treaty (investment protection/liberalization treaty) that provides for national treatment/MFN treatment at the time of the investment approval, ban on performance requirements<sup>26</sup>, prohibition of tightening restrictions on foreign investment, the obligation of progressive liberalization, and the guarantee of transparency (disclosure of laws and regulations, obligation to reply to questions from a partner country, etc.) (see Table 5-2-2-4)<sup>27</sup>.

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<sup>22</sup> The case of Asian Agricultural Products Limited v. Democratic Socialist Republic of Sri Lanka (ICSID Case No.ARB/87/3)

<sup>23</sup> UNCTAD (2005) “INVESTOR-STATE DISPUTES ARISING FROM INVESTMENT TREATIES:A REVIEW”

<sup>24</sup> It is believed that it was the 1996 “Ethyl incident” which aroused broad interest in investment arbitration. (It was the case in which the U.S. Ethyl Corporation filed a suit against a Canadian environmental and public health measure, arguing that it’s considered expropriation of its assets under the rules of NAFTA, and Canada paid compensation to settle the case.)

<sup>25</sup> This was a case over an action taken by the Czech government against a Czech bank acquired by a London subsidiary of a Japanese securities company through a “paper company” in the Netherlands in 1998. The case was filed with the United Nations Commission on International Trade Law (UNCITRAL) under the bilateral investment agreement between the Czech Republic and the Netherlands.

<sup>26</sup> Specific requirements imposed as a condition for allowing investment, such as satisfying certain local content ratios and exporting certain ratios of goods manufactured.

<sup>27</sup> Among the major ones are the Investment chapter of the NAFTA. The Investment chapters of Japan’s bilateral EPAs as well as Japan’s bilateral investment agreements with S. Korea, Vietnam, Cambodia, Laos, Uzbekistan and Peru are also of this type.

**Table 5-2-2-4 Merit of conclusion of investment agreement**

1. Protection of the investment asset & fair services for investors
(1) Business licenses once issued aren't canceled later.
(2) Business assets are neither expropriated nor nationalized.
(3) Business termination due to strengthened regulation ("indirect expropriation") is prevented
(4) Investment contracts that concession contract concluded with the counterpart government are observed (umbrella clause).
(5) Freedom of remittance to Japan is secured.
2. Between firms (foreign firms) excluding local capitals, discriminatory treatment is banned. (Most favored nation treatment (MFN))
3. Between local capital firms, discriminatory treatment is banned. (National Treatment (NT))
4. Duty to offer investors and investment assets fair and equitable treatment. (FET: Fair and Equitable Treatment)
5. Depending on agreement, following investment approval conditions are prohibited. (Prohibition of performance requirement (PR))
(1) Requirement to export goods and services at a certain ratio and level.
(2) Requirement to achieve local procurement at a certain ratio and level.
(3) Requirement to purchase, use of prioritized local goods and services.
(4) Requirement to connect the amount and value of imports with the amount and value of exports, or acquiring of foreign currency.
(5) Requirement to connect the amount and value of domestic sales of produced goods and services with the amount and value of exports, or acquiring of foreign currency.
(6) Requirement to restrict exports or sales for exports.
(7) Requirement of a certain nationality for board members, managers and so on.
(8) Requirement of technology transfer to local capital partners.
(9) Requirement to place headquarters of a certain region.
(10) Requirement to employ a certain ratio or certain number of local persons.
(11) Requirement to inject R&D budget at certain level.
(12) Requirement to supply products exclusively at certain region. (Not to establish other supply bases in other countries)

Notes: When the counterpart country violates these obligations, investors can appeal for international arbitration against the state.

Source: Compiled by METI

#### **(D) Approaches to bilateral investment treaties**

If any country in which a Japanese company is operating or plans to operate is relatively closed to foreign capital, or has an insufficient legal framework (laws are often changed or transparency is poor, etc.), it is necessary to conclude an investment treaty with such a country. At the same time, the human resources the government can use for negotiating bilateral investment treaties are limited. Therefore, when concluding a bilateral investment treaty, it is necessary to prioritize partner countries/regions with the main aim of meeting the real needs, and proceed with negotiations with speed and flexibility.

Possible candidates as contracting partners of bilateral investment treaties are the countries that satisfy the following conditions, apart from their investment environment being considered

insecure: first, countries possessing or likely to receive a certain level of Japanese investment stock; second, resource-rich countries such as those in the Middle East and former Soviet Union; and finally, those who could serve as Japanese companies' regional headquarters for their operations in South America, Africa, etc. Another important factor to consider is whether or not the country has a positive attitude toward concluding such treaty.

And from the perspective of protecting/promoting investment, it is also important to utilize policy support tools, such as JETRO, NEXI, JICA, and JBIC, in addition to promoting the negotiations for investment treaties<sup>28</sup>. The Council for the External Investment Strategy, established in November 2008 with the involvement of these organizations and the private sector, has held three plenary meetings and seven liaison meetings so far, discussing the candidates for negotiating new investment treaties as well as the effective utilization of related tools.

## **(2) Tax treaties**

### **(A) Role tax treaties and an overview of the current situation**

Tax treaties are designed to clarify relations of two countries in regards to taxation on investment and economic activities in order to deal with the issue of international dual taxation. Furthermore, the conclusion of a treaty establishes a cooperative legal framework between the tax authorities of two contracting states for mutual consultations and exchanges of information on taxpayers, thus helping solve conflicts on taxation and prevent tax evasion. Treaties such as these are expected to ensure the legal stability of taxation on corporations and to further promote investment and economic exchanges.

Japan has concluded 48 tax treaties thus far, which are applied to 59 countries/regions (see Table 5-2-2-5).

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<sup>28</sup> “On the Improvement of Japan's Global Investment Environment - Toward the Creation of a Legal Framework for Japanese Foreign Investment” by Nippon Keidanren dated April 15, 2008 and the “Petition for the Acceleration of the Conclusion of Investment Agreements” by the Japan Foreign Trade Council, Inc. dated March 19, 2008 call for an early improvement of the situation with regard to investment treaties. Upon such strong call from the business community, the Japanese government decided on the “strategic utilization of bilateral investment treaties” in 2008, and the “New Growth Strategy: Blueprint for Revitalizing Japan”, announced in 2010, also discusses the need to promote signing of investment treaties. The Nippon Keidanren’s “Proposals for Japan's Trade Strategy”, dated April 19, 2011, also requests for the improvement of the situation with regard to investment treaties.

**Table 5-2-2-5 List of counterpart countries and regions of conclusion of tax convention for Japan**

<b>List of countries/regions with which Japan has concluded tax treaties (48 treaties applied to 59 countries/As of April 2011)</b>			
<b>(East, Southeast Asia)</b>	<b>(Middle East)</b>	<b>(Eastern Europe, Central Asia)</b>	<b>(Europe)</b>
Indonesia	Israel	Azerbaijan	Ireland
South Korea	Egypt	Moldova	U.K.
Malaysia	Turkey	Ukraine	Italy
Singapore		Kyrgyzstan	Austria
Thailand	<b>(Africa)</b>	Georgia	Finland
China	Zambia	Tajikistan	The Netherlands
The Philippines	South Africa	Turkmenistan	Switzerland
Vietnam		Belarus	Sweden
Brunei	<b>(North America)</b>	Uzbekistan	Luxembourg
	U.S.A.	Kazakhstan	Spain
<b>&lt;South Asia&gt;</b>	Canada	Russia	Denmark
India		Armenia	Germany
Sri Lanka	<b>(Central and South America/ Caribbean region)</b>	Slovakia	Norway
Pakistan		Czech	France
Bangladesh	Brazil	Hungary	Belgium
	Mexico	Bulgaria	<b>(Oceania)</b>
	Bermuda	Poland	Australia
		Romania	New Zealand
			Fiji

Source: Compiled from HP of MOF

### **(B) Recent conclusion/revision of tax treaties and tasks ahead**

In recent years, Japan has signed tax treaties with the resource-rich countries of the Middle East and other regions one after another, while revising those with developed countries. And, the new Japan-Netherlands tax treaty, signed in August 2010, includes an arbitration clause, the first of its kind for Japan. Also in September 2010, the tax authorities of the two countries agreed on an implementing arrangement regarding the arbitration procedure. Furthermore, the Japan-Hong Kong tax treaty, signed in November of the same year, also includes an arbitration provision. The arbitration system is designed to facilitate and improve the effectiveness of tax authorities' mutual consultations. Introduction of arbitration systems is expected to help alleviate the issue of prolonged consultations and ensure that double taxation does not occur. It is an effective tool to mitigate the risks facing taxpayers, so it is necessary to promote the introduction of arbitration systems for our tax treaties from now on.

There is a growing voice from the business community with regard to the tax matters related to emerging countries such as those in Latin America and Asia. Among the major tasks ahead are

reduction in the source-country taxation of investment income (dividends, interest, royalties), improvement with regard to provisions related to the transfer pricing taxation, and introduction of arbitration systems. In general, emerging nations tend to be hesitant about measures such as reducing the source-country taxation of investment income, because of their desire to secure as much tax revenue as possible. It's important for us to talk to them effectively so that they would agree to start negotiations for revising the bilateral tax treaties (see Table 5-2-2-6).

**Table 5-2-2-6 Process and present conditions after U.S.-Japan tax convention**

(As of Apr. 2011)		
◇ Signed		
Nov. 2003	U.S.-Japan Tax Convention	(Taken effect in 2004)
Feb. 2006	Japan-UK Tax Convention	(Taken effect in 2006)
Feb. 2006	Japan-India Tax Convention	(Taken effect in 2006)
Dec. 2006	Japan-Philippines Tax Convention	(Taken effect in 2008)
Jan. 2007	Japan-France Tax Convention	(Taken effect in 2007)
Jan. 2008	Japan-Pakistan Tax Convention	(Taken effect in 2008)
Jan. 2008	Japan-Australia Tax Convention	(Taken effect in 2008)
Dec. 2008	Japan-Kazakhstan Tax Convention	(Taken effect in 2009)
Jan. 2009	Japan-Brunei Tax Agreement	(Taken effect in 2009)
Jan. 2010	Japan-Luxembourg Tax Convention	(Yet taken effect)
Jan. 2010	Japan-Belgium Tax Convention	(Yet taken effect)
Feb. 2010	Japan-Bermuda Tax Agreement	(Taken effect in 2010)
Feb. 2010	Japan-Singapore Tax Agreement	(Taken effect in 2010)
Feb. 2010	Japan-Malaysia Tax Convention	(Taken effect in 2010)
Feb. 2010	Japan-Kuwait Tax Convention	(Yet taken effect)
Nov. 2010	Japan-Saudi Arabia Tax Convention	(Yet taken effect)
Nov. 2010	Japan-Hong Kong Tax Agreement	(Yet taken effect)
Aug. 2010	Japan-Netherlands Tax Convention	(Yet taken effect)
May. 2010	Japan-Switzerland Tax Convention	(Yet taken effect)
Jan. 2011	Japan-Bahamas Tax Agreement	(Yet taken effect)
Feb. 2011	Japan-Cayman Tax Agreement	(Yet taken effect)
◇ Basic agreement		
Mar. 2011	Japan-Mann Tax Agreement	[New]
Jan. 2011	Japan-Guernsey Tax Agreement	[New]
Mar. 2011	Japan-Jersey Tax Agreement	

◇Country now under formal negotiation

The United Arab Emirates

[New]

Source: Compiled from HP of MOF

### **(3) Social Security Agreement**

#### **(A) Its roles and the status of agreements**

Amid the expansion of Japanese companies' overseas operations and increasingly active international exchanges of people, there have arisen some cases in which Japanese nationals overseas and foreign expatriates in Japan may face the question of (1) dual coverage by and payment for their social security such as public pension systems, and (2) not being able to receive social security benefits because the period of contribution is not long enough. Social security agreements are designed to help avoid such problems. And also, by relieving companies of the burden of duplicate pension premium payments, these agreements are expected to enhance the competitiveness of Japanese corporations, while contributing to the promotion of inward FDI by foreign companies as well.

With a view to solving the questions of dual payment and lapsed contributions, the social security agreements, signed by Japan so far, provide for the following, among other things.

#### **(a) Application adjustment**

Those temporarily dispatched employees for a period of five years or less shall in principle enroll only in the social security system of the country from which the employee is dispatched. If he /she is dispatched for more than 5 years, then he/she is covered by the other country's social security system exclusively.

#### **(b) Totalization of coverage periods**

When a person is enrolled in social security systems of two countries which have social security agreement with each other, his/her enrollment periods of both countries can be totalized. And, if the totalized period exceeds a certain enrollment period necessary for the qualification to receive social security benefits, then the person can receive the pension in accordance with the enrollment record.

And, because the social security system is different from country to country, the specifics of the social security agreements are also different from each other. When a company dispatches its employee to some foreign country, they need to examine the bilateral agreement as well as the country's domestic rules closely.

Japan's first social security agreement, with Germany, went into effect in 2000. As of June 2011, agreements with 12 countries are in effect, and in addition, those with three countries have been signed. Currently, we have been engaged in intergovernmental negotiations as well as

preliminary talks with several countries (see Table 3-2-3-23). Meanwhile, the domestic legal infrastructure was improved in 2007, facilitating the implementation of the social security agreements within Japan.<sup>29</sup>

When selecting/prioritizing potential partners for negotiating social security agreement, the Japanese government has considered following points in a comprehensive manner: 1. the general level of social insurance premiums for the social security system of the country; 2. the burdens shouldered by Japanese residents and companies in the country with regard to the payment of social insurance premiums; 3. requests from the Japanese business community; 4. bilateral relations; and 5. differences in the social security systems between Japan and the country. Thus, many of the partners in our social security agreements have been developed Western countries with mature social security systems where the amounts of duplicate social insurance contributions were substantial. On the other hand, against the background of the expanding economic relations between Japan and emerging nations, we are also promoting social security agreements with them. For example, the agreement with Brazil was signed in July 2010. And we have been discussing eventual conclusion of social security agreements with India and China as well (see Table 5-2-2-7).

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<sup>29</sup> Legislation of the Act on Special Provisions for the Employees' Pension Insurance Act, etc. Incidental to Enforcement of International Social Security Agreements. This establishment of a blanket provision, in place of special implementation provisions enacted with each country-specific agreement, has made it easier to conduct negotiations with multiple countries at the same time. See “SEISAKU REPORT: SHAKAI HOSHOU KYOUTEI NO TEIKETSU O SUSUMETE IMASU” (Ministry of Health, Labour and Welfare) at <http://www.mhlw.go.jp/seisaku/10.html>.

**Table 5-2-2-7 Japanese conditions of social security agreement**

<b>Agreement that already took effect</b>				
Counterparty	Date effective	Social security system with the risk of double payment		Calculation of total period of insurance
		Japan	Counterparty county	
Germany	2000/2/1	• Public pension system	• Public pension system	Yes
United Kingdom	2001/2/1		• Public employment insurance system	No
South Korea	2005/4/1	• Public pension system	• Public pension system	No
United States	2005/10/1	• Public pension system • Public medical insurance system	• Social Security system (Public Pension system) • Public health insurance system (Medicare)	Yes
Belgium	2007/1/1		• Public pension system • Public health care system • Public labor insurance system • Public employment insurance	Yes
France	2007/6/1		• Public pension system • Public medical insurance system • Public labor insurance system	Yes
Canada	2008/3/1		• Public pension system (Except Quebec pension system)	Yes
Australia	2009/1/1	• Public pension system	• Retirement pension security system	Yes
Netherlands	2009/3/1		• Public pension system • Public medical insurance system	Yes
Czech Republic	2009/6/1	• Public medical insurance	• Employment insurance system	Yes
Spain	2010/12/1	• Public pension system	• Public pension system	Yes
Ireland	2010/12/1	• Public pension system	• Public pension system	Yes
<b>Agreement that already took effect</b>				
Counterparty (Date signed) Italy (Feb. 2009), Brazil (July,2010), Switzerland (Oct. 2010)				
<b>Under bilateral negotiation</b>				
Counterparty (Date initiated) Hungary (Nov, 2009), Luxemburg (May, 2010)				
<b>Preliminary negotiation between relevant authority etc.</b>				
Counterparty (Date initiated) Sweden (March, 2008), Philippines (Aug, 2009), Slovakia (Sept, 2010), Austria (Oct. 2010), India (Jan. 2011), China (May, 2011)*				



Notes: Inter-governmental opinion exchange meeting was held

Source: Ministry of Health, Labour and Welfare Website as in June 1, 2011

### **3. World Trade Organization (WTO) as a multidirectional free trade system. -- 3 roles and problems from now on --**

Since the global economic crisis ignited by the Lehman shock occurred in Sept. 2008, political pressure for introduction of protectionist measures that seemed to be aimed at supporting domestic industry and securing employment rose in each country<sup>30</sup>. When there was the country that adopted protectionism due to such domestic pressure, it was concerned that that could invite a chain reaction of retaliations by other countries, protectionism spread over the whole world, and adversely affect global trade and economy. Being affected by the economic recession, global trade declined by 12.2% in 2009.

However, according to the report of World Trade Organization (WTO) on Apr. 7, 2011, the global trade increased by 14.5% in 2010, and be forecasted to increase by 6.5% in 2011. In addition, the Trade Policy Review in each state by WTO in several times pointed out that each country resisted protectionism pressure (refer to “(1) surveillance of trade policy in each state”).

This shows that the WTO as a multidirectional free trade system restrains protectionism, and works to maintain free trade system effectively. Member countries must maintain and strengthen that in the future.

It can be thought that there are roughly three roles the WTO takes to contribute to international trade – (i) Monitoring the trade policy in each country, (ii) The Doha Round negotiations for further trade liberalization, (iii) Execution of the current rules. We are going to survey the three roles as follows.

#### **(1) Monitoring the trade policy in each country**

To begin with, the multidirectional free trade system was elaborated as a plan as a breakwater for protectionism due to the reflection that protectionism spread in the 1930s, and each country adopted a block economy which contributed to the cause World War II<sup>31</sup>. Therefore one of the important roles that the WTO takes now is monitoring the trade policy in each country.

In response to the request by leaders in the G20 London summit on Apr. 2, 2009, the WTO continues the monitoring of trade policy in each country and the quarterly report that started at the end of 2008<sup>32</sup>. Following the report dated Jan. 26, 2009 (the working document shared only by member countries) and the report dated Apr. 20 (the document shared by member countries on Mar. 26 that was publicly released after the London Summit with approval from WTO member countries), the third report was released on Jul. 15. In addition, the three institutions of the WTO, OECD and UNCTAD jointly reported the trade and investment measures in each G20

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<sup>30</sup> Refer to Section 3, Chapter 2 in 2009 White Paper on International Economy and Trade.

<sup>31</sup> Refer to Section 3, Chapter 2 in 2009 White Paper on International Economy and Trade.

<sup>32</sup> WTO established "Task force" to consider influence of financial crisis in the Director-General Secretariat on Oct. 14th, 2008 in order to monitor and report the trade policy in each country as a part of the countermeasures to the economic crisis.

member country on Sept. 14th.

In the G20 Pittsburgh Summit held Sept. 24-25 the G20 leaders reconfirmed the promise of not to fall into protectionism committed in Washington and London, and welcomed the above mentioned report by the the institutions released on Sept. 14, and called for its continuous report quarterly.

After that, WTO Director-General issued the yearly report that summarized the trends regarding the international trade environment for one year from Oct. 2008 to Oct. 2009 on Nov. 18 afterwards. The yearly report summarized about trade restrictions and trade promotion measures (such as tariff reduction and abolition of trade bailout measures), and economic stimulating and bailout measures for financial institutions that each WTO member country and observer country introduced.

In the 7th WTO regular ministerial meeting held right after the release of the yearly report, the monitoring activity in trade measures in each country by WTO got an generally high evaluation from the attending ministers, and its importance was confirmed in the chairman's summary statement, saying "active arguments were carried out about a functional enhancement of WTO, and there are many indications that monitoring and analysis are important for protectionism prevention".

In 2010, the thre institutions of the WTO, OECD and UNCTAD jointly reported about trade and investment measures in each G20 country three times of Nov. 4, Jun. 14 and Mar. 8. In addition, the WTO Director-General issued the yearly report<sup>33</sup> which summarized trends regarding the international trade environment during a period from Nov. 2009 to mid. of Oct. 2010, then in response to that, he confirmed the importance of monitoring activities with attendance of TPRB member countries on Nov. 18.

In addition, in the G20 Seoul summit held from Nov. 11th to 12th in the year, G20 leaders required continuous monitoring of the conditions and semiannual public reports for the WTO, OECD and UNCTAD<sup>34</sup>. In addition, in the APEC ministerial meeting held from Nov. 10, 2010 to 11st, in the "Statement on the WTO Doha Development Agenda Negotiations and Resisting Protectionism"<sup>35</sup>, it was shown to support the monitoring activities of the international organizations concerned continuously, including the WTO, and to cooperate with these entities.

## **(2) The Doha Round negotiations (promotion of multidirectional negotiations)**

### **(A) Hitherto development of GATT/WTO**

Contracting countries of the GATT established in 1948 executed multidirectional negotiations

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<sup>33</sup> Refer to 5. [1] in Section 3, Chapter 1 in 2009 White Paper on International Economy and Trade.

<sup>34</sup> Refer to G20 Seoul Summit document.

<sup>35</sup> Refer to the "Statement on the WTO Doha Development Agenda Negotiations and Resisting Protectionism".

eight times in the past, and have intended to restrict protectionism and develop free and fair trade rules. Following the several rounds of negotiations<sup>36</sup>, duty reduction was gradually realized, and the trade-related rules except duty were also prepared, and the GATT was progressively reorganized to form the WTO (World Trade Organization) after the realization of the Uruguay Round agreement in 1993.

The WTO newly covers to expand the range of rules, service trade and side aspects of trading of intellectual property rights, adding to reduction of duty and non-tariff barriers concerning trade of goods through round negotiations, and reinforcement and improvement of commerce rules to raise possibility of anticipation that the GATT took charges conventionally. In addition, confrontation settlement function is also strengthened radically in that the objective-range is expanded and practicality also improved over the GATT.

In addition, after establishment of the WTO, member countries and regions have expanded too. There were 76 member countries and regions in 1995 when the WTO was established compared with 153 countries and regions as of Apr. 2011 (China in 2001, Taiwan in 2002, Cambodia in 2004, Saudi Arabia in 2005, Vietnam in 2007 and Ukraine and Cape Verde in 2008 entered WTO respectively). Furthermore, around 30 countries including Russia have applied to become member countries. The number of member countries is expected to increase more and more, and it can be thought that it can support the base of the world free trade system continuously in the future.

### **(B) Features and process of Doha Round negotiations<sup>37</sup>**

The Doha development agenda ("Doha Round" from now on) declared its establishment in the 4th WTO regular ministerial meeting held in Doha, Qatar in 2001. Its features are that it covers, not only the liberalization of trade of goods, a wide range of sectors that correspond to requirements in the new period in that globalization and introduction of IT are progressed, including trade rules such as service trade and anti-dumping and so on, and environment and developing countries issues. For Japan, the promotion of this round has meant – (i) ensuring duty rates in other developed countries and major developing countries are lowered, (ii) making is easier for Japanese service industry to enter overseas markets, (iii) raising the possibility of anticipation via strengthening of commerce rules, and prevent commerce-related confrontations preemptively, (iv) igniting promotion of domestic structural reforms in member countries and

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<sup>36</sup> After the 5th negotiations started in 1960 (Dillon Round), the multidirectional negotiations are called "\*\*\* round".

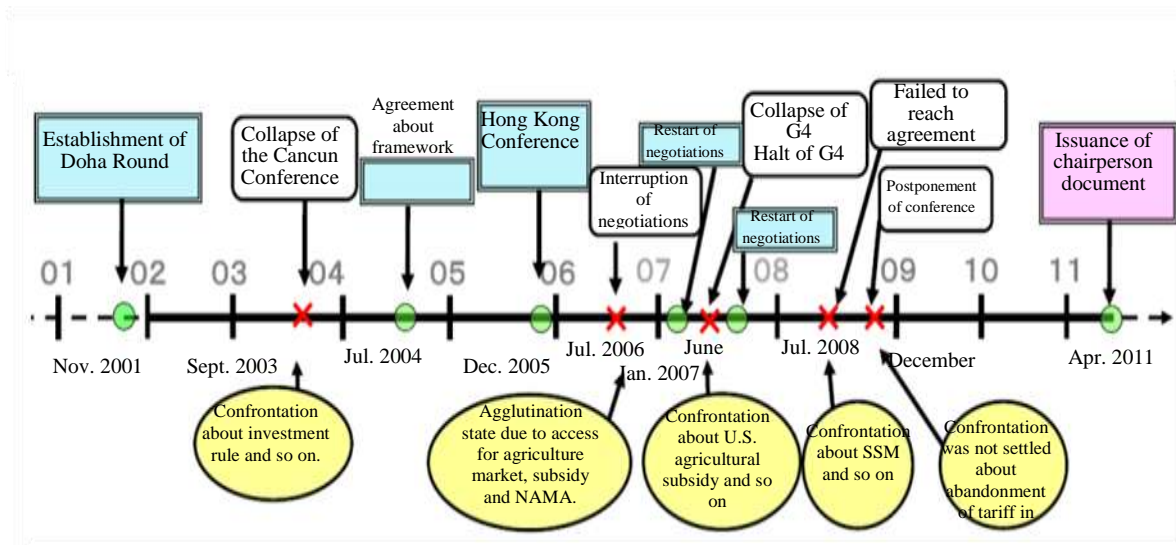
<sup>37</sup> When it comes to detailed process of the negotiation, please refer to the 1st section of material edition "[Moves of Doha Development Agenda](#)" in the "[2011 Report about Unfair Trade: WTO Agreement and Economic Cooperation Agreement, Trade policies of major countries from a viewpoint of Investment Agreement](#)".

regions -- and so on.

The Doha Round negotiations is a complex and tough matter that aims to reach agreement among 153 countries and regions which have differences in economic development stages, benefits and interests. When it comes to the previous Uruguay Round, the agreement was reached, taking eight years, fluctuating repeatedly, by tenacious negotiations by the entities concerned. When it comes to the Doha Round, the negotiations have been delayed due to confrontation between developed countries and newly emerging countries after breakdown of the ministerial meeting in Jul. 2008, and 2011 is said to be a critical year for the negotiations because politically important judgments are thought to become tough as the U.S. presidential election is to be held in 2012. Following the concentrated argument in Geneva, the chairperson document, which reflects the progress of negotiation in all the negotiation fields, was issued on Apr. 21, 2011. Although it was the first time, and a necessary step for the sake of an agreement of the negotiations that well-organized documents in all fields were prepared, the contents reflect the severe conditions of the Doha Round negotiations. In the tenth year of the establishment of the Round, the Doha Round is in a crucial situation (Figure 5-2-3-1, Figure 5-2-3-2). As maintenance and strengthening of a multidirectional free trade system by the WTO is important continuously for Japan, we are going to act positively aiming to an agreement of the Doha Round.

At present, negotiations are carried out in various fields such as NAMA and rule in the Doha Round (Table 5-2-3-3).

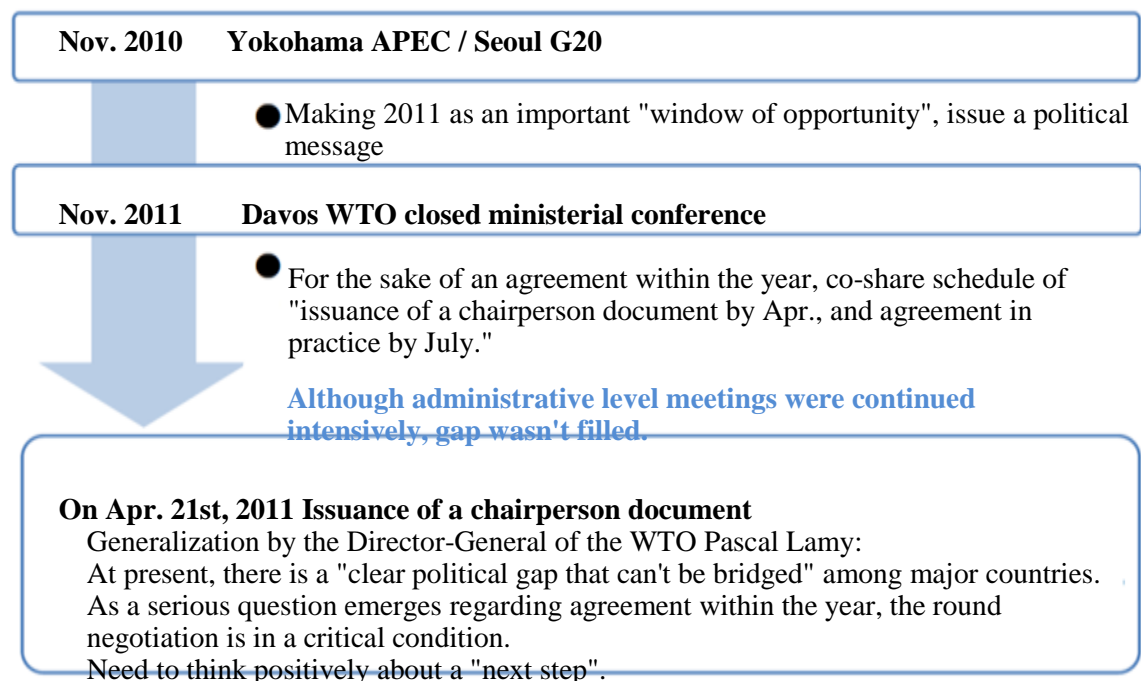
**Figure 5-2-3-1 Process of Doha Round negotiations**



**Notes**

- 1: G4 is the U.S., EU, India and Brazil. G6 is G4 + Japan and Australia
  - 2: SSM means Special Safeguard Mechanisms for agricultural sector in developing countries
- Source: Compiled by METI

**Figure 5-2-3-2 Recent progress of Doha round negotiations**



Source: Compiled by METI

**Table 5-2-3-3 Major argument points in negotiations**

Agriculture	Reduction of U.S. domestic subsidy, market access in major countries (tariff reduction), consideration for developing countries.
NAMA Non-Agricultural Market Access	Tariff reduction (Switzerland - formula, tariff abandonment in each field), abandonment of non-tariff trade barrier.
Service	Foreign capital restriction in each country, movement of people, making domestic regulation transparent.
Rule	Tightening of anti-dumping rule, tightening of subsidy rule.
Trade facilitation	Simplification of trade procedures, as well as assisting developing countries with their implementation.

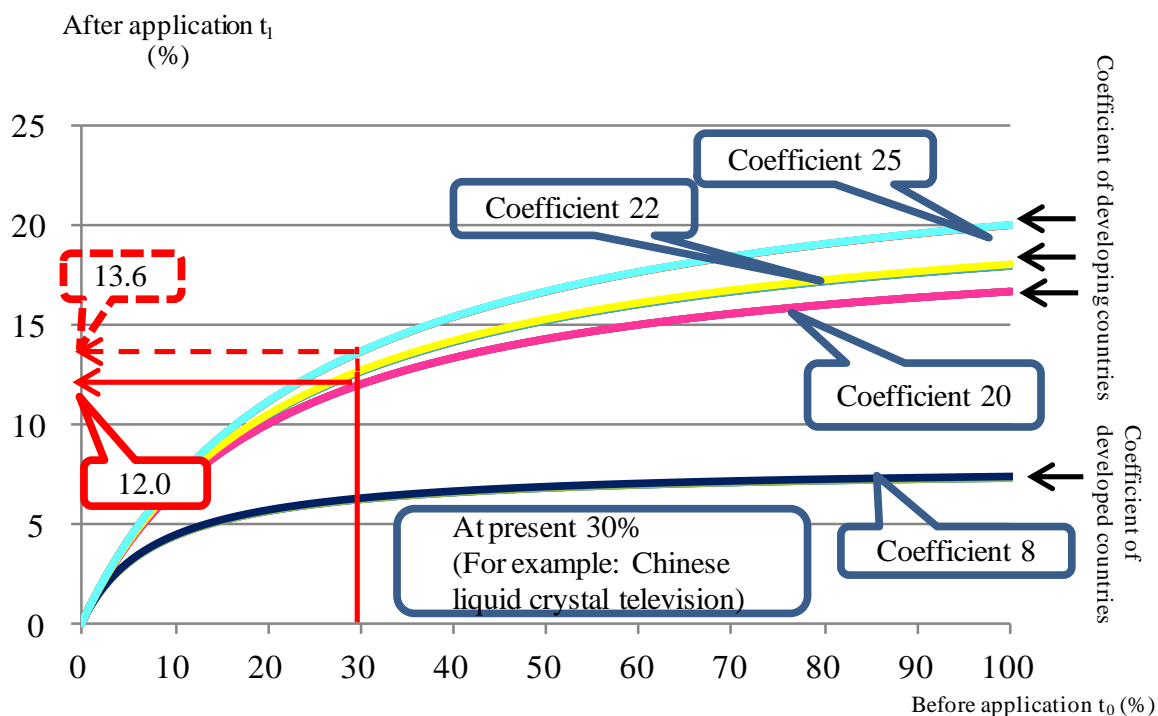
Notes: In addition to the above mentioned, negotiations are carried out regarding TRIPS (intellectual property right-related), development, trade and environment sectors.

Source: Compiled by METI

**(a) Non-Agricultural Market Access (NAMA), exchange of green materials**

NAMA negotiations are negotiations regarding abolition and reduction of duty and non-tariff-barrier concerning items other than agricultural products (mining and manufacturing industries products, and forestry and fishery industries goods). One of the major points at issue is the flat tariff reduction method for all items covered by NAMA negotiations (Switzerland formula), and exceptional measures for developing countries when applying this formula (relaxation of the tariff elimination or exemption). When it comes to the coefficient that decides the reduction width of the Switzerland formula and applying the ratio of exception measures, taking the argument in the ministerial meeting in Jul. 2008 into consideration, although it doesn't reach at the final agreement, a concrete numerical value is shown in the 4th revised edition of chairperson text in Dec. 2008 (Figure 5-2-3-4).

**Figure 5-2-3-4 Change of duty reduction according to Switzerland formula coefficient**



Source: Compiled by METI

In the NAMA negotiations, supplementing duty reduction by a formula to improve market access, duty abolition according to each field becomes one of the major points at issue. Although NAMA commitments are, in principle, voluntary commitments by countries, proponent countries are discussing how to involve more major trading partners. Japan also proposed duty abolition according to electrical and electronic goods field, and auto and auto parts, and actively promoted these goals among member countries. In the non-official WTO ministerial meeting in May 2010 and the senior administrative level meeting held at the opportunity of the APEC ministerial meeting in June the same year, by dividing objective items into the product field, and setting flexible conditions considering each country's export-interests and items of which abolition of duty is difficult, Japan proposed a basket approach seeking contents of suggestion that were ambitious and acceptable, and led the discussion.

When it comes to abolition of non-tariff barriers, interested countries proposed according to each theme and sector such as technical standards, indication obligation, import-regulations and so on, and detailed arguments have been promoted about each proposal since 2009. Japan proposed about strengthening export-regulation reports, asking for each country's participation, and it became to be the joint-proposal by seven countries.

When it comes to green materials, the arguments are carried out at the Special Session of the Committee on Trade and Environment, WTO, and suggestions are turned in by each country about promotion of use of renewable energy and so on. Based on a viewpoint of settling the

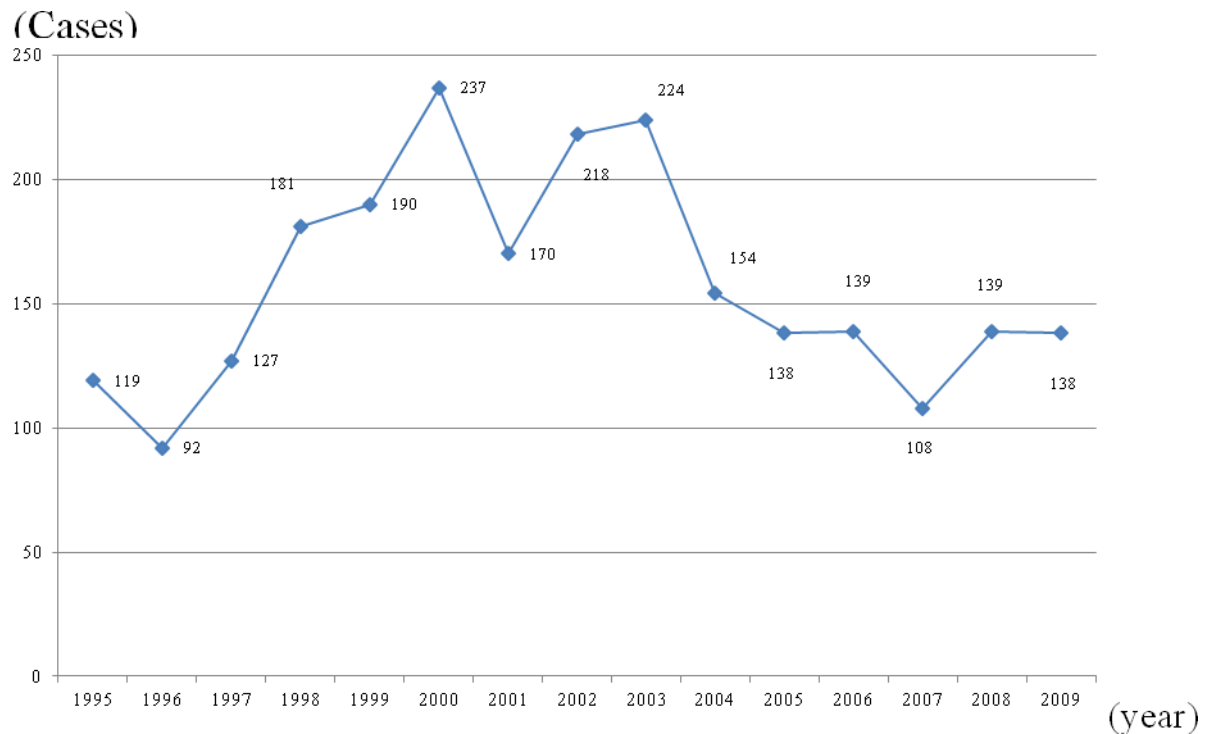


climate change issue, Japan proposed about duty reduction over green materials, mainly hybrid vehicles and energy saving home appliances in Feb. 2010. In the negotiations meeting, the arguments continue about the definition and range of green materials that should be covered for duty abolition and reduction, and the way to reduce duty and so on.

**(b) Rules (Preventing the Abuse of Anti-Dumping Measures)**

One of the topics of the Doha round of trade negotiations were the rules concerning anti-dumping (AD) measures. The number of AD measures implemented has consistently remained at a high level (see graph 5-2-3-5), with an increasing number of measures implemented by developing countries (table 5-2-3-6). At present, there is a large discrepancy among member countries regarding the interpretation of AD rules and their application, which is one of the reasons why they are inappropriately and excessively implemented. The overuse of AD measures harms the goal of tariff reduction and improved market access. Strengthening and clarifying the anti-dumping rules is therefore essential for the maintenance of the free trade system as well as the promotion of global economic growth.

**Figure 5-2-3-5 Number of WTO Anti-Dumping Cases, 1995-2009**



**Table 5-2-3-6 Number of AD measures by country (1995 - 2008)**

Reporting member			Exporting member		
1	India	419	1	China	538
2	The U.S.	284	2	South Korea	164
3	EU	267	3	Taiwan	128
4	Argentina	183	4	The U.S.	122
5	Turkey	133	5	Japan	112
6	China	130	6	Russia	95
7	South Africa	127	7	Thailand	93
8	Brazil	102	8	India	89
9	Canada	92	9	Indonesia	89
10	Mexico	82	10	Brazil	78

Source: Compiled from web site of WTO

In the negotiations, Japan proactively took on a leadership role and, together with other countries also intent on strengthening and clarifying the AD rules, submitted many important proposals.

On the other hand, although the United States are in favor of strengthening the transparency of implementing procedures and ensuring the appropriate use of AD measures, against the backdrop of an increasing number of AD measures being implemented by developing countries against the United States, there is a strong sense in Congress and industry that the implementation of AD measures is required. Therefore, with a view to retaining its discretion as much as possible, the Department of Commerce has been slow to encourage the strengthening of AD rules.

At the end of November 2007, the Chairman of the Negotiating Group on Rules issued a draft text (“the 2007 draft rules”). However, although the draft contained some commendable provisions on sunset clauses, the draft as a whole did not reflect members’ interests in a balanced manner, as it permitted the controversial practice of “zeroing” opposed by the great majority of members. Therefore, Japan submitted a draft proposal amending the main points in dispute and, together with many other members, demanded that a revised, more balanced draft text be issued. As a result, in May 2008, the Chairman of the Negotiating Group on Rules issued a working paper, and in December 2008, a new draft text (“the 2008 draft rules”). That text was a reform proposal based only on points of agreement among all participating members. It did not include provisions on controversial topics such as zeroing, sunset clauses, as well as 12 other issues to which all countries were opposed. Instead, it merely listed each topic along with a record of each country’s point of view.

In April 2011, based on the arguments gathered during the discussion over the 2008 draft rules, the Chairman of the Negotiating Group on Rules once again released a draft text (“the 2011 draft rules”). The provisions contained in the 2008 draft rules were amended in part to reflect the progress in the negotiations on items such as provisions establishing appropriate AD procedures as well as enhancing the transparency of AD investigations, among others, where agreement among all members had been reached. On the other hand, as there was no major change in members’ position regarding 12 contentious issues, including “zeroing” and “sunset clauses”, the 2011 draft rules did not include provisions on these 12 issues, and instead simply listed each member’s position on the matter. It is important for Japan to continue to proactively take part in the Negotiating

Group discussions, with the goal of strengthening the AD rules.

### **(3) The current WTO enforcement regime**

At the same time as providing free and fair trade rules, the WTO Agreement also provides a forum to settle disputes in case disagreements or trade frictions arise among members. The WTO's Dispute Settlement Body interprets and applies the WTO's rules with the aim of reducing trade frictions. The WTO Dispute Settlement Body provides not only recommendations to amend problematic measures, but also has the power to permit members to implement countermeasures in case the Panel's decision is not implemented. Therefore, compared with other international dispute settlement systems, the WTO system is exceptionally effective.

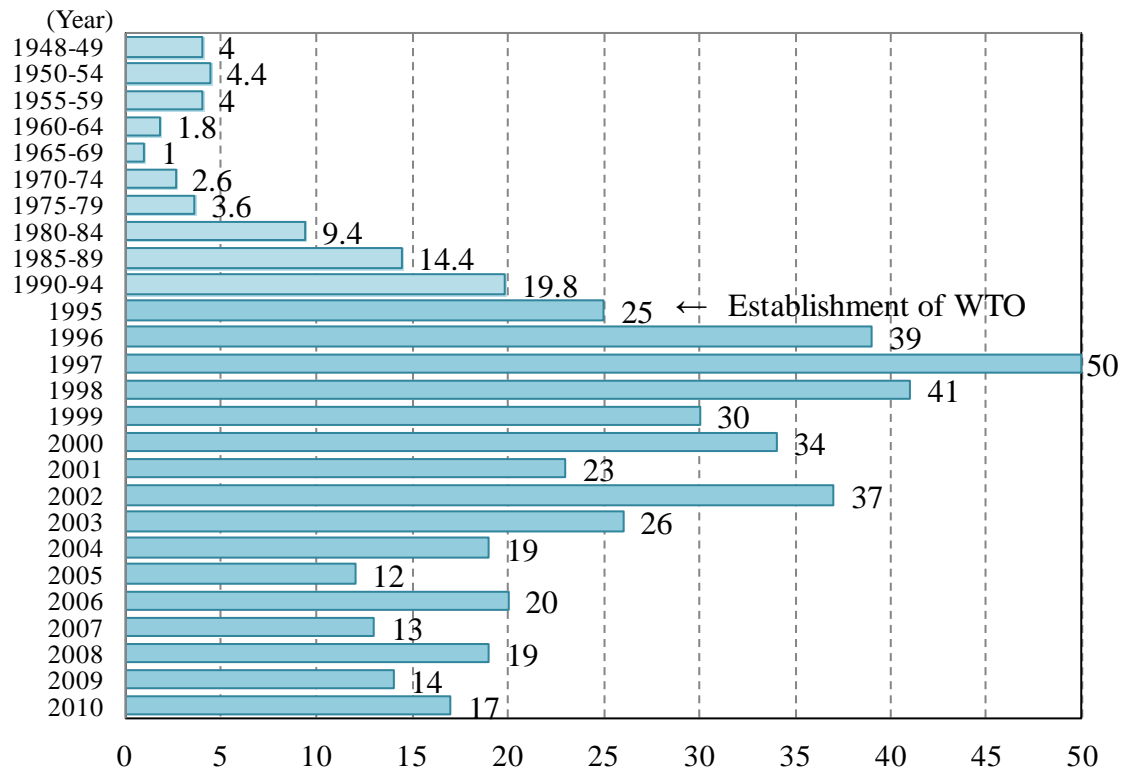
Where a foreign country infringes the WTO Agreement, demanding that it revise its laws is, of course, important to rectify measures which cause disadvantage to Japan, but also to preserve the efficacy of the WTO Agreement. Furthermore, to avoid unnecessary diplomatic rows resulting from trade friction, claims based on the duties and obligations contained in the WTO Agreement must be dealt with and settled. On the basis of this objective, Japan firmly demands the revision of political measures which violate the WTO Agreement, not only through bilateral negotiations, but also through recourse to the WTO Dispute Settlement System.

The creation of the WTO has resulted in a drastic strengthening of the Dispute Settlement System compared to the GATT era. The number of requests for consultation under the Dispute Settlement System has increased dramatically, which shows that the WTO members actively strive to resolve their disputes by reference to the WTO trade rules. (see graph 5-2-3-7). Since the founding of the WTO in 1995, the number of cases under the WTO Dispute Settlement System has reached 424 (as of April 2011). Japan has made requests for consultation in 14 cases, and participates as a third party in a large number of disputes. From the viewpoint of advancing trade policy, disputes currently considered as a high priority (METI priorities) are the below 14 cases<sup>38</sup> (see chart 5-2-3-8).

**Figure 5-2-3-7** Number of Requests for Consultation under the GATT/WTO Dispute Settlement System

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<sup>38</sup> Ministry of Economy, Trade and Industry, 2011 Report on Compliance by Major Trading Partners with Trade Agreements – WTO, FTA/EPAs, BITs-



Note: In GATT period (1948-1994) the numbers are annual average. After establishment of WTO, numbers are for each year.

Source: Compiled from the 2011 Unfair Trade Report and materials of METI.

**Table 5-2-3-8 Prioritized action items of METI from now on**

(a) Issues to be solved through bilateral or multilateral discussion or to be referred to for WTO dispute settlement procedure
<ul style="list-style-type: none"> <li>○ China <ul style="list-style-type: none"> <li>● To respond to export restrictions on mineral resources</li> <li>● To rectify discriminations in the “voluntarily created innovation product certification system”, or to improve government procurement regulations and implementation.</li> <li>● To rectify improper operation at the time of an anti-dumping investigation</li> <li>● To respond to issues of commercial frauds such as counterfeiting and piracy</li> </ul> </li> <li>○ Various Asian countries (ASEAN, South Korea, Taiwan, Hong Kong, India) <ul style="list-style-type: none"> <li>● To respond to issues of commercial fraud such as counterfeiting and piracy</li> </ul> </li> <li>○ U.S. <ul style="list-style-type: none"> <li>● Early elimination of improvement of operation of sunset review procedures and unfairly long-term AD measures to Japan</li> </ul> </li> <li>○ Russia <ul style="list-style-type: none"> <li>● Elimination of measures to raise the automobile tariff</li> </ul> </li> <li>○ Argentina <ul style="list-style-type: none"> <li>● Improvement the Non-Automatic Import Licensing System</li> </ul> </li> </ul>
(b) Issues which have been referred to for WTO dispute settlement procedure
<ul style="list-style-type: none"> <li>○ Canada <ul style="list-style-type: none"> <li>● Elimination of obligation of local content associated with the electric power fixed price purchase system associated with renewable energy in Ontario</li> </ul> </li> </ul>
(c) Issues which shall be continued to be solved although they are not referred to in the WTO dispute settlement procedures
<ul style="list-style-type: none"> <li>○ U.S. <ul style="list-style-type: none"> <li>● Early implementation of WHO recommendations associated with zeroing</li> <li>● Discontinuation of distribution of anti-dumping taxes and countervailing duty revenue on goods that have completed custom clearance to U.S. companies, based on the Byrd amendment</li> <li>● Early implementation of WTO recommendations associated with anti-dumping measures on Japanese made hot-rolled steel</li> </ul> </li> <li>○ EU <ul style="list-style-type: none"> <li>● Elimination of tariffs on commodities applicable to WTO Information Technology Agreement which should be tax-free</li> </ul> </li> <li>○ China <ul style="list-style-type: none"> <li>● Early implementation of WTO recommendations on the trade right and circulation service of publication and the sound picture entertainment products</li> </ul> </li> </ul>

Note: Although this issue is a Sino-U.S confrontation one, Japan also participated in it as a third country, and we continue to pay a close eye with interest to China carrying out the WTO advice.

Source: Compiled from “Action Policy of METI in response to Unfair Trade Report”, METI

## **Column 8 Cases that Japan intends to settle via referring them to the dispute settlement system**

When it comes to policies and measures of foreign governments that violate WTO agreement, Japan makes effort to improve them at every opportunity through bilateral negotiation and the WTO dispute settlement system. As follows are recent cases that Japan expects to refer to the WTO dispute settlement system:

### **(1) Abolition of the local content duty concerning renewable energy-related electricity Feed-in Tariff Program system in Ontario state. (Canada)**

In May, 2009, Ontario (Canada) founded a fixed-price purchase system of electricity (Feed-in Tariff Program) generated by solar and wind power. At that time, as an entry condition for generation firms, the state government made it an obligation (local content requirement) to use more than a certain ratio of added-value facilities of solar power generation and wind power generation (assembling or procurement of raw materials) that were added in-state. When generation firms that are going to enter the Feed-in Tariff Program system and purchase solar power panels and so on, due to local content requirement, the incentive to purchase made in Ontario products rather than imported ones is generated. As a result, products such as solar power panels that Japanese firms export to Ontario are treated less favorably than the products made in the state.

In response to the request from the industry, Japan continued high level pressure in order to abolish the measure. Then Minister of Economy, Trade and Industry Naoshima, and then Foreign Minister Okada asked for corrective measures to the Canada International Trade Minister in an APEC meeting by ministers in charge of trade in Jun. 2010. However, moves of improvement measures were not seen in the Canadian side, and Japan called for bilateral negotiation based on the WTO confrontation settlement procedure in Sept. 2010. Although Japan continued pressure in talks several times, as some moves were seen that were against improvement such as Ontario raised the local content ratio from 50% to 60% in Jan. 2011 and so on, Japan called for a setting of the WTO confrontation processing subcommittee (panel) in Jun. 2011.

Such favorable treatment of domestic products could spread easily in third countries, and Japanese green industries such as solar power panel and so on that have competitiveness could be affected strongly. Japan continuously demands the abolition of the measures based on the WTO confrontation settlement procedure.

### **(2) Abolition of imposing tariffs on products that are subject to the WTO Information Technology Agreement (ITA) that should be duty free (EU)**

Based on the WTO Information Technology Agreement (ITA), the EU imposes high duties on products that are out of the agreement while making electric products covered by the agreement duty-free. In recent years, the EU has been intentionally changing the duty classification of products that should be covered by the agreement originally, and imposes high duties that are same for products out of the agreement. (This includes a tax rate of 6% for complex machines, 14% for PC LCD monitors, 13.9% for set top boxes (cable TV broadcast receivers). For example, exports by Japanese firms to the EU are around ¥300 billion annually for complex machines alone, and overpayment of ¥14 billion occurs annually.

With the U.S. and Taiwan, Japan called for a talk based on the WTO confrontation settlement procedure in May 2008. The talk ended in failure and called for the setting of a panel in Aug. 2008. In Aug. 2010, the panel issued the report that accepted Japan's argument completely, and as the EU didn't appeal to a higher stage, the judgment of the panel was settled in the WTO confrontation settlement institutional meeting held in Sept. of the year (the end of Jun. 2011 is the due date for the EU).

### **(3) Unfair dumping determination by the zeroing method. (U.S.)**

When it comes to AD procedures, the U.S. determines dumping by an unfair method called zeroing (Refer to 2. (2) (b) rule “prevention of anti-dumping”). Unfair AD tax based on this zeroing has been imposed on Japan's ball bearing industry since 1989.

In Nov. 2004, Japan required a talk based on the WTO confrontation settlement procedure, and argued that the U.S. zeroing system and its application violated the WTO agreement. The upper committee report issued in Jan. 2007 authorized WTO agreement violation of zeroing, and urged the U.S. to abolish that. In Feb. 2007, the U.S. partially abolished zeroing measures (applying zeroing in the first investigation using weighted average).

However, as the U.S. maintained a zeroing system other than that procedure and the comparison technique, and did not take enough execution measures afterwards, Japan applied for approval of counter measures in Jan. 2008, and in addition called for the setting of the execution confirmation panel for the confirmation that the U.S. did not carry out enough execution measures in April of that year. As the upper committee decided that the U.S. did not carry out the advice after the execution of the WTO advice deadline in Aug. 2009, Japan restarted an arbitration procedure to decide the scale of counter measures in Apr. 2010 (Japan argues that \$265 million is equivalent). In Dec. of that year, the U.S. released a domestic regulation reform bill to abolish zeroing, and started acceptance of public comments (Japan and the U.S. agreed to suspend an arbitration procedure temporarily in the same month). At present, the enforcement of the reform bill is not done. Japan requires the U.S. to carry out the WTO advice promptly and completely.



## **Column 9 Cases of action to develop rules other than the WTO**

Process and significance of the “ACTA: Anti-Counterfeiting Trade Agreement” (tentative name).

### **[Process]**

The Anti-Counterfeiting Trade Agreement (tentative name) (ACTA) is a new international legal framework to strengthen the execution of intellectual property rights proposed by Japan in the 2005 G8 Summit, and after the negotiating meetings of 11 times in total in that Japan, the U.S., European Union (EU), Switzerland, Canada, South Korea, Mexico, Singapore, Australia, NZ and Morocco participated. The general agreement was reached in Oct. 2010 and ACTA was opened for signing on May 1st, 2011, and aimed to taken effect quickly with countries concerned.

### **[Background of ACTA: The global proliferation of imitation products and pirated editions, and new international approach]**

The global proliferation of imitation products and pirated editions, due to circulation of low-durability auto parts and imitation lithium batteries that have ignition risks and so on, become a direct threat for health and safety of consumers. In addition, it is pointed out that there is a possibility that production and circulation of imitation products and pirated editions are an easy source of funds for criminal syndicates. It can be said that each country's current and bilateral action are necessarily enough for these problems so that action in more countries is required. Although there is the WTO/TRIPS agreement as current multi international rules concerning intellectual property rights protection, as violation of intellectual property rights increases mainly by pirated editions and imitation products due to recent advancement of methods for infringement of intellectual property rights and development of digital technology, recognition for the necessity to establish a more effective legal framework for the execution of intellectual property rights arose. Then in the 2005 G8 Gleneagles Summit, Japan proposed the necessity of legal framework development to prevent imitation products and pirated editions, then the ACTA negotiations were started as initiative of the U.S.-Japan collaboration afterwards.

### **[Contents of ACTA]**

ACTA establishes a framework for the enforcement of the TRIPS Agreement. It provides for extended civil and criminal enforcement, increased border measures, as well as the enforcement of intellectual property rights in the digital environment. For example, in the area of border control measures by customs' authorities, the TRIPS Agreement was

confined to discretionary provisions, whereas under ACTA, each party will be under a duty to set up procedures relating to counterfeit trademark goods and pirated copyright goods allowing customs authorities to act upon their own initiative to suspend the release of suspect goods. Moreover, ACTA does not limit itself to the establishment of an effective legal framework, but also contains provisions relating to capacity building and international cooperation among contracting parties.

#### **[Significance and prospects of ACTA]**

The significance of ACTA is, first of all, that the legal framework regarding intellectual property rights protection of the contracted country itself is strengthened. Second, quality improvement can be expected too via cooperation among contracted countries. Third, it can also be expected to take a role in strengthening intellectual property enforcement beyond the range of contracted countries such as that the contents of ACTA will become a standard model of international regulation about enforcement, and be installed into various international agreements.

From the view point of ACTA contracted countries, along with pressuring non-contracted countries to join; it is thought that efforts should be made for ACTA regulations to be installed into bilateral and multi-national EPAs. It is thought that ideas will be transferred through sharing ACTA experiences with non-contracted countries through enforcement-affiliated execution cooperation between a contracted country and a non-contracted one. From now on, in addition to WTO/TRIPS, WIPO, EPA, ACTA is expected to be utilized as a forum to discuss and develop the framework of the international intellectual property field.

#### **4. Effects of the Great East Japan Earthquake disaster on the world supply chain and the importance of the cooperation agreement for restoration**

Since just after the earthquake disaster, pushing forward on restoration efforts with Japan as a whole, we have worked on restoration of infrastructure that was damaged or stopped due to the earthquake disaster, and making a system appropriate to the decreased availability of electricity. We were able to feel the restoration effort by Japanese firms from the results of the “Urgent Survey of Industrial actual conditions after the Great East Japan Earthquake Disaster” at the beginning of April.

Particularly, although a portion of the supply chain (the supply chain of parts reaching the end product) was cut by the Great East Japan Earthquake disaster, through the strenuous efforts made by each firm, the supply chain recovered quickly in April. In order to accelerate such a trend, and to connect the supply chain that links not only domestically but also overseas, it was expected that Tokyo would support firms well for the sake of revival of the Japanese economy.

However, it is a fact that many statements were issued around the world concerning the supply-chain shock emitted from Japan from just after the earthquake disaster to the end of April, and although restoration efforts are progressing, it became clear again that ripple effects occurred in many locations around the world such as the U.S., China and so on due to a decline of exports from Japan, in particular decline or termination of exports of parts and materials intended manufacturing businesses in various foreign countries and capital goods used by foreign firms.

As it is, Japan must maintain the technical excellence of Japanese firms in the parts, materials and production goods fields that can be considered as core, and the position of the entity in charge of their supply as Japanese strength. That is why Japan must support the revival and further development of such “global suppliers”.

It has become clear that quick copying or substitution of key parts that such firms produce is very difficult. In addition, the bases supporting the existence of such firms are the accumulation of a closely-connected network of related industries, and such clusters have been formed historically so that it is obvious that it is difficult to imitate or replace them overnight. Namely, under the present global economy, the sense of speed of economic activities is becoming so fast that it is not realistic to remake such concentrations of know-how quickly. On the contrary, it is unlikely that we are able to restore them once they are lost.

Furthermore, although it can't be denied that Japanese trade relationships have slightly declined in their presence quantitatively their input-output structure has become deeply integrated into the global economy. We can say that this shows that Japanese industrial accumulation is becoming a “hub” of the global supply chain network, and there are Asian-scale and world-scale networks that are connected downstream, and these connections are global.

Therefore it becomes increasingly important to promote "exports" that support global production more positively to maintain domestic production and employment, and under such conditions, the importance of preparation for an export environment that covers a wide range beyond duty reduction by economic cooperation including EPAs is rising.

Therefore, in order to maintain and develop Japan's agglomeration of technologies and know-how, and its highly advanced and efficient production capacity and know-how, it is beneficial for the world economy that products can be deployed and exported under equal conditions, and at the same time, when various costs fall due to economic cooperation, demands for damaged Japanese industrial accumulation will be secured, and push back production activity that is beginning to recover by corporate effort from the demand side.

The Japanese industrial structure has undergone significant changes. During the previous "full set structure" period, the inducement effects from final demand in export destinations unilaterally flowed into the Japanese domestic market. Under the current structure, the inducement effect from the Japanese domestic market flows outward to other countries. In this way, a situation will inevitably be reached where the inducement effect is linked only to final demand in other countries.

Although Asia currently enjoys striking economic growth and increases in affluence, the outlook is less positive, as the decline in working age populations and insufficient infrastructure will inevitably create constraints on economic growth. To these challenges, Japanese industry, with its superior technology, can offer a solution. One such solution, to counter the effects of the decline in working age populations across Asia, would be to export capital goods which improve productivity, such as robots, and implement a policy of "localization" by introducing Japan's highly effective management system and transferring management authority to local staff. In addition, as seen after the recent earthquake, Japanese infrastructure providers have considerable technological skill in rapidly restoring damaged infrastructure, and Japan can offer such expertise to other countries which currently have insufficient infrastructure.

Japanese exports of products and technology, along with Japanese FDI, can contribute to solving economic problems in East Asia and the Asia-Pacific region by sowing the seeds of economic growth, and sharing in the benefits. To uphold this kind of relationship a set of fair and transparent rules is needed, and herein lies the significance of continuing the negotiations for economic cooperation in East Asia and the Asia-Pacific region. It is hoped that a mutually beneficial relationship will develop between Japan and its trading partners, in which each of the parties' domestic final demand will reciprocally act as an inducement to its trading partners' production.

Moreover, Japanese firms should not limit their exports of products which are essential

elements in the global supply chain to destinations within the Asia and Pacific region. Rather, Japan should strengthen its relationship with Central and Eastern Europe and Central and South America in response to economic growth in these regions, in order to encourage mutually profitable “inducement effects”.

When it comes to each recent multi and bilateral economic cooperation negotiation, aiming to lead to desirable production induction, arguments are promoted intending for broad meaning of cost reduction that affect corporate economic activities and transaction network between firms. The arguments about supply chain connectivity promoted by APEC are the typical example of that, and decisions in wide range of fields are agreed in bilateral cooperative agreements. When it comes to economic cooperation agreements such as Japan-EU EIA, CEPEA and so on, while Japan achieves global supply responsibility, it will also be desirable to be promoted in a viewpoint of preparation of preconditions to maintain and develop domestic industrial accumulation.

As seen in the Sumatra earthquake, the flooding that devastated New Orleans and the major earthquake in Sichuan, it is an undeniable fact that there are natural disaster risks not only in Japan but also for the world economy itself no matter how large or small, and there is no way but for firms and each economic entity to share the burden of such risks under global scale network structure and mutual cooperation.

For the sake of that, it could be the required acts for Tokyo to promote economic cooperation globally in the form of preparation of rules via multi and bilateral negotiations and other various channels, and remove factors that spoil firms' rational judgments concerning securing security (decentralization), effectively balanced corporate locations and commerce actions.