VI. LEGAL ARGUMENTS CONCERNING NON-VIOLATION CLAIMS

A. INTRODUCTION TO ARTICLE XXIII:1(b) OF GATT

1. GENERAL PRINCIPLES

6.1 According to **Japan**, when examining the factual and legal claims brought by the United States concerning consumer photographic film and paper in the Japanese market, three general principles for panel proceedings should guide the analysis. First, any interpretation of GATT should be in accordance with customary rules of interpretation under public international law. Second, the recommendations or rulings of this Panel cannot add to or diminish the rights and obligations of the WTO Members. Third, the burden of proof rests with the complaining party. Japan emphasizes that these general principles should guide the Panel's consideration not only of the claims under Article XXIII:1(b), but also with respect to those raised under Articles III and X (discussed in detail in Part VII infra).

6.2 Japan points out that Article 3.2 of the DSU refers to "customary rules of interpretation of public international law" as general principles for interpreting WTO Agreements within the framework of the WTO dispute settlement system. Japan is of the view that Article 31 on the general rules of interpretation and Article 32 on the supplementary means of interpretation of the Vienna Convention on the Law of Treaties represent such "customary rules of interpretation of public international law".[1] Japan requests the Panel in this proceeding to interpret and apply the provisions of the WTO Agreement pertinent to this case in accordance with the relevant rules of the Vienna Convention.

6.3 Japan also urges the Panel to take a cautious approach and to refrain from adding to or diminishing the rights and obligations of the WTO Members under the WTO Agreement in accordance with Articles 3.2[2] and 19.2[3] of the DSU which provides for the same principle with respect to the findings and recommendations of panels and the Appellate Body.

6.4 With respect to Japan's admonition to the Panel that it should not add to or diminish the rights and obligations of the WTO Members under the WTO Agreement, the **United States** notes that in this case Japan appears to be trying to diminish the rights of the United States and all other Members under Article XXIII:1(b) by instructing the Panel to apply certain "rules" in its interpretation and application of Article XXIII:1(b) in this dispute.[4]

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[1]See, e.g., Appellate Body Report on *United States - Standards for Reformulated and Conventional Gasoline* (*"United States - Gasoline"*), WT/DS2/AB/R, adopted on 20 May 1996 and Appellate Body Report on *Japan - Taxes on Alcoholic Beverages* (*"Japan - Alcoholic Beverages"*), WT/DS8, 10 & 11/AB/R, adopted on 1 November 1996.

[2]In a recent article, Professor John Jackson of the University of Michigan echoed the same concern:
"Arguably, [Article 3 of the DSU] resonates in the direction of a caution to the panels to use judicial restraint and avoid being too activist. ... So this notion of restraining panels from making changes in the rights and obligations of the nation states is quite prevalent in the system. The United States would likely be one of the most jealous in preserving judicial restraint, yet at the same time it appears to be pushing the envelope in some of its own complaints to the WTO. When, for instance, the United States or another country brings a case that does not involve a violation but instead targets competition policy, the Japanese *keiretsu*, or something else that current treaty texts do not cover, it is likely to be asking a panel to change 'rights and obligations'. In other words, it is saying to a panel, 'We want you to interpret nullification or impairment to embrace some of these results that for policy reasons we would like to see in this case'. That is risky - akin to doing with one hand what the other is trying to prevent. Obviously, this has fundamental long-term implications." John Jackson, The WTO Dispute Settlement Procedures: A Preliminary Appraisal, in: Jeffrey J. Schott (ed.), The World Trading System: Challenges Ahead December 1996, p. 163, Japan Ex. E-10.

[3]Japan notes that Article 19:2 of the DSU stipulates: "... in their findings and recommendations, the panel and Appellate Body cannot add to or diminish the rights and obligations provided in the covered agreements".

[4]The United States refers in particular to Japan's statement that "in determining whether a benefit is being nullified or impaired, this Panel must focus exclusively on the measures themselves".

6.5 **Japan** submits that under the WTO dispute settlement system, the Member bringing a case has the initial burden of proving its claims. This was a well-established principle under GATT 1947 dispute settlement[5] and has been carried over into the WTO, based on Article 3.1 of the DSU and Article XVI:1 of the Marrakesh Agreement Establishing the WTO.[6]

6.6 Japan emphasizes that in non-violation cases under Article XXIII:1(b), the complaining party is required to bear a particularly heavy burden of proof according to Article 26:1(a) of the DSU, which requires "[t]he complaining party shall present a detailed justification in support of any complaint relating to a measure which does not conflict with the relevant covered agreement". In this connection, Japan notes that this requirement of a "detailed justification" in non-violation cases was incorporated in the 1979 Agreed Description of the Customary Practice of the GATT in the Field of Dispute Settlement[7] and had been applied by the relevant GATT panels.[8]

2. THE LEGAL TEST UNDER ARTICLE XXIII:1(b)

6.7 The **United States** claims that Japan's liberalization countermeasures detailed in Part V nullify or impair tariff concessions on consumer photographic film and paper within the meaning of Article XXIII:1(b) of GATT. Article XXIII:1(b) provides for dispute settlement under the following circumstances:

> "1. If any [Member] should consider that any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired or that the attainment of any objective of the Agreement is being impeded as the result of . . .
>
> (b) the application by another [Member] of any measure, whether or not it conflicts with the provisions of this Agreement . . .".

6.8 The United States recalls that the panel report on *European Economic Community - Payments and Subsidies Paid to Processors and Producers of Oilseeds and Related Animal Feed Proteins* ("EEC -Oilseeds") noted that the underlying purpose of Article XXIII:1(b) was to safeguard the process of reciprocal tariff concessions under Article II:

> "The idea underlying [the provisions of Article XXIII:1(b)] is that the improved competitive opportunities that can legitimately be expected from a tariff concession can be frustrated not only by measures proscribed by the General Agreement but also by measures

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[5]See, e.g., Panel Report on *Japan - Tariff on Imports of Spruce, Pine, Fir (SPF) Dimension Lumber*, adopted on 19 July 1989, BISD 36S/167, p. 198, para. 5.10; Panel Report on *Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies* ("Canada - Alcoholic Drinks"), adopted on 18 February 1992, BISD 39S/27, p. 75, para. 5.3. See also John H. Jackson, William J. Davey & Alan O. Sykes, Legal Problems of International Economic Relations, 1995, p. 355, Japan Ex. E-2.

[6]Article 3.1 of the DSU affirms that the WTO Members adhere "to the principles for the management of disputes heretofore applied under Articles XXII and XXIII of GATT 1947". Article XVI:1 of the Marrakesh Agreement Establishing the WTO provides that "the WTO shall be guided by the decisions, procedures, and customary practices followed by the CONTRACTING PARTIES to GATT 1947 . . .".

[7]Understanding Regarding Notification Consultation, Dispute Settlement and Surveillance, Annex, adopted on 28 November 1979, BISD 26S/210, p. 216.

[8]A past panel report states that "[a]ccording to the 1979 Understanding on Dispute Settlement, a contracting party bringing a complaint under Article XXIII:1(b) is called upon to provide a detailed justification" (*United States - 1955 Waiver*, BISD 37S/228, 261, para. 5.21). See also Panel Report on *Japan - Trade in Semi-Conductors ("Japan - Semi-Conductors")*, adopted on 4 May 1988, BISD 35S/116, 35S/116, 161, para. 131; and Panel Report on *Uruguayan Recourse to Article XXIII*, adopted on 14 November 1962, BISD 11S/95, 99-100, para. 15.

> consistent with that Agreement. In order to encourage contracting parties to make tariff concessions they must therefore be given a right of redress when a reciprocal concession is impaired by another contracting party as a result of the application of any measure, whether or not it conflicts with the General Agreement".[9]

"The Panel considered that the main value of a tariff concession is that it provides an assurance of better market access through improved price competition. Contracting parties negotiate tariff concessions primarily to obtain that advantage. They must therefore be assumed to base their tariff negotiations on the expectation that the price effect of the tariff concessions will not be systematically offset. If no right of redress were given to them in such a case they would be reluctant to make tariff concessions and the General Agreement would no longer be useful as a legal framework for incorporating the results of trade negotiations".[10]

6.9 The United States cites another panel report to the same effect: "Article XXIII:1(b), as conceived by the drafters and applied by the CONTRACTING PARTIES, serves mainly to protect the balance of tariff concessions".[11] The value that the United States placed on obtaining tariff concessions on photographic film and paper and the attendant expectations of improved competitive opportunities is evident from its continuing efforts to secure improved access to the Japanese film and paper market during three successive rounds of multilateral trade negotiations. The United States assumed that the concessions for which it negotiated would not be systematically offset by the Japanese Government.

6.10 According to the United States, prior working parties and panels have applied the following elements in analysing claims under Article XXIII:1(b):

(1) a tariff concession was negotiated;
(2) government measures, whether or not inconsistent with the General Agreement, were introduced which upset the competitive relationship between the bound product and directly competitive products from other origins; and
(3) the measures could not have been reasonably anticipated by the party to whom the binding was made, at the time of the tariff concession.[12]

6.11 In the current case, the United States submits that the consideration of the US claim can be broken down into three separate elements:

(1) whether the United States had a reasonable expectation of improved market access opportunities arising from Japan's tariff concessions;
(2) whether Japanese Government measures upset the competitive relationship between imported and domestic products; and
(3) whether the United States could have anticipated Japan's nullification or impairment of its tariff concessions.

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[9] Panel Report adopted on 25 January 1990, BISD 37S/86, pp. 126-127, para. 144.

[10] Ibid., pp. 128-129, para. 148.

[11] Panel Report on *United States - Restrictions on the Importation of Sugar and Sugar-Containing Products Applied Under the 1955 Waiver and Under the Headnote to the Schedule of Tariff Concessions* (*"United States - 1955 Waiver"*), adopted on 7 November 1990, BISD 37S/228, 261, para.5.21.

[12] *EEC - Oilseeds*, BISD 37S/86, 126-131, paras. 142-152. See also *Report of the Working Party on the Australian Subsidy on Ammonium Sulphate* ("Australia - Ammonium Sulphate"), adopted on 3 April 1950, BISD II/188, 192-193, para. 12; Panel Report on *Treatment by Germany of Imports of Sardines*, adopted on 31 October 1952, BISD 1S/53, 58-59, paras. 16-17; *EEC - Citrus Products*, L/5776 (unadopted) pp. 84-85, para. 4.26; Panel Report on *European Economic Community - Production Aids Granted on Canned Peaches, Canned Pears, Canned Fruit Cocktails and Dried Grapes* ("EEC - Canned Fruit"), GATT Doc. L/5778, 20 February 1985 (unadopted), p. 15, para. 51.

6.12 The United States claims that each of these elements is present in this case:

(1)The United States negotiated for and Japan granted the United States tariff concessions on photographic film and paper products in successive rounds of multilateral trade negotiations: the Kennedy, Tokyo, and Uruguay Rounds.
(2)Japan enacted, implemented and applied the distribution countermeasures, restrictions on large retail stores, and promotion countermeasures to obstruct market access and alter the competitive relationship between imports and domestic products.
(3)At the time each round of tariff concessions was made, the United States reasonably anticipated that better market access through improved price competition would result from the concessions, and neither the United States nor any of Japan's other trading partners could have foreseen that the Japanese Government would impair the value of those concessions through an intricate web of measures designed to counter the effects of liberalization.

6.13 The United States emphasizes that it provided, in accordance with Article 26.1 of the DSU, a detailed justification establishing its claim that Japan's distribution countermeasures, Large Stores Law and related measures, and promotion countermeasures collectively and individually nullify or impair its

(1) Kennedy Round tariff concessions on black and white film and paper;
(2) Tokyo Round tariff concessions on black and white film and paper and on colour film and paper; and
(3) Uruguay Round tariff concessions on black and white film and paper and on colour film and paper.

6.14 **Japan** submits that the scope of Article XXIII:1(b) in GATT jurisprudence is well defined and may be discerned by reference to three key phrases in the text of the provision:

(1) "any benefit accruing ... under this Agreement",
(2) the "application by another [Member] of any measure", and
(3) "is being nullified or impaired".

6.15 First, there must be a "benefit" accruing under this Agreement. This benefit consists of the legitimate expectations of improved competitive opportunities arising out of relevant tariff concessions. For expectations to be legitimate, they must take into account all measures of the party making the concession that could have been reasonably anticipated at the time of the concession. In other words, measures reasonably anticipated at the time of the tariff concession cannot frustrate legitimate expectations, and thus cannot nullify or impair a benefit accruing under this Agreement.

6.16 Second, there must be the application of a measure by another WTO Member. The term "measure" refers to a government policy or action, but not every such policy or action constitutes a measure for purposes of Article XXIII:1(b). Measures must either provide benefits or impose obligations. As to the latter, a measure for non-violation purposes must be a government policy or action which imposes legally binding obligations or the substantive equivalent. Furthermore, there must be an "application" of the measure. This requirement is relevant in the case of measures no longer in effect and measures not applied to products.

6.17 Third, the complaining party must show that the benefit in question "is being nullified or impaired" as the result of the application of the measure. To meet this requirement, the complaining party must demonstrate that the relevant measure is upsetting the competitive position of the imported products subject to the relevant tariff concession.

6.18 With respect to the case at issue, in Japan's view, the US non-violation claims do not meet any of the required elements mentioned above for the following reasons:

6.19 With respect to the first element, Japan notes that for measures to nullify or impair the benefit of tariff concessions, it must be established that they could not have been reasonably anticipated at the time of the relevant concession. Although the United States alleges nullification or impairment of tariff concessions on film and paper in three successive negotiating rounds - the 1967 Kennedy Round concessions (only on black and white film and paper), the 1979 Tokyo Round concessions, and the 1994 Uruguay Round concessions - Japan believes that the "benefits accruing under the Agreement" is limited to the benefits of the Uruguay Round concessions. In Japan's view, the 1994 concessions form a new balance of tariff concessions that were actually negotiated and agreed upon at that time.

6.20 Japan further argues that all of the policies in question were enacted and known to the United States long before the relevant tariff concessions, i.e., those made in 1994 with respect to black and white and colour film and paper. Even if earlier tariff concessions were to be taken into account, the timing problems that plague the US argument would remain. With respect to colour film and paper, the 1967 tariff concessions cannot be relevant at all because there were no tariff concessions on colour film and paper until 1979. Since virtually every government action in this case occurred before 1979, it is inconceivable that these policies could not be reasonably anticipated at the time of the 1979 tariff concessions. Even with respect to the 1967 concessions on black and white film and paper, many policies could be reasonably anticipated at the time of the tariff concessions. Accordingly, in Japan's view, all of the alleged measures could have been reasonably anticipated by the United States at the time of those tariff concessions.

6.21 With respect to the second element, in Japan's view, the United States claims that MITI's distribution modernization policies during the 1960s and '70s directed the private sector to restructure distribution practices so as to disadvantage imports. Furthermore, according to Japan, those policies did not impose any legally binding obligations or the substantive equivalent, and thus were not measures within the meaning of Article XXIII:1(b). However, those policies ended years ago, and thus, in Japan's view, are not currently actionable under Article XXIII:1(b). In the case of the Large Scale Retail Store Law, Japan argues that the United States fails to allege specific applications which nullify or impair a benefit. Japan concludes that the absence of any "application" of a measure renders the US claims regarding this law legally insufficient.

6.22 With respect to the third element, Japan contends that the government policies in question do not upset the competitive conditions relating to any of the distinct products subject to this dispute: black and white film, black and white paper, colour film, and colour paper. With respect to each of the three sets of policies at issue Japan submits that: (i) none of these government policies distinguishes between the imported and domestic products concerned or imposes any inherent disadvantage on imports; (ii) there is no causal connection between the alleged measures and any unfavourable competitive conditions; and (iii) the alleged measures as they exist today are unchanged or more favourable to imports as compared to the time of any relevant tariff concession.

6.23 The United States contends that the legal criteria suggested by Japan have no basis in the text of Article XXIII:1(b) or other WTO Agreements, any subsequent agreements of the Members, or the negotiating history of Article XXIII:1(b). To the extent that prior panel decisions support the application of Japan's rules, the United States contends that the disputes involved in those panel decisions presented significantly different facts and circumstances than those present in this dispute.

6.24 The United States suggests that Japan's purpose in proposing these rules is to preclude the Panel from seriously examining the liberalization countermeasures at issue in this dispute and thereby permitting Japan to evade responsibility for the measures that have impeded market access in Japan for imported film and paper for thirty years. In contrast, the United States proposes that the Panel consider this dispute in

the manner in which panels always have resolved disputes: on a case-by-case basis in consideration of all of the relevant facts and circumstances.

6.25 The United States notes that the Appellate Body in *Japan - Taxes on Alcoholic Beverages* stressed the importance of case-by-case analysis.[13] While the Appellate Body's comments were directed specifically at how a panel should conduct an Article III:2 inquiry, the United States argues that those comments, consistent with past precedent, are relevant to all disputes.[14] The United States alleges that Japan would prefer that the Panel avoid substantive consideration of the facts and circumstances in this dispute by applying Japan's fabricated, mechanical rules or adopting findings from other cases that are based on completely different facts and circumstances. The United States urges the Panel to address this dispute on its own merits in light of Article XXIII:1(b) and a thorough examination of the relevant facts and circumstances in this dispute.

3. SYSTEMIC IMPLICATIONS FOR WTO DISPUTE SETTLEMENT

6.26 In **Japan**'s view, this case has important implications for the WTO dispute settlement mechanism. Japan submits that the US non-violation claims are urging a dramatic expansion of what has historically been an exceptional and limited remedy. Japan notes that with one exception all previous non-violation cases involved tariff concessions and subsequent government actions that essentially undid the benefits accruing from those concessions.[15] In all these cases, the measures in dispute were essentially either tariff or product-specific subsidies which provided direct financial benefits to specific products. Therefore, it was obvious that the measures affected the competitive conditions of the products concerned. In all prior panels which found non-violation nullification or impairment, the complaining party showed a clear connection between the alleged measures and the unfavourable competitive position of the imported products.

6.27 The **United States** rejects Japan's accusation that the United States is seeking a "dramatic expansion" of the non-violation remedy under Article XXIII:1(b). The United States argues that what Japan claims to be a "dramatic expansion" is in fact nothing more than the legitimate exercise of the US right of redress under Article XXIII:1(b). In the US view, Article XXIII:1(b) of GATT provides a right of redress to a Member who considers that any benefit accruing under the Agreement is being nullified or impaired by the application of *any measure* whether or not it conflicts with the provisions of the Agreement.

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[13]"[W]e believe that an examination in any case of whether dissimilar taxation has been applied so as to afford protection requires a comprehensive and objective analysis of the structure and application of the measure in question on domestic as compared to imported products. ... Although it is true that the aim of a measure may not be easily ascertained, nevertheless its protective application can most often be discerned from the design, the architecture, and the revealing structure of a measure. . . . *In conducting this inquiry, panels should give full consideration to all the relevant facts and all the relevant circumstances in any given case"* (*Japan - Alcoholic Beverages*, WT/DS8/AB/R, p. 29, emphasis added).

[14]See, e.g., Panel Report on *European Economic Community Restrictions on Imports of Dessert Apples, Complaint by Chile*, adopted on 22 June 1989, BISD 36S/93, 123, para. 12.1 ("[The Panel] would take into account ... the particular circumstances of this complaint"); *Japan - Semi-Conductors*, BISD 35S/116, 154, para. 108 ("The Panel recognized that not all non-mandatory requests could be regarded as measures within the meaning of Article XI:1. Government-industry relations varied from country to country, from industry to industry, and from case to case and were influenced by many factors"); Panel Report on *Canada - Withdrawal of Tariff Concessions*, adopted on 17 May 1978, BISD 25S/42, 48, para. 17 ("The Panel came to the conclusion that a correct and reasonable interpretation of the GATT, in the particular circumstances applying in this case ...."); *Australia - Ammonium Sulphate*, BISD II/188, 192-193, para. 12 ("[T]he inequality created and the treatment that Chile could reasonably have expected at the time of the negotiation, after taking into consideration all pertinent circumstances, including the circumstances mentioned above...were important elements in the working party's conclusion").

[15]The exception is the case of the Panel Report on *European Economic Community - Tariff Treatment on Imports of Citrus Products from Certain Countries in the Mediterranean Region* ("EEC - Citrus Products"), GATT Doc. L/5776, 7 February 1985 (unadopted), p. 85, para. 4.27, which dealt with unbound tariffs on some products, and bound tariffs on other products.

The United States emphasizes that the language of Article XXIII:1(b) could not be written any more clearly, i.e., it sets *no* limitations on the types of measures that can be subject to scrutiny. Nor would such a limitation serve the purposes of Article XXIII:1(b). As noted by the *EEC - Oilseeds* panel, Article XXIII:1(b) provides a "right of redress" in the event that another Member nullifies and impairs a tariff concession.[16] Absent this right of redress, drafters feared that Members would be reluctant to make tariff concessions and GATT would no longer be useful as a legal framework for incorporating the results of trade negotiations.[17] Therefore, contrary to Japan's argument, the United States contends that it would be detrimental to the WTO system if the non-violation "remedy" were artificially limited to cases involving only subsidies and tariffs.

6.28 **Japan** states that neither contracting parties nor panels pushed to extend the non-violation concept beyond a limited range of cases, and the concept was applied consistently and with discipline only when specific requirements were met. Both the contracting parties and panels were justifiably concerned about the policy implications of an undisciplined expansion of the concept. The non-violation remedy was used as a tool to preserve the integrity of negotiated tariff concessions. If, however, the remedy were applied without proper restraints, in Japan's view, it could degenerate into a mechanism not for maintaining the agreed balance of tariff concessions between parties, but for imposing a de facto rearrangement of the established balance of tariff concessions in the complaining party's favour without any formal tariff negotiations. Thus, Japan argues that overuse of the non-violation remedy could perversely undermine, rather than preserve, the integrity of tariff concessions.

6.29 Japan concurs with the position taken by the United States in the *EEC - Oilseeds* proceeding, i.e. that the non-violation remedy should remain an exceptional concept and that any change of governmental policies, even if it has harmful trade effects, is not necessarily actionable under Article XXIII:1(b):

> "114. *The United States concurred in the proposition that non-violation nullification or impairment should remain an exceptional concept.* Although this concept had been in the text of Article XXIII of the General Agreement from the outset, a cautious approach should continue to be taken in applying the concept. *The United States did not consider that any change of governmental policies, even if it has harmful trade effects, constitutes non-violation nullification or impairment.* A contracting party does not have a reasonable expectation that a contracting party which grants it a tariff concession will not change general income tax rates."[18]

6.30 Moreover, Japan notes that in that case, the EEC also took the position that "recourse to the 'non-violation' concept under Article XXIII:1(b) should remain exceptional, since otherwise the trading world would be plunged into a state of precariousness and uncertainty".[19]

6.31 The **United States** notes that it continues to believe that the non-violation remedy remains an "exceptional concept" in that it provides a right of redress whether or not a measure conflicts with the GATT. There should be a "cautious approach" in applying this concept and that such caution is achieved by the Members' exercise of self-restraint and panels' application of the "detailed justification" requirement in Article 26.1 of the DSU. After 50 years, there have been only 8 cases *(i.e., Ammonium Sulphate, Sardines, Uruguayan Recourse, Citrus, Canned Fruit, Oilseeds, Semiconductors, and Sugar)* in which panels have substantively considered Article XXIII:1(b), and in three of those cases *(i.e., Uruguayan Recourse, Semiconductors, and Sugar)* the panel applied the "detailed justification" requirement that now appears in Article 26.1 of the DSU to dismiss frivolous non-violation claims. According to the United States, the EC made a similar argument in the *EEC - Oilseeds* case that an affirmative finding under

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[16]See *EEC - Oilseeds*, BISD 37S/86, 126-127, para. 144.

[17]Ibid., pp. 126-128, paras. 144 and 148.

[18]Ibid., pp. 117-118, para. 114 (emphasis added).

[19]Ibid., p. 117, para. 113

Article XXIII:1(b) would "plunge" the world "into a state of precariousness and uncertainty,"[20] which a decade later has not turned out to be the case. Most importantly, the United States continues to believe that panels should determine whether particular government policies constitute non-violation nullification or impairment on a case-by-case basis in light of all the relevant facts and circumstances. In this case, the United States emphasizes, the issue is not whether some unrelated social or economic policy is having an incidental effect on the film market. Rather, this case is about a concerted and coordinated effort by the Japanese Government directed at protecting its domestic film industry from import competition.

6.32 **Japan** points out that when the non-violation remedy is applied, the losing party - although it has fully complied with all of its GATT obligations, - must nonetheless make a "mutually satisfactory adjustment", i.e., either change policies or offer compensation, or else face the suspension of concessions by another WTO Member. Thus, the non-violation remedy has the practical effect of imposing a range of constraints on Members with respect to GATT-consistent measures similar to that which applies to measures that violate the GATT. Japan emphasizes that past panels have consistently construed the remedy narrowly, and applied the remedy in exceptional circumstances. Japan argues that these reasons apply with even greater force in the WTO framework which reaffirmed the limited nature of non-violation remedies.

a. First, Article 26.1(a) of the DSU imposes important limitations on the application and scope of the non-violation remedy. It makes clear the non-violation remedy should apply only when the complaining party has provided a "detailed justification in support of any complaint". Thus, the complaining party must meet a particularly high standard of justification for its complaint. In Japan's view, however, the US non-violation claims in this proceeding transparently fail to meet any of the established requirements for application of Article XXIII:1(b).

b. Second, even if a panel accepts the non-violation claim, the party complained about does not have to withdraw the measure at issue. Rather, Article 26.1(b) of the DSU specifically indicates that "there is no obligation to withdraw the measure". In Japan's view, the WTO Members were correctly wary of applying the extraordinary non-violation remedy unless there was a clear, compelling, and unambiguous basis for doing so; even then, they were not willing to oblige the party complained against to withdraw the measure.

6.33 The **United States** responds that the Panel should interpret Article XXIII:1(b) correctly, not broadly or narrowly, but consistently with the customary rules of international law. Thus, the United States argues that the Panel's task in this case is not different than in any other WTO dispute.

6.34 **Japan** submits that the reasons for a narrow construction of the non-violation remedy have grown even more cogent with the addition of other multilateral agreements to the GATT. Under GATT 1947, the non-violation remedy served the function of protecting GATT contracting parties' expectations with respect to tariff concessions from frustration by measures not subject to multilateral discipline. Now, as more and more areas have come within the scope of multilateral discipline, and the gaps in the scope of multilateral discipline have narrowed considerably, the need for the protection of benefits accruing under GATT 1994 by the non-violation remedy has become correspondingly less. For Japan, given the broad range of WTO agreements now in force, restraint in application of the non-violation remedy is more appropriate than ever before.

6.35 The **United States** replies that Japan's opinion on the utility of Article XXIII:1(b) is irrelevant to this Panel's determination of whether the US claim satisfies Article XXIII:1(b). Although the scope of the WTO disciplines has expanded beyond the original GATT disciplines, in the US view, the

[20]Ibid.

non-violation "safety net" is still needed for those measures that do not violate the WTO Agreements.[21] The United States emphasizes that the Uruguay Round negotiators recognized this need by adding a non-violation remedy to the GATS and the TRIPS Agreement (although the non-violation remedy will not be available under the TRIPS Agreement until the year 2000).

6.36 **Japan** contends that the US non-violation claims in this proceeding urge a dramatic expansion of the non-violation remedy because, in Japan's view, the United States asks that this exceptional remedy be applied beyond recognized and appropriate limits:

-not only to measures subsequent to the most recent tariff concessions, but also to alleged measures taken earlier and stretching back three decades;
-not only to measures unanticipated at the time of the relevant tariff concessions, but also to alleged measures already in effect and/or known about at the time the concessions were made;
-not only to government measures, but also to private conduct allegedly encouraged by government action;
-not only to legally binding requirements and their substantive equivalents, but also to non-mandatory requests and government reports;
-not only to current measures, but also to the allegedly continuing effects of past measures which are no longer in effect;
-not only to measures that draw distinctions between products and disadvantage imports, but also to alleged measures that make no distinctions between imported and domestic products;
-not only to measures which disadvantage imports, but also to measures which have no causal connection with competitive conditions unfavourable to imports;
-not only to adverse changes in policy since the time of the relevant tariff concessions, but also to policies that have stayed the same or even been liberalized.

6.37 Japan emphasizes that no binding GATT rules concerning private business practices or market structures has ever been established. The 1948 Havana Charter for an International Trade Organization (ITO) included a chapter on restrictive business practices, with obligations on governments. The ITO never came into existence and those rules were not carried over into the GATT. In 1958, the Contracting Parties decided to appoint a group of experts to study and make recommendations with regard to restrictive business practices in international trade. In 1960, the Report of the Group of Experts on "Restrictive Business Practices" was adopted by the Contracting Parties. In the Report, the Group was divided on the nature of further measures to be recommend but the majority first noted that there was no multilateral agreement on restrictive business practices.[22] Of greater relevance in this proceeding is the Report's further admonition for caution in this area.[23] Having considered the Report, the Contracting Parties adopted a Decision on Arrangements for Consultations in 1960, which did not refer to Article XXIII.[24] Japan further mentions that the WTO Members only took a tentative step to addressing issues

[21]As noted by Professors Jackson, Davey and Sykes in their textbook: "The discovery of new protective devices appears to be an endless process. As soon as the international system establishes restraints or regulations on a particular protective device, government officials and human ingenuity seem able to turn up some other measures to accomplish at least part of their protective purposes", Legal Problems of International Economic Relations, op. cit., p. 377.

[22]"The necessary consensus among countries upon which such an agreement could be based did not yet exist, and countries did not yet have sufficient experience of action in this field to devise an effective control procedure." Report of the Group of Experts on Restrictive Business Practices: Arrangements for Consultations, L/1015, adopted on 2 June 1960, BISD 9S/170.

[23]"However, the majority were convinced that, regardless of the question whether Article XXIII could legally be applied, they should recommend to the CONTRACTING PARTIES that they take no action under this Article. Such action would involve the grave risk of retaliatory measures under the provisions of paragraph 2 of that Article, which would be taken on the basis of judgments which would have to be made without adequate factual information about the restrictive practice in question, with consequent counter-productive effects on trade." Ibid., p. 172.

[24]Decision on Restrictive Business Practices: Arrangements for Consultations, adopted on 18 November 1960, BISD 9S/28. Japan notes that experts from the United States were part of the majority in that working party, and thus participated in making this specific recommendation.

such as competition and investment policies at the Singapore Ministerial Conference in December 1996. The Ministers reached a compromise to establish a working group to address the emerging issue of the interaction between trade and competition policy.[25] Japan recalls that there is still no consensus among the WTO Members on how to deal with the issue of the relationship between certain private business practices and their impact on trade. According to Japan, in particular the US claims regarding "distribution countermeasures" boil down to an attack against vertical relationships, e.g., single-brand wholesale distribution of film. However, vertical relationships may be pro-competitive or anticompetitive, depending on the circumstances of each case. While there is widespread consensus that horizontal agreements to fix prices are anticompetitive, and that they should be subject to legal restrictions, there is no such consensus about vertical restraints.[26] Accordingly, Japan urges the Panel to take a cautious approach in the examination of the US claims concerning alleged "distribution countermeasures" and not to engage itself in a rule-making exercise in this respect.

6.38 The **United States** responds that it is not challenging "private business practices" or "market structures" in this dispute, but measures of the Japanese Government. The specific measures at issue in this dispute are those listed in the US response to a Panel question (see Section III.A. supra). The term "any measure" in Article XXIII:1(b) is broad enough to encompass measures designed, promulgated, and applied by Councils, Committees, Centers, trade associations, and other quasi-governmental entities that have included private sector participants, acting under the authority or in concert with Japanese Government ministries and agencies. Although a market structure is not a measure *per se* within the meaning of Article XXIII:1(b), the steps taken by the Japanese Government to create and maintain an exclusionary market structure in the Japanese photographic materials sector do constitute measures. To this end, the characteristics of the market structure in the Japanese consumer film and paper market are clearly relevant in this dispute and provide compelling evidence of the Japanese Government's systematic efforts to impede market access for imported film and paper.

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[25]Specifically, the Singapore Ministerial Declaration states:

"Having regard to the existing WTO provisions on matters related to investment and competition policy and the built-in agenda in these areas, including under the TRIMs Agreement, and on the understanding that the work undertaken *shall not prejudge whether negotiations will be initiated in the future*, we also agree to: . . .

-establish a working group to study issues raised by Members relating to the interaction between trade and competition policy, including anti-competitive practices, *in order to identify any areas that may merit further consideration in the WTO framework* ...

The General Council will keep the work of each body under review, and will determine after two years how the work of each body should proceed. *It is clearly understood that future negotiations, if any, regarding multilateral disciplines in these areas, will take place only after an explicit consensus decision is taken among WTO Members regarding such negotiations".* Singapore Ministerial Declaration, adopted on 13 December 1996, WT/MIN (96)/DECEMBER, (emphasis added).

[26]Japan notes that this uncertainty has led Professor F.M. Scherer of Harvard University to conclude:

"Vertical restraints are recognized by both economists and competition policy authorities to have both benefits and competition-impeding costs. It is difficult to draw neat lines between those that should be allowed and those that should be prohibited. Even when those lines have been drawn, as my analysis of US antitrust policy toward automobile parts distribution has shown, enforcement of the vertical restraints law has been a muddle. *If nations have difficulty determining the correct policies and enforcing them within their own borders, it will surely be much more difficult to adjudicate such policies internationally.* This pessimistic conclusion may leave an occasionally significant barrier to international trade untouched. But wisdom in public policy analysis begins with the recognition that not all problems can be solved." F.M. Scherer, Retail Distribution Channel Barriers to International Trade, October 1995, p. 30, Working paper presented at a Columbia University Conference entitled The Multilateral Trading System of the 21st Century, Japan Ex. A-19. (emphasis added)

4. REMEDIES

6.39 The United States argues that in GATT jurisprudence, the remedy available depends upon the legal theory at issue: For "violation" disputes, DSU Article 19.1 provides that where the panel concludes that a measure is inconsistent with a covered agreement, it "shall recommend that the Member concerned bring the measure into conformity with that agreement". It is Japan's decision in the first instance to determine what steps it will take to eliminate the nullification or impairment resulting from its violation. In accordance with Article 19.1 of the DSU, however, the Panel could suggest that Japan take steps to undo the exclusionary aspects of the distribution system for photographic materials that its measures have brought about.

6.40 For disputes concerning non-violation nullification or impairment, Article 26.1 of the DSU provides that where the panel finds that a measure is nullifying or impairing benefits, it "shall recommend that the Member concerned make a mutually satisfactory adjustment". Pursuant to Article 26.1(c) of the DSU, an arbitrator may suggest "ways and means of reaching a mutually satisfactory adjustment". A mutually satisfactory adjustment in this dispute could involve either an effort by the Japanese Government to restore the competitive relationship between imported and domestic products or to grant compensation to the United States for the nullification or impairment of tariff benefits, although Japan has no obligation to withdraw the measures or provide compensation. If the parties fail to reach a mutually satisfactory adjustment, the panel's finding of nullification or impairment under Article XXIII:1(b) would entitle the United States to restore the original balance of concessions between the parties by suspending the application of appropriate obligations or concessions under the GATT 1994 and other WTO Agreements.

6.41 The United States submits that this Panel need not attempt to assess the quantum of nullification or impairment. In violation disputes, this becomes an issue only if the responding party pays compensation or the complaining party suspends concessions in accordance with Article 22.6 of the DSU, in which case the parties have recourse to arbitration if the level of suspension proposed is contested. In non-violation disputes, however, either party may request arbitration, in accordance with Article 26.(1)(c) of the DSU, to determine the level of benefits which have been nullified or impaired.

6.42 In Japan's view, the United States seems to be essentially requesting a type of affirmative action whereby primary wholesalers handling domestic brands, including Konica's subsidiaries, are forced to deal with Kodak as the "mutually satisfactory adjustment" in the case of non-violation claims or means to "bring the measures into conformity with the agreement" in the case of Article III claims. This is an extraordinary remedy which would involve this Panel in the restructuring of the Japanese distribution sector. For a Panel to make such a decision would be a radical expansion of the authority granted under the DSU.

B. RELEVANT TARIFF CONCESSIONS

1. GENERAL CONSIDERATIONS

6.43 The **United States** submits that Japan granted the following tariff concessions to the United States on photographic film and paper products in the Kennedy, Tokyo, and Uruguay rounds of multilateral trade negotiations.

ROUND	FILM		PAPER	
	B&W	Colour	B&W	Colour
Pre-Kennedy Round	30 %*	40%*	25 %*	40%*
Kennedy Round (1967)	15 %	40%*	12.5%	40%*
Tokyo Round (1979)	7.2%	4%	6.6%	4%
Uruguay Round (1994)	Free	Free	Free	Free

(* = Applied, not bound)

6.44 The United States claims that the three sets of policies - (i) distribution modernization policies, (ii) restrictions on large retail stores, and (iii) restrictions on promotional and marketing activities - individually and collectively "nullify or impair", within the meaning of Article XXIII:1(b), each of the tariff concessions that Japan granted on black and white and colour photographic film and paper in the Kennedy Round, Tokyo Round, and Uruguay Round.

6.45 **Japan** submits that the United States does not establish how the required elements for an non-violation claim are met with respect to the relevant tariff concessions on each of the four distinct products subject to this proceeding. In Japan's view, as regards black and white film as well as black and white paper, and the tariff concessions on these products, there is neither argument nor evidence how any of the alleged measures or the alleged results of these measures upset the competitive conditions for these products. The United States has not addressed these products specifically in terms of the alleged measures, the applicability of the alleged measures to the products or the effect of the alleged measures on the products. Japan argues that these products have unique characteristics from a retailing and marketing perspective. Furthermore, Japan emphasizes that imports of black and white film and paper rose dramatically almost immediately after the Kennedy Round tariff concessions, continued to rise throughout the period of the alleged liberalization "countermeasures" and did not peak until at least a decade after the last of the alleged measures. With foreign market share of black and white film peaking at 41.4 percent in 1985 and foreign market share of black and white paper peaking at 54.0 percent in 1989, Japan alleges that the United States tries to obscure any focus on these specific products.

6.46 Japan also contends that the United States has not distinguished the alleged measures and their effects on colour paper from the alleged measures and their effects on colour film. In Japan's view, the distribution system for colour paper differs significantly from that for colour film. Colour paper is sold to photofinishers, not retailers. For Japan there is no credible evidence that the alleged measures creating the market structure for film even addressed the market structure for distribution of colour paper.[27] Moreover, Japan asserts that there is no evidence that the US claims regarding large scale retail stores are applicable to colour paper. Thus, Japan contends that to the extent that the United States has tried to establish non-violation case, that case relates only to colour film, but fails to satisfy even a single element required under Article XXIII:1(b).

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[27] Japan submits that the only allegations relevant to paper are claims about SMEA financing to photofinishers. In Japan's view, even the United States admits this point. However, Japan recalls that it has raised procedural objections against these claims.

6.47 The **United States** argues that paragraph 1(b)(i) of GATT 1994 incorporated all of the protocols and certifications relating to tariff concessions that had entered into force under the GATT 1947 before the effective date of the WTO Agreement, including Japan's tariff concessions in the Kennedy and Tokyo Rounds. Thus, the United States asserts that the benefits accruing to it under these concessions, as well as the concessions arising from Japan's schedule attached to the Marrakesh Protocol, are GATT 1994 benefits. The United States argues that, in each Round, it bargained for the concessions and anticipated improved competitive opportunities. On each occasion, Japan granted a concession, but in the US view, then systematically sought to undermine its benefits, and the competitive relationship between imported and domestic photographic materials has been, and continues to be, upset as a result of Japan's measures.

6.48 **Japan** explains that the benefits of tariff concessions consist of the legitimate expectation of better market access opportunities created by the reduction of bound tariff rates as well as the legitimate expectation that the value of the concession will not be frustrated. Since the negotiation of successive tariff concessions provides an opportunity for any alleged frustration of expectations created by prior tariff concessions to be addressed, in Japan's view, it should be presumed that such frustration will also be taken into account by the parties during subsequent negotiations. Therefore, as long as the new balance of tariff concessions has been actually negotiated and agreed upon, the result of the latest tariff negotiation should be deemed to have created a new expectation concerning the balance of tariff concessions and to have replaced any reasonable expectation that arose under a prior tariff negotiation. Since the tariff concessions on photographic film and paper in the present case have been actually negotiated and granted at reduced rates under three successive rounds, the Uruguay Round tariff concessions should be deemed to have replaced all previous expectations and formed a new balance of tariff concessions. Japan thus argues that the presumption should be that any alleged frustration of expectations relating to prior concessions has already been incorporated into the new balance of tariff concessions as the result of the latest tariff negotiations under the Uruguay Round. Therefore, as to the issue whether rights and expectations from the earlier concessions survive even when during each subsequent round further tariff reductions are negotiated and granted, Japan believes that the "benefit accruing ... under the Agreement" is limited to the benefit of the Uruguay Round tariff concessions. Accordingly, in Japan's view, the benefits of the Kennedy Round and Tokyo Round negotiations are irrelevant in this case.

6.49 Japan also maintains that the results of the latest tariff negotiations in the Uruguay Round have removed any reasonable expectations of the benefits that arose under prior tariff negotiations and have created new expectations concerning the balance of tariff concessions. The benefits of (or the expectations relating to) the tariff concessions of 1967 and 1979 themselves should, in Japan's view, be deemed to be past benefits (or expectations) under GATT 1947. Accordingly, Japan argues that their nullification or impairment (or their alleged frustration) cannot constitute a situation where "any benefit accruing ... under this Agreement [i.e., GATT 1994] is being nullified or impaired".

6.50 As to the relevance of different protocols embodying tariff concessions, the **United States** submits that Article XXIII provides that a Member has a "non-violation" claim if it considers that "any *benefit* accruing to it directly or indirectly under this Agreement is being nullified or impaired ...". Article 31 of the Vienna Convention on the Law of Treaties instructs that this language "shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in light of its object and purpose". According to Article 31, the ordinary meaning of a treaty term is to be interpreted in context and by taking into account "any subsequent agreement between the parties regarding the interpretation of the treaty of the application of its provisions".

6.51 The United States claims that the "benefits" at issue in this dispute are the market access opportunities arising from Japan's Kennedy Round, Tokyo Round, and Uruguay Round tariff concessions on consumer photographic film and paper. In the US view, nothing in the Kennedy Round, Tokyo Round or Uruguay Round tariff protocols suggests that the tariff concessions attached thereto would be "deemed" to have expired or to have been withdrawn at a specific time or as a result of a specific event or by virtue of a subsequent tariff agreement.

6.52 The United States further explains that the object and purpose of the non-violation remedy is to encourage tariff concessions under Article II of GATT. In the US view, a finding by this panel that a Member's reasonable expectations from an existing tariff concession are extinguished as soon as it receives a new tariff concession would have the opposite effect. Members would be reluctant to enter into new negotiations and the negotiations themselves would become impossibly burdensome. Members would be compelled to initiate and complete non-violation disputes on all suspected instances of nullification or impairment prior to negotiating new tariff concessions. Alternatively, Members would abandon the formulaic approach to tariff cuts first adopted in the Kennedy Round in favour of product-by-product negotiations to redress the nullification or impairment of prior concessions and attempt to pursue further tariff liberalization simultaneously.

6.53 **Japan** requests that the United States should not be allowed to rely on tariff concessions arising from previous rounds of tariff negotiations because this would undermine the integrity and stability of negotiated tariff concessions. Japan points out that a country may adopt a measure which is consistent with the WTO Agreement but somehow nullifies or impairs a benefit accruing to another WTO Member. In that case, an "aggrieved" country could sit on its rights for decades. Round after round of subsequent tariff negotiations on the product in question would have occurred, and still the "aggrieved" party would do nothing. And yet, decades later, the "aggrieved" party could at long last decide to assert its rights and expect a panel to find in its favour.

6.54 The **United States** rejects Japan's suggestion that, if this Panel affirms that tariff concessions and reasonable expectations arising therefrom continue to exist unless the concession is modified or withdrawn under Article XXVIII, Members would "sit on their rights for decades". The United States responds that the purpose of WTO dispute settlement is remedial, not punitive, and therefore WTO dispute settlement provides only prospective relief. As a consequence, Members have no incentive to delay in bringing a dispute once they discover that another Member is violating an agreement or otherwise nullifying or impairing its tariff concessions within the meaning of Article XXIII:1(b). While, in the US view, this discovery could take years, a Member's right of redress should not be extinguished because the nullifying and impairing measures are hard to detect.

2. PAST GATT PANEL REPORTS

6.55 The United States submits that two prior panels have found nullification or impairment of tariff benefits that were granted in a tariff negotiation that was succeeded by multilateral tariff negotiations, i.e., *EEC - Canned Fruit*[28] and *EEC - Oilseeds*.[29] According to the United States, these two panel decisions support its position and there are none to the contrary. The United States explains that the panel on *EEC - Canned Fruit* found that the United States had a reasonable expectation arising from the EC's 1974 tariff concessions pursuant to Article XXIV:6 negotiations and 1979 Tokyo Round tariff concessions.[30] In the view of the United States, the panel on *EEC - Oilseeds* found that the United States had a reasonable expectation arising from the EC's 1962 Dillon Round tariff concessions.[31] The United States notes that these disputes were initiated in 1982 and 1988, respectively, subsequent to the 1979 Tokyo Round multilateral tariff negotiations. The United States also mentions that neither the EC nor the panels questioned whether the Tokyo Round negotiations created a new balance of tariff concessions that extinguished US reasonable expectations with respect to prior tariff concessions. Rather, the EC argued only that it had withdrawn tariff concessions pursuant to Article XXIV:6 and Article XXVIII negotiations

[28]GATT Doc. L/5778, 20 February 1985 (unadopted).

[29]Adopted on 25 January 1990, BISD 37S/86.

[30]The panel found separately that the United States could have anticipated certain subsidies in respect of the 1979 tariff concessions. See *EEC - Canned Fruit*, L/5778, p. 17, para. 49.

[31]See *EEC - Oilseeds*, BISD 37S/86, pp. 126-128, paras. 144-146.

and thereby extinguished US reasonable expectations with respect to those particular concessions. The United States concludes that these findings would not have been possible if subsequent multilateral tariff agreements or enlargement agreements were deemed to extinguish wholesale the tariff concessions in prior tariff schedules.

6.56 In **Japan**'s view, its position with respect to the relevant tariff concessions to be considered in an non-violation case is consistent with the reasoning of the panel on *EEC - Oilseeds*. The facts before that panel were that the tariff concessions for oilseeds (duty-free tariff bindings) had been originally made in 1962. During successive tariff negotiations under Article XXIV:6 of GATT 1947, these duty-free tariff bindings were maintained at the same level. The panel examined "whether benefits accruing to the United States under the tariff concessions presently in force [at the time of the panel deliberations] include the protection of expectations that prevailed in 1962 when tariff concessions ... were originally incorporated" into the Schedule.[32] Noting that "[Article XXIII:1(b)], as conceived by the drafters and applied by the CONTRACTING PARTIES, serves mainly to protect the balance of tariff concessions", that panel found that:

> "... the answer to the question of whether the expectations of 1962 continue to be protected depend on whether the concessions on oilseeds resulting from the subsequent renegotiations under Article XXIV:6 were part of a *new balance of concessions* or whether the reinstitution of the concessions at the same rate after the successive enlargements of the Community meant that the balance of concessions originally negotiated in 1962 was to be continued ... The result of the Article XXIV:6 negotiations following the successive enlargement of the Community was not the creation of a new common external tariff but the extension of the existing tariff concessions ...".[33]

6.57 Japan distinguishes the facts in the *EEC - Oilseeds* case from those in the present one as follows: In the *EEC - Oilseeds* case, the balance of tariff concessions originally granted with duty-free tariff bindings was continued throughout the successive tariff concessions. In the present case, by contrast, Japan agreed to reduce its bindings on colour film, black and white film, and colour paper from 3.7 percent to zero, and its binding on black and white paper from 6.6 percent to zero in the Uruguay Round tariff negotiations. The *EEC - Oilseeds* panel also suggested that a new balance of concessions would involve a "global reassessment of the value" of all of a party's concessions.[34] The Uruguay Round was a process of such a "global reassessment of value" of tariff concessions. Therefore, in Japan's view, the reasoning of the panel on *EEC - Oilseeds* leads to the conclusion that the result of the Uruguay Round tariff negotiations was the creation of a new balance of tariff concessions on the products at issue in this case.

6.58 The **United States** submits that the first *EEC - Oilseeds* case of 1989 focused on the expectations flowing from a 1962 concession by the EC (the zero binding on oilseeds). The EC argued that because negotiations had been conducted since 1962 under Article XXVIII procedures (through the route of Article XXIV:6) concerning the EC Schedule, the expectations that had to be taken into account were the expectations as of the most recent such negotiation in 1986. According to the United States, the panel on *EEC - Oilseeds* correctly rejected that argument, noting that the practice of the Community in each enlargement had been to extend the application of its pre-existing common customs tariff (CCT) to include the territory of its new member States. Where the application of the CCT resulted in the impairment of tariff concessions in the schedules of the acceding member States, the Community (acting on behalf of its member States) discharged its obligations under Article XXVIII and paid compensation by lowering duty rates on certain items for the EC as a whole. However, none of the enlargements ever modified or withdrew the particular CCT concession on oilseeds made in 1962. Thus, even though the EC substituted successive Schedules for the 1962 Schedule of the EEC of Six, the concession on oilseeds

[32]Ibid., pp. 126-127, para. 144.

[33]Ibid., pp. 126-127, paras. 144-145 (emphasis added by Japan).

[34]Ibid., pp. 126-127, para. 145.

made in 1962 had never itself been modified or withdrawn. For the United States, it was therefore the expectations of 1962 that were relevant, not the expectations of 1986 or any other year after 1962.

6.59 **Japan** contests the US conclusion that the panel on *EEC - Oilseeds* rejected the EC argument that the expectations which had to be taken into account were the expectations of the most recent tariff negotiation under Article XXIV:6 because none of the enlargements ever modified or withdrew the particular common customs tariff concession on oilseeds made in 1962. Japan explains that the findings of the panel on *EEC - Oilseeds* need to be looked at in the proper context. From the reference that "the answer to the question of whether the expectations of 1962 continue to be protected depends on whether the concessions on oilseeds resulting from the subsequent renegotiations under Article XXIV:6 were part of a new balance of concessions or whether ... the balance of concessions originally negotiated in 1962 was to be continued", it is clear for Japan that the panel focused on the issue of whether or not a new balance of concessions was created, and not on the issue of the procedures and the formalities of the tariff negotiation. Japan maintains that the panel on *EEC - Oilseeds* also referred to the issue of whether or not the tariff negotiation at issue involved a "global reassessment of the value of all the Community's concessions". Japan insists that its argument is consistent with this analysis by the *EEC - Oilseeds* panel, while the US argument is not.

3. THE TYPES OF TARIFF NEGOTIATIONS UNDER GATT

6.60 As to the issue whether the legal relationship between tariff concessions bound in the Uruguay Round, Tokyo Round and Kennedy Round schedules differs depending on whether tariff bindings derive from tariff negotiations or re-negotiations under Articles XXIV:6, XXVIII and XXVIII*bis*, the **United States** describes its position as follows: Under the GATT 1947, each new Schedule of a contracting party coexisted legally with all prior Schedules. Each of the concessions in each Schedule remained legally binding except to the extent it had been modified or withdrawn under Article XXVIII. Since the GATT 1947 Schedules were incorporated into the GATT 1994, the concessions in the GATT 1947 Schedules remain legally binding and coexist with the concessions in the Uruguay Round schedules and all subsequent schedules entered into under the GATT 1994.[35]

6.61 With respect to the legal relationship among Article XXIV:6 negotiations, the modification of Schedules under Article XXVIII, and the types of tariff negotiations stipulated by Article XXVIII*bis*, **Japan**'s view is that the legal nature of tariff negotiations or the modification of schedules in relation to non-violation complaints needs to be evaluated based on the substance of whether the new balance of concessions has been formed.

(a) Article XXVIII

6.62 The **United States** points out that GATT provides only one generally-available legal means for modifying or withdrawing, i.e. "re-negotiating" a tariff concession, which is Article XXVIII. A Member may invoke Article XXVIII only under specifically defined circumstances. The United States elaborates that a Member may modify or withdraw a concession by negotiation and agreement under Article XXVIII:1-3 during the triennial "open season". A Member may enter into negotiations for modification or withdrawal of a concession under Article XXVIII:4 if so authorized. A Member may modify or withdraw a concession in accordance with the procedures of Article XXVIII:1-3 if it has made a timely reservation of rights to do so under Article XXVIII:5.

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[35]The United States also mentions that the initial negotiating rights attached to GATT 1947 concessions remain in force today and that the party which initially negotiated any given concession, even a concession from 1947, retains a right to be consulted and compensated if that concession is modified or withdrawn today.

6.63 The United States contends that Japan has made various sets of tariff concessions in various Schedules attached to protocols after trade negotiating rounds. The later concessions have not had the legal effect of modifying or withdrawing the earlier concessions, because Japan has never invoked Article XXVIII with respect to its concessions on film and paper. The United States maintains that all of Japan's concessions on film and paper therefore remain in effect, and the expectations attached to each remain protected by Article XXIII:1(b).

6.64 With regard to the modification or withdrawal of the concessions on specific products contained in the schedule of an individual WTO Member made under Article XXVIII, **Japan** explains that the Member which proposes to modify or withdraw the concession negotiates compensation with respect to other products with other Members in order to "maintain a general level of reciprocal and mutually advantageous concessions". Therefore, the legal nature of modification or withdrawal under Article XXVIII should be deemed as the continuation of the balance of tariff concessions as a whole. Japan also states that the procedure set forth in Article XXVIII also applies to the modification of the schedules for the Article XXIV:6 negotiations.

(b) Article XXIV:6

6.65 The **United States** submits that Article XXIV:6 permits a Member which has entered into a customs union and which proposes to increase a rate of duty above bound levels to modify or withdraw that concession under the procedures of Article XXVIII.[36] The United States points out that Article XXIV:6 thus does not provide an independent route to modification of concessions with independent procedures, but merely a means to invoke the standard procedures of Article XXVIII outside of an "open season".

6.66 **Japan** contends that the negotiations under Article XXIV:6 are conducted to extend the existing common external tariff of a customs union to their new member(s), on the premise that "the duties ... shall not on the whole be higher or more restrictive than the general incidence of the duties ... applicable in the constituent territories" (Article XXIV:5). Although the negotiations will lead to the modification of the part of the schedules of the customs union, the legal nature of the negotiations under Article XXIV:6 should be deemed as the continuation of the prior balance of tariff concessions as a whole. In this connection, Japan points out that the panel on *EEC - Oilseeds* found that "the result of the Article XXIV:6 negotiations following the successive enlargements of the Community was ... the extension of the existing tariff concessions of the Community to the new member States" and that the balance of tariff concessions originally made was to be continued.

[36]The United States elaborates that Article XXIV:6 was added to the General Agreement in 1948 to accommodate a customs union between France and Italy. Analytical Index (1995), p. 810. At the time, the text of Article XXVIII barred any modification of schedules until 1 January 1951. See: Final Act Adopted at the Conclusion of the Second Session of the Preparatory Committee of the United Nations Conference on Trade and Employment, Vol. 1, pp. 61-62. France sought the addition of Article XXIV:6 because of the timing element in Article XXVIII. France needed to be able to invoke the procedures of Article XXVIII immediately so that it could raise duties consistent with its legal obligations.

(c) Article XXVIII*bis*

6.67 The **United States** argues that, by its terms, Article XXVIII*bis*[37] provides a legal basis for adding concessions to Schedules, but not a basis for modifying or withdrawing pre-existing concessions.[38] Tariff negotiating rounds in GATT were always conducted as occasions for reducing or eliminating tariffs, not as opportunities for contracting parties to throw the pre-existing level of trade liberalization into uncertainty and renegotiate their schedules. When concessions have been modified or withdrawn during a round of trade negotiations, the modification or withdrawal has taken place through invocation of Article XXVIII itself, not Article XXVIII*bis*.[39] According to the United States, there are only two exceptions to the general rule that tariff negotiations add, and do not subtract, concessions, but these exceptions prove the rule:

6.68 First, the Protocol Embodying the Results of the 1960-61 Tariff Conference ("Dillon Round Protocol") included a special paragraph found in no other GATT tariff protocol. Under this paragraph, in each case where certain schedules provided for treatment for a product less favourable than that provided in a pre-existing schedule applicable to the same contracting party, the provision in the earlier schedule would be terminated.[40] However, there is no similar provision in the Kennedy Round protocol or Tokyo Round protocol, and, in any event, this circumstance would not apply to Japan's reductions of its tariffs for photographic film and paper.

6.69 Second, during the Uruguay Round, certain developing country participants offered to make ceiling bindings on all products or entire product sectors in their schedules. During the final tariff negotiations in the spring of 1994, in almost all instances these participants agreed not to modify or withdraw pre-existing bindings at lower duty rates in their GATT 1947 schedules. However, four participants did modify or withdraw such bindings: Egypt, Peru, South Africa and Uruguay. To provide the legal basis for such modification or withdrawal, paragraph 7 was added to the Marrakesh Protocol, using language borrowed from the Dillon Round Protocol. Paragraph 7 provides that these four Members "shall be deemed to have taken appropriate action as would otherwise have been necessary under the relevant provisions of GATT 1947 or 1994". The United States concludes that paragraph 7 of the Marrakesh Protocol was legally necessary to ensure that the more favourable earlier concessions of Egypt, Peru, South Africa and Uruguay would not continue to be legally binding, and to make it possible for these four Members to liquidate their prior inconsistent tariff concessions. However, the United States emphasizes that this provision by its terms applies only to the four Members listed therein, whereas all other countries continue to be bound by all prior concessions in GATT 1947 schedules.

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[37] Article XXVIII*bis* was added to the GATT in 1955 and entered into force on 7 October 1957.

[38] Concessions also have been added to Schedules under other legal bases: through the four rounds of tariff negotiations that took place before 1957, through exchanges of concessions in accession tariff negotiations, and through the Procedures for Modification and Rectification of Schedules (which were utilized, for example, in the case of the recent Information Technology Agreement). See 26 March 1980, CONTRACTING PARTIES' Decision on Procedures for Modification and Rectification of Schedules of Tariff Concessions, BISD 27S/25.

[39] The United States mentions the following examples:

(i) The EC's 1994 modification of its concession on bananas was carried out not under the authority of the Punta del Este Declaration but pursuant to an invocation of Article XXVIII. Panel Report on *European Communities - Regime for the Importation, Sale and Distribution of Bananas*, circulated on 22 May 1997, para. 3.31; Article XXVIII notification in SECRET/343, referenced in Analytical Index (1995) p. 979.

(ii) The negotiation of the common external tariff of the EEC which took place in the Dillon Round took place in accordance with the provisions of Articles XXVIII:1-3 and XXIV:6. BISD 8S/112, para. 18.

(iii) When Denmark, Ireland and the United Kingdom acceded to the EC in 1972, the EC carried out negotiations under the procedures of Article XXVIII (invoked through Article XXIV:6), not as part of the Tokyo Round tariff negotiations.

[40] BISD 8S/8, 9, para. 4.

6.70 In **Japan**'s view, the types of tariff negotiations stipulated by Article XXVIII*bis* are "directed to the substantial reduction of the general level of tariffs", "with due regard to the objectives of the GATT and the varying needs of individual Members", as opposed to the modification and withdrawal under Article XXVIII, which is a process of "maintaining a general level of reciprocal and mutually advantageous concessions". Tariff negotiations under Article XXVIII*bis* should be deemed to be conducted from scratch, taking into account the various circumstances at the time regarding the products concerned. When the reduction or elimination of tariff concessions are negotiated and agreed upon in those tariff negotiations, they should be deemed to have created a new balance of concessions, and a new expectation concerning the balance of tariff concessions created by the latest negotiations should be deemed to have replaced any previous expectation under prior concessions. In particular, any multilateral trade negotiation round like the Kennedy Round, the Tokyo Round and the Uruguay Round, should be deemed a process of creating a "new balance of concessions" as a whole, by making a global reassessment of the value of the concessions through the comprehensive tariff negotiations on a broader basis. Accordingly, Japan maintains that the measures existing prior to the new concessions, which should be deemed to be taken into account during such negotiations, will not nullify or impair benefits under Article II of GATT.

6.71 The **United States** responds that Japan's argument that Article XXVIII*bis* negotiations - but not Article XXVIII or XXIV:6 negotiations - create a new balance of tariff concessions that extinguishes previous expectations under prior concessions is exactly backwards. In the US view, Article XXVIII*bis* negotiations do create a new balance of tariff concessions with new expectations relating to tariff concessions arising out of those negotiations. However, because Article XXVIII*bis* negotiations cannot and do not withdraw or modify prior tariff concessions, such negotiations cannot extinguish or affect the expectations relating to those prior tariff concessions. In contrast, when a Member withdraws or modifies a tariff concession under Article XXVIII - either directly under Article XXVIII or through the route of Article XXIV:6 - the Member may be changing the legal obligation that the tariff concession represents and as a consequence the reasonable expectations associated with those concessions would necessarily change and a new balance of concessions would be achieved with respect to that round of tariff concessions.

6.72 The United States submits that the panel report on *EEC - Oilseeds* fully supports its position:

> "In these circumstances, the partners of the Community in the successive renegotiations under Article XXIV:6 could legitimately assume, in the absence of any indications to the contrary, that the offer to continue a tariff commitment by the Community was an offer not to change the balance of concessions previously attained. The Panel noted that nothing in the material submitted to it indicated that the Community had made it clear to its negotiating partners that the withdrawal and reinstitution of the tariff concessions for oilseeds as part of the withdrawal of the whole of the Community Schedule meant that the Community was seeking a new balance of concessions with respect to these items. There is in particular no evidence that the Community, in the context of these negotiations, offered to compensate its negotiating partners for any impairment of the tariff concessions through production subsidies or that it accepted compensatory tariff withdrawals by its negotiating partners to take into account any such impairment. The balance of concessions negotiated in 1962 in respect of oilseeds was thus not altered in the successive Article XXIV:6 negotiations. The Panel therefore found that the benefits accruing to the United States under the oilseed tariff concessions resulting from the Article XXIV:6 negotiations of 1986/87 include the protection of reasonable expectations the United States had when these concessions were initially negotiated in 1962."[41]

[41] *EEC - Oilseeds*, BISD 37S/86, 127-128, para. 146.

For the United States, the quoted text shows that the panel on *EEC - Oilseeds* found that even though the tariff concessions on oilseeds had been withdrawn and re-instituted intact, pursuant to Articles XXIV:6/Article XXVIII (actions that cannot occur under Article XXVIII*bis*), no new balance of concessions had been achieved.

6.73 **Japan** responds that the parties differ with respect to the criterion of judgement over when a new expectation should be deemed created regarding tariff concessions. In Japan's view, the United States refers to the procedures and the formalities of whether or not a tariff negotiation was conducted in accordance with Article XXVIII of GATT and whether or not a bound tariff rate was increased. Japan considers what the United States points out may only mean that certain tariff concessions will result in the expectation that customs duties will not be applied in excess of the bound rates, and that such expectations can continue unless the concessions will be modified or withdrawn under Article XXVIII. Japan does not disagree, since it certainly would not argue that a Member can negate its commitments on tariff bindings unilaterally. On the contrary, Japan believes that every Member is bound by its tariff concessions irrespective of the procedures and the formalities followed.

6.74 However, which expectations created by previous tariff concessions should be taken into account in the examination of non-violation claims, in Japan's view, is a completely different issue. In this respect, Japan takes the position that the criterion to be used should not be whether or not the level of the tariff binding has been increased or reduced, but whether or not a new balance of tariff concessions has been created as a result of multilateral or sector-specific tariff negotiations, in which various circumstances including non-tariff measures (e.g., domestic subsidies) relating to the products subject to negotiation are taken into account. In Japan's view, what needs to be examined regarding the expectation arising out of certain tariff concessions in relation to the issue of the "benefit" for the purpose of a non-violation case is the following: When the surrounding situations are changed because of the introduction of a certain measure, which expectations created by previous tariff concessions should be taken into account in evaluating the impact of the change in situations.

6.75 Japan reiterates that the *Oilseeds* panel stated that "the answer to the question of whether the expectations of 1962 continue to be protected depends on whether the concessions on oilseeds resulting from the subsequent renegotiations under Article XXIV:6 were part of a new balance of concessions or whether ... the balance of concessions originally negotiated in 1962 was to be continued". From this reference, in Japan's view, it is clear that the panel focused on the issue of whether or not a new balance of concessions was created and not on the issue of procedures and the formalities of the tariff negotiation. Japan also emphasizes that the *Oilseeds* panel also referred to the issue of whether or not the tariff negotiation at issue involved a "global reassessment of the value of all the Community's concessions".

4. THE INCORPORATION CLAUSE OF GATT 1994

6.76 The incorporation clause of GATT 1994 provides in the relevant parts:

"1.The General Agreement on Tariffs and Trade 1994 ("GATT 1994") shall consist of: ...
(b)the provisions of the legal instruments set forth below that have entered into force under GATT 1947 by the date of entry into force of the WTO Agreement:
(i)protocols and certifications relating to tariff concessions; ...
(d)the Marrakesh Protocol to GATT 1994".

6.77 The **United States** submits that prior to the Uruguay Round, Japan made tariff concessions on film and paper in the Kennedy Round and Tokyo Round. Those concessions are now part of GATT 1994 by virtue of paragraph 1(b)(i) of GATT 1994, which incorporated all of the protocols and certifications relating to tariff concessions that had entered into force under the GATT 1947 before the effective date of the WTO Agreement, including Japan's tariff concessions in the Kennedy and Tokyo Rounds.

Therefore, the United States claims that the benefits accruing directly or indirectly under GATT 1994 within the meaning of Article XXIII:1 include the benefits that the United States reasonably expected to receive from Japan's Kennedy Round and Tokyo Round concessions, as well as the concessions arising from Japan's schedule attached to the Marrakesh Protocol. All of them give rise to expectations of improved market access for which the General Agreement provides a right of redress in the event that expectations are frustrated under Article XXIII:1(b).

6.78 In support of its position that the only tariff concessions embodied in the Uruguay Round Schedule can be relied on for purposes of non-violation complaints under Article XXIII:1(b), **Japan** submits that paragraph 1 of the GATT 1994 provides that the GATT 1994 shall consist of, among others, "protocols and certifications relating to tariff concessions" which "entered into force under the GATT 1947" (paragraph 1(b)(i)), but also includes sub-paragraph (d), which refers to "the Marrakesh Protocol to GATT 1994". In Japan's view, this provision means that the effective concessions included in the Schedules of the Members annexed to these prior protocols and certifications, and the concessions newly agreed as a result of the Uruguay Round negotiations, as a whole, constitute tariff concessions which are applied under the GATT 1994.

6.79 Japan argues that, since paragraph 1 does not provide for a hierarchy among sub-paragraphs (a) to (d), it must be read as a whole so that each sub-paragraph is applied and interpreted in a manner consistent with the others. Accordingly, paragraph 1 must be read so that the earlier protocols and certifications referred to in paragraph 1(b)(i) of GATT 1994 do not undermine the most recent balance of concessions agreed among the WTO Members and included in their Schedules to the Marrakesh Protocol. Therefore, when there is any difference between the concessions contained in the schedules annexed to the Marrakesh Protocol and those in the schedules annexed to prior protocols and certifications referred to in paragraph 1(b)(i) of GATT 1994 (e.g., when the concessions on the same products are different), in Japan's view, the concessions contained in the schedules annexed to the Marrakesh Protocol prevail as a later agreement and shall be applied to WTO Members pursuant to Articles I and II of GATT. For Japan, allowing prior protocols and certifications to alter the agreed balance of concessions in the Marrakesh Protocol would detract from stability and certainty among the parties to GATT in their trading relations.

6.80 The **United States** responds that Japan, in arguing that concessions in the schedules annexed to the Marrakesh Protocol prevail over concessions in other tariff protocols as a "later agreement", appears to be relying on the principle provided in Article 30 of the Vienna Convention on the Law of Treaties, although it does not state this affirmatively. Article 30(1) of the Vienna Convention deals with "the rights and obligations of parties to successive treaties relating to the same subject-matter" and provides generally that where the earlier treaty has not been terminated, "the earlier treaty applies only to the extent that its provisions are compatible with those of the latter treaty". However, the United States contends that Article 30 does not apply to the situation before this Panel because this case is not about "successive treaties" but about coexisting treaties which must be interpreted so as to give effect to each.

6.81 The United States explains that the effect of the GATT 1994 incorporation clause was to create a new legal instrument, the "GATT 1994"[42] which was contemporaneous with the other legal instruments attached to the WTO Agreement. Under the GATT 1994 incorporation clause, "GATT 1994" is composed of a number of elements including, *inter alia*, the Marrakesh Protocol and other tariff protocols. Through the GATT 1994 incorporation clause, WTO Members agreed anew to each element of "GATT 1994" and each such element is contemporaneous with each other such element. Although

[42]The United States explains that it was for this reason that the General Interpretative Note to Annex 1A was inserted into the text of the WTO Agreement in the fall of 1993, as part of the decision to include the GATT in the WTO Agreement through an incorporation clause. The negotiators wished that Annex 1A agreements other than the GATT 1994 take precedence over the GATT 1994 in the event of conflict. Absent the General Interpretive Note to Annex 1A, this would not have occurred because the effect of the incorporation clause was to make the entire "GATT 1994" contemporaneous with the other agreements, so that Article 30 of the VCLT would not have achieved the desired result.

GATT 1947 has been terminated, the tariff protocols done under GATT 1947 remain legally binding solely because they are part of GATT 1994. Thus, Article 30(3) of the Vienna Convention does not apply to the relationship between these tariff protocols and the other elements comprising GATT 1994. Therefore, for the United States neither Article 30 of the Vienna Convention nor the principle expressed therein establishes any hierarchy between the various tariff protocols within "GATT 1994". In any event, the United States points out that the general principle reflected in Article 30 of the Vienna Convention cannot be read to override the specific rule established by the GATT 1994 incorporation clause. In the US view, even if Article 30 did apply, the concessions annexed to the Marrakesh Protocol are fully compatible with the concessions in the other tariff protocols in GATT 1994, because there is no "conflict" between tariff concessions unless a subsequent concession is less favourable than a prior concession.

6.82 According to the United States, Japan argues that the GATT 1994 incorporation clause does not constitute an express agreement between Members to ensure the continuing existence of tariff concessions relating to GATT 1947. The United States responds that paragraph 1(b)(i) of that clause cannot be read so as to undermine paragraph 1(d) which refers to the Marrakesh Protocol of GATT 1994. The United States emphasizes that no subsequent instrument suggested that the Members had agreed to the withdrawal of Japan's Kennedy Round and Tokyo Round tariff concessions. In the US view, the GATT 1994 incorporation clause provides to the contrary. In the US view, Japan has presented no reasons why this Panel's recognition that Japan's Kennedy Round and Tokyo Round tariff concessions on film and paper continue to exist would undermine the Marrakesh Protocol. For the United States, to reach any other conclusion defies the ordinary meaning of the GATT 1994 incorporation clause and Article XXIII:1 of GATT 1994.

5. CERTIFICATION OF MODIFICATIONS AND RECTIFICATIONS

6.83 **Japan** submits that the Certification of Modifications and Rectifications to Schedule XXXVIII - Japan to GATT 1994, dated 8 February 1996, states that "[t]his Schedule replaces all prior Schedules XXXVIII to the General Agreement on Tariffs and Trade 1994 ... on the date that this Schedule becomes effective". This Certification, containing Japan's Schedule annexed to the Marrakesh Protocol, as modified in accordance with the 1996 Harmonized Commodity Description and Coding System ("Harmonized System"), is a part of the WTO Agreement. The provisions of the Certification, including the reference to the replacement of prior schedules, are legally effective. Japan further notes that no objection was raised by any Member to this specific provision during the procedures of the modifications and rectifications to Schedule XXXVIII - Japan, which has been completed in accordance with a Decision on Procedures to Implement Changes in the Harmonized System.[43] Accordingly, Japan claims that its schedule currently legally effective under GATT 1994 has "replaced" the prior tariff concessions under GATT 1947.

6.84 According to the **United States**, Japan argues that the 1996 "Certification of Modifications and Rectifications to Schedule XXVIII - Japan to the GATT 1994" constitutes a subsequent agreement between the parties to the effect that Japan was withdrawing all of its prior tariff concessions. However, in the US view, this Certification may replace Japan's prior schedules - but it does not withdraw its prior concessions as attested to by Japan's representation that the certification was made "in conformity with the 8 October 1991 CONTRACTING PARTIES Decision on Procedures to Implement Changes in the Harmonized System (8 February 1991)". This decision makes clear that the parties did not intend for schedules submitted to implement changes in the Harmonized System to have any substantive effect on prior tariff concessions. In the US view, the submission of a Schedule pursuant to this Decision does not substitute for a proper invocation of Article XXVIII. The United States further maintains that Japan did not invoke Article XXVIII to modify or withdraw tariff concessions on consumer photographic film and paper.

[43] L/6905, Decision of 8 October 1991, BISD 39S/300.

6. CONCLUSIONS

6.85 The United States submits that Japan has made various sets of tariff concessions in various Schedules attached to protocols after trade negotiating rounds. The fact that the concessions given in a prior multilateral round have been succeeded by concessions in a subsequent multilateral round does not extinguish either the prior concessions, or the expectations arising from those prior concessions. In the US view, the later concessions have not had the legal effect of modifying or withdrawing the earlier concessions because Japan never has invoked Article XXVIII to explicitly give notice of its intent to modify or withdraw its prior tariff concessions on photographic film and paper. Thus, Japan - as well as the United States - continue to be legally bound by their GATT 1947 concessions and the reasonable expectations attendant upon those receiving the concessions, as well as by the legal obligations incidental to those concessions, including compensation obligations connected with initial negotiating rights. Similarly, the United States argues, Japan's 1996 schedule proposed as a rectification to incorporate changes in the Harmonized System does not affect the scope of any of Japan's prior tariff concessions. Therefore, in the US view, all of Japan's Kennedy Round, Tokyo Round and Uruguay Round concessions on consumer photographic film and paper remain in effect and continue to exist in parallel. Accordingly, the United States claims to have retained its expectations of improved market access arising from each concession and thus retains the right to redress under Article XXIII:1(b) to protect those reasonable expectations.

6.86 **Japan** maintains that only the benefit accruing from the Uruguay Round tariff concessions are relevant in this case, because a new balance of tariff concessions on photographic film and paper has been actually negotiated and agreed upon under the type of tariff negotiations stipulated by Article XXVIII*bis*, and the result of the latest tariff negotiation should be deemed to have created a new expectation concerning the balance of tariff concessions, and to have replaced any reasonable expectation that arose under a prior tariff negotiation. In Japan's view, the criterion of judgement should be a substantive one, i.e., whether or not a new balance of tariff concessions has been created as a result of tariff negotiations, in which various circumstances at the time of the tariff concessions were taken into account. Japan requests the Panel to examine the US non-violation complaints before it on that basis.

C. GOVERNMENTAL MEASURES

1. THE LEGAL TEST

6.87 According to the **United States**, by the terms of Article XXIII:1(b), "the application ... of any measure, whether or not it conflicts with the provisions of [the General Agreement]", may give rise to an Article XXIII:1(b) claim. The ordinary meaning of the term "any measure" as it appears in the Article suggests that it includes all manner of government policies and actions. This reading of the term is reinforced by the object and purpose of Article XXIII:1(b), which, GATT Panels have found, is to provide a right of redress in situations outside the scope of other GATT articles.

6.88 The United States argues that all of the measures that it has specifically challenged are "measures" within the meaning of Article XXIII:1(b). The United States notes that the phrase "any measure" has never before been the subject of controversy in an Article XXIII:1(b) dispute. Nor has any GATT panel attempted to define the term "any measure". The United States further notes that Japan goes to great lengths to craft a definition that would not only exonerate Japan in this dispute, but also would place Japanese administrative guidance beyond the reach of the WTO.

6.89 **Japan** submits that in the context of a non-violation claim, the complaining party must establish the existence of an application of a measure by another WTO Member. For Japan, this textual requirement means the following three criteria:

(1) First, since the measure must be a government measure, private conduct is outside the scope of Article XXIII:1(b). When a government does nothing more than make formally and substantively non-binding recommendations, the decision whether to comply is a private and voluntary one.

(2) Second, not every government policy or action constitutes a measure for non-violation purposes. A measure must either provide a benefit or impose legally binding obligations or their substantive equivalent. With respect to the latter, any policy or action allegedly regulating private conduct must impose legally binding obligations or their substantive equivalent.

(3) Third, there must be a current and actual application of the measure to the products in question. In particular, there can be no application of a measure that is no longer in effect.

6.90 Japan suggests that the United States seems to agree with the first and the third requirements,[44] but that the parties differ, however, with respect to the second criterion.

6.91 The **United States** responds as follows:

(1)The United States is not challenging purely private conduct in this proceeding. Its claim is based on actions taken by, at the direction of, or in concert with, the Government of Japan in order to achieve government objectives.

(2)There is no requirement under Article XXIII:1(b) that a measure impose legally binding obligations or provide a benefit. The cases cited by Japan, i.e., *Japan - Restrictions on Imports of Certain Agricultural Products ("Japan - Agricultural Products")*[45] and *Japan - Trade in Semiconductors ("Japan - Semiconductors")*,[46] are not applicable here with respect to what constitutes a measure under Article XXIII:1(b), although they are applicable to the extent they stand for the general proposition that administrative guidance can be a measure.

(3)All of the measures challenged by the United States in this proceeding are either still in effect today, or have been superseded by other measures that carry forward their objectives and policies. Virtually all of the measures challenged by the United Sates in this proceeding remain in effect today. The few that have been revoked, such as JFTC Notification 17 of 1967, were redundant in that their objectives are still achieved though measures remaining in effect.

(a) Administrative guidance

6.92 The United States submits that when the Japanese Government gives guidance to industry, it is expressing the Government's policy and taking action to develop, disseminate, and enact that policy. Japan should be just as accountable for the effects arising from this type of measure as for the effects arising from a measure which is "binding". The United States points out that two GATT panels, i.e., the panels in *Japan - Agricultural Products* and *Japan - Semiconductors*, have found that administrative guidance has "played an important role in Japan" and is a "traditional tool of Japanese Government policy based on consensus and peer pressure," noting further that administrative guidance has operated within the context

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[44]Japan points out that with regard to the first requirement, the United States admits that "[t]he term 'any measure' in Article XXIII:1(b) does refer to government policies and actions". With regard to the third requirement, Japan asserts that the United States only argues that the measures at issue in this case are still in effect.

[45]*Japan - Restrictions on Imports of Certain Agricultural Products*, adopted on 22 March 1988, BISD 35S/163.

[46]*Japan - Trade in Semiconductors*, adopted 4 May 1988, BISD 35S/116.

of the "special characteristics of Japanese society."[47] These panels have found that these administrative guidances constituted "measures" in both of those cases. The Japanese Government is able to rely on its traditionally close relationship with industry and its extraordinary power and influence over industry to achieve its goals through measures that are not formally binding.

6.93 The United States explains that Japan defines the term "administrative guidance" as "guidance, recommendation, advice, or other acts by which an Administrative Organ may seek, within the scope of its duties or designated functions, certain feasance or non-feasance on the part of specified persons in order to realize administrative aims, where such acts are not dispositions".[48] Although in a technical sense "administrative guidance" does not have a formal legal consequence attached to non-compliance, "administrative guidance is a form of government regulation which imposes some kinds of rules of conduct on private individuals or enterprises".[49] What differentiates "administrative guidance" from a request made between two private entities is the extraordinary power of the entity making the request, i.e., the Government of Japan.[50] This power is enhanced manifold because in Japan "the government often represents the consensus of the industry in which the rule of conduct should be enforced".[51] Thus, what might be seen by outsiders as nothing more than policy guidelines or recommendations are in fact accepted within Japan as tantamount to governmental directives. Ministries like MITI may pressure or induce regulated enterprises into compliance with "guidances".[52] "[A]dministrative guidance can put irresistible pressure upon the addressee".[53]

6.94 In **Japan**'s view, the United States ignores critical distinctions among types of administrative guidance and distorts Professor Matsushita's analysis. Japan emphasizes that MITI issues different types of administrative guidance: MITI's guidance varies from "soft" guidance (i.e., mere suggestions) to "hard" guidance (i.e., guidance issued in place of more formal regulatory measures). Japan explains that Professor Matsushita has divided administrative guidance into three distinct types, which provide a useful analytical framework for understanding the nature of administrative guidance, and the importance of evaluating administrative guidance on a case-by-case basis. *Regulatory* administrative guidance covers guidance used by government agencies to regulate the conduct of business enterprises and persons, often as a substitute for a more formal order. Administrative guidance used in this way is a substitute for legal compulsion. This is the kind of guidance which the United States would assert as the universal norm. Aside from regulatory guidance, however, there is also *promotional* administrative guidance, which covers advice and information given to enterprises to advance and promote their own interests. This category describes the 1970 Guidelines perfectly: MITI was advising film manufacturers and distributors on ways to make their businesses more efficient and competitive, not imposing some obligation on them in furtherance of a public policy objective. Finally, *adjudicatory* administrative guidance, not relevant here, covers guidance used to help private enterprises to solve disputes among themselves.[54]

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[47] *Japan - Agricultural Products*, BISD 35S/163, para. 5.4.1.4, quoted in *Japan - Semiconductors*, BISD 35S/116, para. 107.

[48] Article 2(6) of the Administrative Procedure Law, Public Law No. 88 (1993). MITI's legal authority to issue administrative guidance arises out of its organic enabling legislation, the MITI Establishment Law (Public Law 275, 1952), US Ex. 52-2. "Government agencies, especially the MITI, have emphasized that administrative guidance is allowed by the 'establishment law' even though there is no specific provision in the authorization law". Matsushita Mitsuo, op. cit., p. 65.

[49] Ibid. p. 60.

[50] Ibid. p. 61.

[51] Ibid.

[52] Ibid. pp. 61-62, 67.

[53] Ibid. p. 69.

[54] See Mitsuo Matsushita, op. cit., pp. 61-64, Japan Ex. E-7; Mitsuo Matsushita and Thomas Schoenbaum, Japanese International Trade and Investment Law 31-41 (1989), Japan Ex. E-8. A Japanese administrative law professor also adopts these three categories. Hiroshi Shiono, Gyoseiho I (Administrative Law I), (2d ed. 1994) pp. 166-167, Japan Ex. B-6. Other commentators also recognize the three categories. See, e.g., Ken Duck, Comment: Now That The Fog Has Lifted: The Impact of Japan's Administrative Procedure Law on the Regulation of Industry and Market Governance, 19 Fordham Int'l. L.J. 1686, 1709 (1996), Japan Ex. E-9.

6.95 The **United States** argues that Japan's argument that administrative guidance must be "binding" was rejected by the panel in *Japan - Semiconductors* and *Japan - Agricultural Products* and should be rejected here. Any type of Japanese administrative guidance -- whether regulatory, promotional, or adjudicatory -- can be a "measure" within the meaning of Article XXIII:1(b). When the Japanese Government is giving "promotional guidance" to industry, it is expressing the Japanese Government's policy and taking action to develop, disseminate, and enact that policy. The Japanse Government should be just as accountable for the effect arising from this type of measure as for the effects arising from the measure for which it imposes a criminal penalty. In either case, the Japanese Government has taken action to influence the market consistent with the special circumstances in Japan. The two situations illustrate a difference in degree as to how far the government needs and is willing to go to achieve the desired effects -- not any substantive difference in whether the government has taken purposeful action. The two GATT panel decisions noted offer strong support for the US position.[55]

6.96 The United States further argues that the important question regarding administrative guidance in Japan is its operation and effect -- not the labels that may be used to describe it. Professor Hiroshi Shiono, described by Japan in its first submission as "a leading scholar of Japanese administrative law," stated: "[t]he three categories mentioned above are not necessarily exclusive to one another ... . Even if assistance-related administrative guidance is issued, it involves an aspect of leading the parties concerned to a certain direction laid out by the administrative body, and thus it cannot be denied that it has a regulatory aspect as well."[56] Further, the Japanese Government itself has promulgated an official definition of administrative guidance in the Administrative Procedure Law which does not differentiate among different types of administrative guidance.[57] The United States concludes that, regardless of how one might sub-categorize each particular administrative guidance in this case, it is clear that the guidance played a critical role in the achievement of the objectives of the Government of Japan.

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[55]See *Japan - Agricultural Products*, para. 5.4.1.4 (finding that "the practice of 'administrative guidance' played an important role" in Japanese Government policy-making and is a "traditional tool of Japanese Government policy based on consensus and peer pressure"): *Japan - Semiconductors*, para. 108 (recognizing that non-mandatory measures of the Government of Japan can be measures within the meaning of Article XI).

[56]Article 2(6) of the Administrative Procedure Law provides Japan's official definition of administrative guidance.

[57]Hiroshi Shiono, Administrative Law I, p. 167, Japan Ex. B-6. The United States also notes that Japan submitted only one part of student Ken Duck's law review article to contend that the distinctions among types of administrative guidance dramatically change the legal effects of the guidance, the article actually does not support that premise. The article also stated that:

"The non-transparent and anti-competitive regulatory methods of Japan's economic bureaucracy impede new entrants to Japanese markets. Japan's regulatory system emphasizes close, informal contacts between the regulators and the firms they regulate. Gyosei shido, or administrative guidance, the process by which ministries used implied threats of future action or inaction in seeking a party's compliance with an administrative goal, is the primary regulatory method in Japan. Japan's informal style of regulatory governance, including administrative guidance, evolved from informal means of governance in Japanese history. The Japanese legal system and other institutional arrangements, like the amakudari [descent from heaven retirement] system and the shingikai councils, which emphasize close, informal ties between government and business, perpetuate Japan's informal regulatory system and enhance compliance with administrative guidance."

Ken Duck, Comment: Now That The Fog Has Lifted: The Impact of Japan's Administrative Procedure Law on the Regulation of Industry and Market Governance, 19 Fordham Int'l L.J. 1686 (1996), Japan Ex. E-9.

(b) Past GATT panel reports

6.97 **Japan** argues that GATT precedent confirms that not all administrative guidance qualifies as a "measure" for GATT purposes, and that the relevant distinction is whether the guidance in question amounts, in substance if not formally, to the imposition of a binding obligation. Specifically, the panel on *Japan - Semi-Conductors*[58] considered whether formally non-mandatory administrative guidance, namely, requests that Japanese semiconductor producers eliminate dumping in third country markets, could constitute "measures" for purposes of Article XI. Japan points out that there is no explicit distinction made between a "measure" for purposes of Article XI and a "measure" for purposes of non-violation claims. Absent a reason to the contrary, in Japan's view, a term used in one provision of GATT may be construed to have the same meaning when it is used in another provision. Japan argues that there is nothing to suggest that the term "measure" was intended to have a broader meaning in Article XXIII:1(b) than in Article XI. For Japan, the textual interrelation between Article XXIII:1(b) and Article XXIII:1(c) also supports the conclusion that the non-violation remedy is not available in the case of formally and substantively non-binding recommendations. Specifically, Article XXIII:1(b) applies to "measures", while Article XXIII:1(c) then allows parties to complain about "any other situation". In Japan's view, "measures", as opposed to the all-encompassing "any other situation", has a limited meaning, referring to government measures, not to private decisions whether or not to follow non-binding recommendations.

6.98 The **United States** responds that the criteria advanced by Japan would render administrative guidance - a traditional tool of Japanese Government policy - beyond the reach of GATT disciplines. According to the United States, Japan's argument is not supported by the text of Article XXIII:1(b) and, if accepted, would defeat the purpose of that provision. The United States explains that throughout GATT, the drafters used a variety of terms to describe government policies or actions in the context of distinct rules aimed at particular concerns.[59] Article XI:1 refers to "prohibitions or restrictions ... on the importation ... or on the exportation ... of any product". In comparison, the United States underscores that Article XXIII:1(b) refers to "*any measure*", reflecting the drafters' intent that Article XXIII:1(b) should be a safety net potentially providing redress for any government policy or action that nullifies or impairs benefits under the General Agreement. Had the drafters intended Article XXIII:1(b) to cover only those government policies and actions which directly conferred a benefit or imposed a legal obligation, they could have done so by selecting words to convey those limitations just as they selected words to limit the scope of other Articles.

6.99 **Japan** contends that although the panel on *Japan - Semi-Conductors* recognized the special importance of administrative guidance as a tool of Japanese government policy,[60] it nonetheless made clear that "not all non-mandatory requests could be regarded as measures".[61] The panel emphasized that the issue would have to be decided on a case-by-case basis.[62] The panel identified two "essential criteria" that would need to be met for non-mandatory requests to qualify as "measures" for Article XI purposes:

(1) "there were reasonable grounds to believe that sufficient incentives or disincentives existed for non-mandatory measures to take effect"; and

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[58]BISD 35S/116, adopted 4 May 1988.

[59]For example, Article I:1 refers to "customs duties and charges of any kind;" Article III:2 refers to "internal taxes or other internal charges of any kind"; Article III:4 refers to "all laws, regulations, and requirements"; Article VIII:1 refers to "[a]ll fees and charges of whatever character ... imposed ... in connection with importation or exportation"; Article IX:2 refers to "laws and regulations relating to marks of origin"; Article X:1 refers to "[l]aws, regulations, judicial decisions and administrative rulings of general application".

[60]*Japan - Trade in Semiconductors*, BISD 35S/116, p. 154, para. 107.

[61]Ibid. p. 154, para. 108.

[62]Ibid.

(2) the fulfilment of the government requests "was essentially dependent on Government action or intervention".[63]

In *Japan - Semi-Conductors*, the panel found that these two criteria were met. The panel found that the official commitment by the Japanese Government in a formal agreement to eliminate third country dumping created reasonable incentives or disincentives for Japanese producers to perform appropriately, and thus fulfilled the first criterion. The panel noted, however, that this circumstance alone was not sufficient to ensure compliance, since subsequent to the conclusion of the United States - Japan Semiconductor Arrangement in September 1986 (in which this commitment was made) some producers and exporters continued to engage in dumping. By requiring the submission of price and cost data and instituting regular supply and demand forecasting, the Japanese Government secured effective compliance. The panel thus determined that the Japanese Government created an administrative structure "which operated to exert maximum possible pressure on the private sector" to comply with non-mandatory administrative guidance. Accordingly, the panel found that the only difference between this guidance and formal legally binding obligations "amounted to a difference in form rather than substance",[64] and that the administrative guidance therefore constituted "measures" for Article XI purposes.

6.100 The **United States** contends that GATT precedent does not confirm that administrative guidance must be "binding" to constitute a measure within the meaning of Article XXIII:1(b). In the US view, the only precedent that Japan cites for this proposition is *Japan - Semi-Conductors* which it attempts to argue is relevant here because there is no distinction between the terms "any measure" in Article XXIII:1(b) and "other measures" in Article XI. In the US view, however, the panel should not apply the two part test used in that case to determine whether the distribution countermeasures at issue in this dispute are measures within the meaning of Article XXIII:1(b).

6.101 First, according to the United States, Japan argued in that dispute that the non-mandatory "measures" complained of were not restrictions within the meaning of Article XI:1.[65] In contrast, the question in this dispute is whether the measure complained of are "any measures" that nullify or impair benefits within the meaning of Article XXIII:1(b). Second, the meaning of the term "measures" under Article XXIII:1(b) should not be confused with the question of whether a measure is having an effect that GATT intends to prevent. The panel in *Japan - Semi-Conductors* focused on whether the measure had the effect of prohibiting or restricting exportation of semiconductors. Thus, it looked at whether the Japanese Government's actions prohibited manufacturers from exporting at dumped prices or gave them incentives not to do so. In the US view, this is a different inquiry from that needed to decide whether distribution countermeasures had the effect of upsetting the competitive relationship between imported and domestic products. A non-mandatory measure may not be able to have the same effect as a "restriction or prohibition" under Article XI:1 if it is not legally binding or does not impose an equivalent obligation. But a non-mandatory measure can certainly have the effect of adversely affecting the competitive opportunities for imported products.

6.102 **Japan** responds that since both the *Japan - Semi-Conductors* case and the present case deal with non-mandatory administrative guidance, the finding of the *Japan - Semi-Conductors* panel provides a useful benchmark for the present case in determining what constitutes a "measure" for the purpose of non-violation complaints. Japan deems US efforts to distinguish Article XI from Article XXIII unpersuasive because in both provisions, the term "measure" is then followed by a qualification that relates

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[63]Ibid. p. 155, para. 109.

[64]Ibid. p. 158, para. 117.

[65]Ibid., pp. 153-154, para. 106. The Panel noted "that Article XI:1, unlike other provisions of the General Agreement, did not refer to laws or regulations but more broadly to measures. This wording indicated clearly that any measure instituted or maintained by a contracting party which restricted the exportation or sale for export of products was covered by this provision, irrespective of the legal status of the measure". Ibid.

the "measure" to the operative purpose of that provision and there is no explicit distinction being made between "measures" for purposes of Article XI and a "measure" for Article XXIII:1(b) purposes. Japan further notes that although the United States argues that the *Semiconductor* panel does not support Japan's argument because it found that "any measure ... was covered, irrespective of the legal status of the measure," the panel further stated that "not all non-mandatory requests could be regarded as measures within the meaning of Article XI:1" and applied its "two essential criteria" to the "non-mandatory requests."

6.103 Japan further submits that the question of whether Japanese administrative guidance constituted a "measure" also arose in the panel report on *Japan - Agricultural Products*.[66] The issue arose under Article XI:2(c)(i), which provides an exception to Article XI for import restrictions on agricultural products that are necessary to the enforcement of "measures" which operate to restrict domestic production. The panel found that production restrictions pursuant to administrative guidance did constitute "measures" within the meaning of the provision. In Japan's view, this kind of regulatory guidance, in which the subjects are urged to act contrary to their commercial self-interest, is clearly distinguishable from the promotional guidance at issue in this case. Japan further notes that non-compliance with the guidance in *Japan - Agricultural Products* resulted in loss of eligibility for government subsidies and loans.[67]

6.104 In response to Japan's argument that the administrative guidance at issue before the panels on *Japan - Agricultural Products* and *Japan - Semi-Conductors* urged industry to act contrary to its self-interest, the **United States** argues that a government action or policy need not be adverse to industry interest to be a measure. The United States contends, if that were the case, none of the prior Article XXIII:1(b) cases involving subsidies would have been successful. In the US view, the real significance of the issue raised by Japan is that a government may use less formal, less intrusive means to achieve its policies if industry is receptive to those policies. The fact that the government can more easily achieve its goals because of an industry's receptiveness does not absolve a government of responsibility for the changes in the conditions of competition resulting from its measures. In the US view, Japan admitted that MITI's administrative guidance on distribution countermeasures was in the interest of manufacturers who would benefit from systematized distribution channels.

6.105 The United States also argues that when the Japanese Government gives guidance to industry, it is expressing the Government's policy and taking action to develop, disseminate, and enact that policy. Japan should be just as accountable for the effects arising from this type of measure as for the effects arising from a measure which is "legally binding," as that term is used by the Government of Japan. A contrary finding would make acceptable all collaboration between government and industry, effectively immunizing Japanese administrative guidance, concerted adjustment, and industrial policy from attack at the WTO. Such an outcome would give WTO sanction to a careful and calculated plan to offset and undermine tariff concessions. This could cause numerous countries that made difficult concessions in the Uruguay Round to question why they should honour their commitments. It would have been an open invitation for nation's to practice new forms of import-inhibiting industrial policy and protectionist government intervention.

(c) Governmental attributability of measures

6.106 **Japan** argues that MITI advisory committee reports, plans, and manuals and the formation of codes and councils that regulate promotions are not measures within the meaning of Article XXIII:1(b), because these measures are attributable to the private sector, not the Japanese Government.

6.107 The **United States** responds that it is not challenging private business practices, but measures of the Japanese Government. The term "any measure" in Article XXIII:1(b) is broad enough to include not only actions of the government, but measures designed, promulgated, or applied by a number of Councils,

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[66]Adopted on 22 March 1988, BISD 35S/163.

[67]Ibid., pp. 234-237, paras. 5.3.5.1, 5.3.8.1.

Committees, Centres, trade associations, and other quasi-governmental entities that have included private sector participants, acting under the authority of or in concert with Japanese Government ministries and agencies. In each of the principal areas in which Japan applied liberalization countermeasures, i.e., distribution countermeasures, the Large Stores Law and related measures, and the promotions countermeasures, the Japanese Government made extensive use of quasi-governmental agencies to implement government policy. These entities are not acting independently of governmental authority or direction. Measures developed or applied by these entities are measures within the meaning of Article XXIII:1(b).

6.108 According to the United States, for Japan's restructuring of the photomaterials distribution system to succeed, "a close relationship between government and business [was] necessary".[68] The government and private sector cooperate well because "there has historically been a close relationship between the government and business community" and "[t]here is a strong desire among the business community to avoid confrontation with the government even if the business community feels that the administrative agency has acted without legal authority".[69] Given the strong ties between the government and business community, the Japanese Government has been able to rely upon informal methods as well as formal measures in imposing its policies.[70] The United States argues that MITI frequently relies on informal administrative guidance to achieve its policy objectives.[71]

6.109 The United States argues that the Japanese Government actively promoted as part of its industrial policy mechanism the close government-private sector relationship based on the approach described in a MITI document entitled "The Formation of a New Industrial Order."[72] This document introduced the concept of "concerted adjustment" between the government and private sector to formulate and implement industrial policy and liberalization countermeasures. And, in fact the MITI History notes the importance of the New Industrial Order initiative in implementing the liberalization countermeasures:

> "As the new industrial order is shaped, it might be effective that the specific target is set by the cooperation between government and businesses, businesses make efforts to achieve the target, and in the process of businesses achieving its target, the government takes preferential measures with respect to taxation and financing. Of course, in this process, persuasion and assertions would repeatedly be held between government and businesses, and this effort should be continued until both sides are satisfied."[73]

6.110 Although the Japanese Diet did not pass the "Special Measures Law For Promoting Designated Industries" that was based on "The Formation of the New Industrial Order," MITI did take alternative action to implement the New Industrial Order initiative and the concept of concerted adjustment. In June 1964, MITI Minister Takeo Fukuda presented a policy statement to the Cabinet entitled "The Future Policy after the Failure of the Proposed Special Measures Law for Promoting Designated Industries," which the Cabinet accepted.[74] The statement outlined how MITI would implement this government-private sector coordination system discussed in the Formation of the New Industrial Order. MITI's official history, published in 1990, confirms that Japan did implement the New Industrial Order approach to government and private sector coordination:

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[68]Matsushita Mitsuo, International Trade and Competition Law in Japan (Oxford: Oxford University Press, 1993) p. 276, US Ex. 93-1.

[69]Ibid. pp. 67, 276.

[70]Ibid. p. 277.

[71]Ibid. p. 60.

[72]MITI, Formation of the New Industrial Order, US Ex. 62-5.

[73]Ibid., p.9, US Ex. 62-5.

[74]MITI, History on Industrial Policy, Vol. 10, 31 March 1990, pp. 82-83, US Response to Supplemental Panel Questions, US Ex. 7.

"the realization was sinking in that the time had arrived to undertake liberalization countermeasures and work on creating a new industrial order. Thus, the decision was made to realize the ideal of public-private sector cooperation on an industry-by-industry basis through administrative guidance."[75]

6.111 The United States further argues that under the concerted adjustment process, the close involvement of industry at the early stages of the policy development process helps ensure that the actual implementation can later be achieved through informal measures such as administrative guidance without the Japanese Government having to rely on more formal laws or regulations. The participation of industry associations, advisory councils and other quasi-governmental policy entities, in turn, enhances the "peer pressure" generated in the industrial policy process to ensure compliance with the adopted measures.

6.112 The United States argues that given that the domestic industry is an active participant and its self-interest is fully considered at the initial stage of developing the measures, the measures often take on the characteristic of confirming actions that are already being taken in the marketplace by domestic firms. The United States believes that only when it is impossible to implement measures through this approach does MITI apply formal measures. To this end, the United States contends that an important part of implementing administrative guidance is continued follow-up by the government to ensure that the desired actions have been taken, to assist some segments of the private sector in acting on their own interest, and to continue pressuring companies that may be inclined to stray from the guidance. The United States notes that a common method of such follow-up is to continue to survey industry and to publicly identify and criticize those companies that are not complying.

6.113 For the United States, the use of the "concerted adjustment" method in this case, including the application of administrative guidance, echoes the findings of the panel in *Japan - Agricultural Products,* which stated that administrative guidance has "played an important role" in Japan and has been "a traditional tool of Japanese Government policy based on consensus and peer pressure."[76]

6.114 **Japan** asserts that the United States attempts to paint a picture of Japan as an unusual country with unique practices unlike those anywhere else in the world. In Japan's view, the United States has focused particular attention on government-business relationships and suggests that any governmental interaction with business is somehow strange. Japan responds that the United States tries to distort and exaggerate the government-business relationship in Japan. In reality, all governments, including the US Government interact with business.[77] The government-business interaction in Japan is not unusual, in particular since the United States itself acknowledges playing such a role with its private sector.

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[75]Ibid.

[76]*Japan - Agricultural Products*, adopted on 22 March 1988, BISD 35S/163, para. 5.4.1.4.

[77]In a presentation at the OECD in 1968, the United States explained:
"The Department of Commerce is at the centre of the Government's relations with business. Over the years the Department has been accused of speaking for business within the Government. This is clearly not the case at the present time: the Department talks with and to business, rather than for business, and the difference is far from being merely verbal. It is now considered the Department's task to identify those things which need to be done in the public interest and to which the business community has not given sufficient attention or with which business cannot deal because it is not properly organized for that purpose. The Department brings together people from industry to discuss such matters - some of which, it might be added, businessmen are reluctant to explore within their own private groupings because of the anti-trust laws".
See US Industrial Policies: Observations Presented by the US Delegation before the Industry Committee at its 6th Session (OECD, 1968), p. 38, para. 113 (emphasis original). Japan Ex. F-3.

(d) Measures "applied" and measures "in effect"

6.115 Japan points out that many of the US allegations in this case concern "measures" that are no longer in effect (i.e., distribution modernization policies during the 1960s and '70s) or past application of currently existing measures (i.e., the Large Scale Retail Store Law and the Premiums Law). Japan emphasizes that the WTO dispute settlement process is designed to resolve differences over present policies that affect trade, not to serve as an historical tribunal or to attempt to punish or undo alleged past transgressions.

6.116 Japan argues that the language of Article XXIII:1(b) makes clear that the non-violation remedy is designed to apply when a benefit is being nullified or impaired by the application of any measure, whether or not it "conflicts" with the provisions of GATT. Given that the text contemplates nullification or impairment in the present tense, caused by the application of a measure in the present tense, the ordinary meaning of this provision, with its use of present tense verbs, in Japan's view, limits the non-violation remedy to measures that are currently being applied. According to Japan, this conclusion is reinforced by Article 26.1 of the DSU which provides that even when a measure is found to nullify or impair benefits under Article XXIII:1(b), "there is no obligation to withdraw the measure". In Japan's view, this language clearly contemplates the ongoing existence of the measure in dispute.

6.117 According to Japan, since the GATT 1994 "is legally distinct from" the GATT 1947, as Article II:4 of the WTO Agreement provides, GATT 1994 should not be applied retroactively to many of the alleged "measures" which were no longer in effect before its entry into force on 1 January 1995. This position is in line with Article 28 of the Vienna Convention on the Law of Treaties regarding the general principle of non-retroactivity of treaties.[78]

6.118 Japan further submits that GATT precedent supports the rejection of the US non-violation claims regarding past Japanese measures. In *United States - Gasoline*, the panel stated clearly that it would not rule on measures that were not in effect and were unlikely to be renewed.[79]

6.119 The **United States** does not disagree with Japan's basic argument that the measures must be in effect to nullify or impair tariff concessions within the meaning of Article XXIII:1(b), although it does disagree with some of Japan's legal reasoning and Japan's factual conclusion that the measures at issue in this dispute are no longer in effect. In fact, the United States has demonstrated that all of the measures being challenged are in effect and are being reinforced by the Japanese Government. The United States has demonstrated that Japan has engaged in a continuing course of conduct over more than 25 years and that Japan's more recent actions should properly be viewed as ancillary measures reinforcing the distribution countermeasures, as well as evidence that those original measures and the policies underlying them continue to be implemented by the Japanese Government. Recognized principles of state responsibility lend additional support to the conclusion that Japan should properly be held accountable for its actions as a result of its continuing course of conduct.[80]

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[78]Article 28 of the Vienna Convention provides "Unless a different intention appears from the treaty or is otherwise established, its provisions do not bind a party in relation to any act or fact which took place or any situation which ceased to exist before the date of the entry into force of the treaty with respect to that party".

[79]"The Panel observed that it had not been the usual practice of a panel established under the General Agreement to rule on measures that, at the time the panel's terms of reference were fixed, were not and would not become effective". WT/DS2/R, pp. 37-38, para. 6.19. *United States - Standards for Reformulated and Conventional Gasoline*, WT/DS2/R, adopted on 20 May 1996, pp. 37-38, para. 6.19.

[80]See, e.g., Draft Articles on State Responsibility, Article 25:2, which provides:

"2. The breach of an international obligation, by an act of the State composed of a series of actions or omissions in respect of separate cases, occurs at the moment when that action or omission of the series is accomplished which establishes the existence of the composite act. Nevertheless, the time of commission of the breach extends over the entire period from the first of the actions or omissions constituting the composite act not in conformity with the international obligation and so long as such actions or omissions are repeated."

6.120 The United States also points out that some panels have even ruled that measures, prior to their revocation, were contrary to GATT rules, even though they were no longer in effect at the time of the panel's deliberations.[81] This is not the case with the measures at issue in this dispute.

6.121 The United States explains that Japan's reliance on the *United States - Gasoline* decision in support of its arguments is misplaced. That dispute involved a measure that had never been applied and that had affirmatively and officially expired before the panel was established. The complaining parties argued that the non-application of the measure should not prevent the panel from ruling on it because "the mere existence of [the measure] might have inhibiting effects on commercial and investment decisions" and "the possibility of its future application was sufficient to establish an Article I violation".[82] In the view of the United States, the critical facts in the *United States - Gasoline* dispute are significantly different from the critical facts in this dispute. First, the distribution countermeasures were and are being applied, whereas the "75 percent rule" at issue in *Gasoline* lapsed without ever being applied. Second, the distribution countermeasures do not have a specified expiration date, whereas the lifetime of the 75 percent rule was clearly stated in the regulations. And third, the distribution countermeasures continue to have an effect, even after the panel's terms of reference were established, whereas the *Gasoline* panel found the 75 percent rule not to have an effect subsequent to its expiration.

6.122 The United States further argues that prior panels considering the question of measures no longer in force were presented with measures that were unquestionably no longer in force which, in the US view, is not the case in this dispute. The United States maintains that virtually all of the measures applied by Japan remain in force today and Japan has not made any showing to the contrary.

6.123 The United States further explains that Japan's distribution countermeasures that block foreign film from the principal wholesale distribution channels, the Large Stores Law that buttresses these measures and limits alternative routes to market through large stores and the promotion countermeasures that restrict innovative and effective promotion to Japanese consumers continue to have the effect of severely curtailing competitive opportunities for imported products today.

6.124 According to the United States, through the distribution countermeasures, Japan established an exclusionary wholesale distribution system that could operate in perpetuity with little additional government intervention given the oligopolistic structure of the Japanese film sector and the Government's ongoing enforcement of the Large Stores Law and the Premiums Law and related promotion countermeasures.

6.125 The United States further contends that, notwithstanding the self-perpetuating nature of the exclusionary system established by the distribution countermeasures, Japan is continuing to reinforce and supplement these measures. First, it is continuing to enforce the Large Stores Law and promotion countermeasures. Second, the Japanese government is continuing to support the structure of the system through business assistance programs. Third, Japan's passage of the Business Reform Law and its initial designation of the photographic materials sector for assistance under this broad measure demonstrates Japan's ongoing effort to buttress the structure of the system whenever the need arises. In the US view, these actions by the Japanese government demonstrate ongoing, active efforts to reinforce the system

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Yearbook of the International Law Commission, 1980, Vol. II, Part. II, p. 32-33 (United Nations 1981). See also Yearbook of the International Law Commission, 1978, Vol. II, Part. II, p. 89-97 (United Nations 1979) (for commentary on Article 25).

[81]See, e.g., Panel Report on *United States - Measures Affecting Imports of Woven Wool Shirts and Blouses ("United States - Wool Shirts")*, adopted on 23 May 1997, WT/DS33/R, p. 77, para. 8.1; Panel Report on *EEC - Measures on Animal Feed Proteins*, adopted on 14 March 1978, BISD 25S/49; Panel Report on *United States - Prohibition on Imports of Tuna and Tuna Products from Canada*, adopted on 22 February 1982, BISD 29S/91, 106, para. 4.3.

[82]*United States - Gasoline*, WT/DS2/R, p. 7, para. 3.10. The United States adds that the panel did not examine the measure under Article I:1 for a variety of reasons, including that "the Panel's terms of reference were established after the [measure] had ceased to have any effect". Ibid., pp. 37-38, para. 6.19.

established by the initial distribution countermeasures so that it remains a bulwark against penetration by imports.

6.126 The United States emphasizes that this Panel's determination as to whether the distribution countermeasures are in effect will send an important signal to Members considering using informal and ephemeral means to accomplish protectionist purposes. Members should be held accountable for measures which may superficially appear to be short-lived but in reality achieve lasting distortions in the competitive relationship between domestic and imported products. To excuse Members in these circumstances would create an important exemption to the WTO rules and disciplines.

6.127 **Japan** also argues that in relation to the requirement in Article XXIII:1(b) that nullification or impairment of a benefit needs to be the result of the "application" of a measure, the complaining party must show how the "application" of a measure to specific products nullifies or impairs benefits with respect to those products. Since the benefit consists of legitimate expectations concerning the competitive opportunities for imported *products*, it follows that for a measure to nullify or impair that benefit, it must "apply" to the products in question. In Japan's view, given the basis of the non-violation remedy in tariff concessions on goods, it is not enough to name a law and assert some economic impact on specific products.

(e) Measures and market structure

6.128 The **United States** submits that the ongoing application of distribution countermeasures, the Large Retail Stores Law and the promotion countermeasures has continued to operate to nullify or impair US benefits, due to: (1) foreclosure from the primary wholesale channels of distribution as a result of the distribution countermeasures; (2) sharp diminution of alternative channels (i.e., large stores, secondary wholesalers); and (3) inability to price and promote products effectively and competitively as a result of restrictions under the Premiums Law and Antimonopoly Law. In the view of the United States, these measures nullify or impair benefits accruing to the United States not only from the Uruguay Round, but the Tokyo and Kennedy Rounds as well.

6.129 **Japan** responds that the United States is in fact complaining about the market structures, in particular, the decisions by the primary wholesalers of the domestic film manufacturers not to carry other brands of film, and affiliations between domestic manufacturers and photofinishing laboratories, that have been in place since the mid-1970s. According to Japan, the United States makes no allegation of any additional measures since that time which allegedly encourage single-brand distribution.[83] To Japan it appears that the United States considers the continued existence of a market structure - i.e., single-brand distribution - allegedly encouraged by policies in the past to constitute "ongoing application" of measures. Japan argues that a market structure should not be deemed a measure. Since a "measure" must be applied by a WTO Member, the term "measure" must refer exclusively to the policies and actions of a government.[84] In Japan's view, the decisions of certain primary wholesalers to purchase film only from particular suppliers are as such a matter of purely private conduct. Japan concedes that the United States may believe that these private company decisions constitute restrictive business practices. However, for Japan it is beyond contention that allegedly restrictive business practices are not covered by the current dispute settlement system under GATT.

6.130 Japan contends that the United States has not identified any government-imposed or legal obstacle that prevents wholesalers from buying other brands of film or that prevents photofinishing laboratories from switching to other brands of paper. Japan argues that the United States has not even tried to point out any ongoing active involvement by the Japanese Government in continuing to encourage or maintain the market structures it complains about. Accordingly, in Japan's view, the US claims about "ongoing application" of "distribution countermeasures" boil down to allegations about private business practices which are wholly outside the scope of Article XXIII:1(b).

6.131 The **United States** responds that it is not claiming in this dispute that market structure is a measure, only that Japan's bottle-necked distribution system provides compelling evidence of the Japanese Government's systematic efforts to impede market access for imported film and paper. Although a market structure is not a measure *per se* within the meaning of Article XXIII:1(b), the steps taken by the Japanese Government to create and maintain an exclusionary market structure in the Japanese photographic materials sector constitute measures. Therefore, the United States argues that the characteristics of the market structure in the Japanese consumer film and paper market are clearly relevant in this dispute. Whereas the continued existence of the exclusionary market structure, in the US view, reflects the ongoing application of measures, the United States emphasizes that it is not claiming in this dispute that purely private conduct is a measure. Rather, the United States is claiming that measures designed, promulgated or applied by a number of councils, committees, centres, trade associations and

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[83]Japan emphasizes that the alleged "distribution countermeasures" during the 1960s and '70s are no longer in effect. According to Japan, the United States itself mentions in passing the 1990 Guidelines. In Japan's view, given the fact that the United States itself has urged Japanese industry to follow those guidelines, it is not surprising that the United States mentions these guidelines only in passing and does not make any effort to incorporate these guidelines into its legal theory.

[84]Article II of the Marrakesh Agreement Establishing the World Trade Organization describes the WTO as providing the framework for conducting trade relations "among its Members" (Article II:1), and explains that the agreement is "binding on all Members" (Article II:2). The focus of WTO remedies should also be on the Members - in other words, governments.

other quasi-governmental entities that have included private sector participants, acting under the authority of or in concert with Japanese government ministries and agencies, constitute measures. In each of the principal areas in which Japan applied liberalization countermeasures, the United States argues that the Japanese Government made extensive use of quasi-governmental entities to implement government policy. In the US view, these entities are not acting independently of governmental authority or direction.[85] Accordingly, in the US view, measures developed or applied by these entities are measures within the meaning of Article XXIII:1(b).

6.132 **Japan** contends that Article XXIII:1(b) focuses on "measures" because the WTO applies only to *governmental* actions, not private actions. The requirement of a "measure" thus creates a fundamental dividing line between actions subject to WTO discipline and actions beyond the scope of WTO obligations. The WTO properly reflects the absence of any international consensus to go beyond governmental acts to reach private sector conduct. Japan argues that the alleged "measures" identified by the United States are merely advisory bodies' analysis or suggestions and the industries' self-regulation, which is a purely private sector conduct.

2. DISTRIBUTION "COUNTERMEASURES"

6.133 The **United States** specifies the following distribution countermeasures as subject to its claim under Article XXIII:1(b):

(1) 1967 Cabinet Decision;
(2) 1967 JFTC Notification 17;
(3)1968 Sixth Interim Report of the Industrial Structure Council Distribution Committee;
(4)1969 Seventh Interim Report of the Industrial Structure Council Distribution Committee; (5)1969 Survey on Transaction Terms;
(6)1970 Guidelines for Rationalizing Terms of Trade for Photographic Film;
(7)1971 JFTC Rule 1 (International Contract Notification);
(8)1971 Basic Plan of the Distribution Systemization Promotion Council;
(9)1975 Manual of the Distribution Systemization Development Center;
(10)1976 JDB funding for Konica's wholesalers;
(11)1977 SMEA funding for photoprocessing laboratories.

These measures and the background leading to their adoption are described in detail in Section B of Part II and in Section A of Part V above.

6.134 The United States contends that the foregoing measures are governmental measures and that they are effectively still in force.

6.135 **Japan** responds that they are not governmental measures for purposes of Article XXIII:1(b) and that they are not currently in effect.

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[85]See Panel Report on, *Review Pursuant to Article XVI:5*, adopted on 24 May 1960, BISD 9S/188, 192, para. 12 (explaining that "the GATT does not concern itself with such action by private persons acting independently of their governments") (emphasis added by the United States).

(a) Attributability to the government

6.136 Japan concedes that four of the foregoing items, i.e.,

(2) JFTC Notification 17;
(7) International Contract Notification;
(10) JDB funding;
(11) SMEA funding.

were once "measures". Japan notes, however, that all four of these items were raised by the United States for the first time in its first submission to the Panel and thus, are subject to procedural objections by Japan.

6.137 In Japan's view, the 1967 Cabinet Decision (item 1) was not a "measure" because it was merely a policy statement issued by the Cabinet and addressed to government agencies and did not legally obligate anyone outside of the government to do anything. Only subsequent actions by the agencies could constitute measures, depending on the particular circumstances of each action.

6.138 The **United States** counters that the Cabinet Decision contained both broad and specific direction of the Japanese Government to implement the liberalization countermeasures, and that the Decision specifically referenced problems related to liberalization of the distribution sector.[86] Further, the United States has also demonstrated that the other documents and actions referenced by Japan also constitute "measures" within the meaning Article XXIII:1(b).[87]

6.139 According to **Japan**, the remaining items listed by the United States did not impose binding obligations or the substantive equivalent. They offered recommendations, to be followed or not on a voluntary basis. Japan contends that the United States tries to blur a wide range of actions into a single catch-all category of "administrative guidance". For Japan, however, it is critical to keep in mind that in fact there is only one item of administrative guidance in the US list, i.e., the 1970 Guidelines (item 6). In Japan's view, the other items identified by the US do not even rise to the level of administrative guidance.

6.140 More specifically, Japan argues that the five remaining alleged "measures" relating to distribution policies are reports or surveys:

(3)1968 Sixth Interim Report of the Industrial Structure Council Distribution Committee;
(4)1969 Seventh Interim Report of the Industrial Structure Council Distribution Committee;
(5)1969 Survey on Transaction Terms;
(8)1971 Basic Plan of the Distribution Systemization Promotion Council;
(9)1975 Manual of the Distribution Systemization Development Center.

6.141 Japan emphasizes that none of these reports by advisory councils represents an official statement or policy of MITI or the Japanese Government. Advisory councils merely fill an advisory role and their reports merely analyze issues and make recommendations to the government of possible policy responses. Private organizations, such as the Institute for Distribution Research (1969 Survey), undertake research and analysis, and provide information to the government as appropriate. Therefore, Japan concludes that these reports cannot be considered to be administrative guidance.

6.142 Japan explains that reports by advisory councils, such as the Industrial Structure Council and the Distribution Systemization Promotion Council, reflect not official government policy, but steps in the process of formulating policy. They analyze issues and make recommendations of possible policy

[86]See para. 2.9 of Section II.B.1.

[87]See sub-sections VI.C.1.(a) and (c) on "Administrative guidance" and "Governmental attributability of measures," in particular paras. 6.94 and 6.108.

responses. Although these reports shed light on MITI's decision-making process in pursuing distribution modernization, the reports themselves do not decide anything because the authorizing legislation of the Industrial Structure Council allows the Council only to submit its opinions to the MITI minister. Thus, according to Japan, there is no delegation of decision-making authority. Japan points out that under its law, administrative agencies are not legally bound to follow the opinion of their advisory councils. As noted by a leading scholar of Japanese administrative law:

"[G]enerally speaking, the raison d'être of councils is to democratize administration, to introduce professional knowledge, to ensure fairness of administrative acts, and/or to adjust among interested parties ... A council is different from an independent administrative committee. It does not express the intent of the government to the public. Although the administrative agency must respect the Council's opinions as a natural consequence, the agency is not legally bound by the opinions".[88]

Japan explains that in practice, agencies sometimes adopt their councils' suggestions and recommendations, and sometimes do not. Therefore, Japan concludes that its reports are not formal statements of the Japanese Government and, accordingly, they cannot constitute "measures" within the meaning of Article XXIII:1(b).

6.143 As to Japan's contention that the Panel should not consider the various surveys, reports, and actions other than the Guidelines to be measures of the Japanese Government, the United States responds that each of the quasi-governmental organizations carrying out the studies, reports, or other actions had close links to the government and in many respects acted as an arm of the government in the "concerted adjustment" process. In many cases, MITI made clear that the reports and other documents were to be seen as official government policy, often by repeatedly republishing the survey or study under MITI's name and with clear indication that the document represented MITI policy.

6.144 For example, with respect to the Industrial Structure Council, MITI's official historians have explained that:

"The council was generally made up of representatives of relevant industries and groups of people of experience or academic standing (such as scholars, journalists, and former bureaucrats), and the responsible MITI bureau or division would serve as the Secretariat office. To this council, the materials from MITI would be presented, policies indicated, pertinent opinions from relevant industries are heard, experts make the adjustments, and then the information is compiled by the relevant bureaus. This was the normal process. Because of their large size and influence, which was a result of being related to trade and industry, the Industrial Structure Survey Committee and Industrial Rationalization Council were integrated in 1964, creating the Industrial Structure Council (ISC). When necessary, a number of committees were set up. This structure made it possible to gain consensus within industry, or between industry and the government; and functioned as an effective organization for obtaining cooperation between the public and private sectors."[89]

[88]Hiroshi Shiono, Gyoseiho I (Administrative Law I) (2d ed., 1994) p. 265, Japan Ex. B-6.

[89]MITI, MITI History: "Public-Private Sector Cooperation, Volume 1 (May 31, 1991), p. 62, US Ex. 69 and First Panel Meeting, US Response to Supplemental Panel Questions, Attachment 22.

6.145 The United States further notes that Japanese scholars confirm the policy role played by quasi-governmental entities in obtaining cooperation between the public and private sectors:

"These councils tend to be criticized as being captive to the ministry, and certainly the bureaucrats work to see that deliberations come out to reflect their opinions. In practice, however, it is not the case that only things desired by the ministry are reflected in the groups' reports, for on issues that directly affect the interests of firms, industry representatives do speak out strongly. In fact, on such issues, the councils take on the coloration of a forum in which parties can adjust proposals to reflect their joint interests. Thus, proposals that are passed through these councils, that is, that have been negotiated to reflect vested interests, can be afterwards implemented relatively smoothly, at least in terms of the industries represented on the relevant councils. In this sense, the Shingikai [deliberative council] process is one explicitly democratic development in postwar Japanese Government. One point that needs to be emphasized regarding such councils is their role in the exchange of information and obtaining consensus on policy matters.[90]

(i) 1970 Guidelines: background, publication and follow-up

6.146 The United States argues that in order to develop and implement its industrial policy, the Japanese Government relies heavily on different types of quasi-governmental entities including deliberative councils, advisory committees, study groups, research institutes, chambers of commerce, and trade associations. These organizations have played a central role in Japan's use of the government-industry cooperation method (kanmin kyocho seido) to implement its liberalization countermeasures. The participation of these entities in the "concerted adjustment" process increases the "peer pressure" on these entities to comply with the industrial policies adopted by the government.

6.147 The United States reports that in 1963, MITI directed the four domestic photographic film and paper manufacturers to establish the Natural Colour Photography Promotion Council (NCPPC) to counter foreign competition. MITI officials, including the official responsible for the photosensitive materials sector, attended the Council's meetings, and MITI officials recommended specific policies to help the Council achieve its objectives. According to the United States, throughout the mid-1960's, MITI worked to develop the "government-private sector cooperation system" in the consumer photographic film and paper sector, and laid the groundwork for working with the domestic manufacturers to restructure the distribution system to resist foreign competition after the liberalization of formal trade and investment restrictions.

6.148 The United States submits that in 1968, following the Sixth Interim Report by the Distribution Committee, MITI commissioned the Institute for Distribution Research, a MITI-affiliated organization, to make a survey of transaction terms in several sectors including photographic film which was completed in 1969. It reported that foreign manufacturers posed a threat to the oligopolistic distribution system dominated by Fuji and Konica, and emphasized that rationalizing and standardizing transaction terms was important to address this concern.

6.149 According to the United States, based on the 1969 survey, MITI Business Bureau prepared transaction terms guidelines for the photographic sector which were published in a photo industry journal in September 1969. The draft guidelines advocated each of the three transaction terms important for distribution keiretsu-nization, i.e., shortening of payment terms, and greater use of volume discounts and progressive rebates. The United States notes that although Japan disputes promoting progressive rebates, these published draft Guidelines stated, "[w]ith regard to rebates, progressive rebates should be aggressively promoted in order to facilitate large volume transactions".

[90]Ryutaro Komiya, Industrial Policy of Japan (Academic Press Japan, Inc. 1988) pp. 15-18, US Ex. 59.

6.150 The United States continues that in March 1970, MITI published the final Guidelines for Standardization of Transaction Terms for Photographic Film[91] that called for the standardization[92] of transaction terms in order to "prevent disruption of the established order of trade by foreign capital". The final Guidelines noted that the terms between manufacturers and wholesalers already were in a desirable state, but as between primary wholesalers and secondary wholesalers and retailers, the final Guidelines repeated the call for shortened payment terms and volume discounts.

6.151 **Japan** concedes that the 1970 Guidelines did constitute a form of administrative guidance. However, in its view, that fact alone does not establish that they were "measures" for purposes of non-violation complaints. In this regard, Japan recalls its argument that the United States relies on a distorted characterization of administrative guidance in the Japanese system because the United States attempts to lump all administrative guidance into one catch-all category of informal but nonetheless binding regulations. Japan contends that not all administrative guidance is the same. With regard to the issue of whether administrative guidance constitutes the substantive equivalent of formally binding regulation, the panel on *Japan - Semi-Conductors* found that each set of guidance must be evaluated on a case-by-case basis and not based on a mechanical rule.[93]

6.152 In Japan's view, an examination of the contents of the 1970 Guidelines makes clear that the government action in this instance was nothing more than recommendations. Japan emphasizes that MITI merely issued promotional guidance with (1) no government-provided benefit attached to compliance, and (2) no government sanction attached to non-compliance. Accordingly, the administrative guidance reflected in the 1970 Guidelines does not meet the two criteria outlined in *Japan - Semi-Conductors*. Japan explains the difference between the administrative guidance in *Japan - Semiconductors* and the 1970 Guidelines as shown in the table below:

[91]MITI, "Guidelines for the Standardization of Transaction Terms for the Photofilm Industry", 1970, reprinted in Zenren Tsuho, July 1970, US Ex. 70-4.

[92]Japan notes that the United States consistently translates "tekisei(-ka)" as "standardization" rather than the more accurate alternative "rationalization." In Japan's view, if the Japanese original had meant "standardization", it would have used the term "Ityoujun-ka".

[93]*Japan - Semiconductors*, BISD 35S/116, 154, para 108.

COMPARISON OF ADMINISTRATIVE GUIDANCE IN *JAPAN - SEMICONDUCTORS* AND THE 1970 GUIDELINES

Semiconductors Panel	1970 Guidelines
specific request to companies not to export semiconductors at prices below the cost of production to third country markets (paras. 99, 115)[94]	several general suggestions of basic principles to rationalize trade terms, no single specific instruction for which the Government of Japan could verify compliance
mandatory data collection requirements imposed on each individual semiconductor producer (para. 99)	one time factual survey before Guidelines; no data collection system after the Guidelines was developed to measure compliance
The Government of Japan created "statutory requirement" to provide data, and created "heavy penalties" for non-compliance, including fines and prison terms (paras. 99, 113)	no penalties at all for non-compliance; some suggestions were followed, others were not followed; no legal basis for any penalties
systematic price and cost monitoring for "precise identification" of individual companies not complying with dumping requirements (paras. 99, 113)	no specific follow up at company level; only a one time request that the association report generally on what was being done; only 1 of 3 associations replied
more stringent export licensing practices, in order to improve the effectiveness of the monitoring efforts (paras. 112, 116)	no effort to expand scope of some other law to improve compliance, or bring industry within the scope of other regulatory regimes
created a new system of quarterly supply and demand forecasts, with the Government of Japan playing the "decisive role" in implementing the system (paras. 99, 114)	no new system of developing data to help guide the industry, or to monitor compliance
implementing formal international arrangement, with formal government commitment to "ensure" no third country dumping (para. 110)	no formal international agreement to pursue rationalization of trade terms; no formal commitments to another country
the Government of Japan itself had touted in writing the effectiveness of measures in meeting its obligation "to ensure" no third country dumping (paras. 112, 116)	no written claims given to other countries about the effectiveness of the 1970 Guidelines in realizing objective.

[94]References to paragraph numbers are to the panel report in the *Japan - Semiconductors* case. BISD 35S/116.

6.153 Japan explains that the text of the 1970 Guidelines and their transmittal letter to the film industry make clear that compliance with the guidelines, although obviously recommended, was purely voluntary. According to Japan, in some instances, specifically with respect to curtailing rebates, industry flatly ignored the guidelines. Furthermore, Japan points out that no government benefit was contingent upon following the recommendations of the 1970 Guidelines and that MITI did not prod compliance with its recommendations.[95] The Japanese Government had made no formal agreement with another foreign country committing to distribution modernization. Japan emphasizes that MITI did not establish any ongoing institutional mechanism that was "essential" for achieving compliance. Thus, in Japan's view, MITI's 1970 Guidelines were fundamentally different from MITI's efforts to control semi-conductor pricing. In the semi-conductor situation, MITI was attempting to pressure private parties to act contrary to their perceived interests in furtherance of a public policy goal, i.e., honouring Japan's formal commitment to the United States. However, with respect to the 1970 Guidelines, the recipients of the Guidelines were asked to submit a one-time progress report on their implementation of the Guidelines' recommendations, but whether to submit a report or not and the content of the report was left to their discretion. Japan argues that when it became apparent that some of the Guidelines' recommendations were being ignored, MITI did nothing. For Japan, the fact that two decades later, MITI was still addressing the same traditional business practices in its 1990 Guidelines shows the difference between MITI's suggestions and actual legally binding obligations. Japan argues that if the 1970 Guidelines were legally binding, the problematic business practices would have been eliminated and there would have been no need for the 1990 Guidelines. Japan concludes that there was no indication of an ongoing monitoring and enforcement system established and administered by MITI.

6.154 In response to Japan's argument that the 1970 Guidelines were merely suggestions that its industry could chose to adopt or reject as it saw fit, the **United States** submits that the 1970 Guidelines were preceded and followed by a near continuous series of measures, including surveys and studies carried out at the behest of the Japanese Government by organizations it controlled or dominated, reports and monitoring by MITI of implementation of its Guidelines, and promulgation of standard contracts and specific industry guides to bring about industry acceptance and implementation of the measures.

6.155 The United States questions Japan's contention that MITI did nothing to follow-up its issuance of the 1970 Guidelines. It notes that when publishing the Guidelines in an industry journal, MITI explained that the Guidelines were "abstract" and "the greatest common denominator" and that industry associations were asked to formulate and implement more specific transaction terms based on the Guidelines and to report back to MITI by November 1970. The United States submits that, in response to MITI's demand, the photospecialty wholesalers association promptly published a "Transaction Outline" to implement the association's own transaction terms based on the MITI Guidelines and reported it to MITI. With respect to payment terms, the Outline gave specific content to the Guidelines' call for shortened payment terms. As for rebates, the Outline stated, "with regard to quantity-related [volume] rebates, these will be adopted toward mass distribution of products under sound and fair competition". The United States argues that, although the Outline did not mention standardization of transaction terms, nonetheless, the Outline in itself amounted to an exercise of standardization because it was an outline by an industry association of business practices that the association intended to pursue.

6.156 The United States further submits that in 1971, MITI republished the 1969 survey report on transaction terms in the photo film sector originally written by the Institute for Distribution Research.[96] The new publication contained in addition an extensive report setting forth the particular transaction terms

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[95]Japan notes that the cover letter, accompanying the 1970 Guidelines, said, "[W]e expect that the transaction parties understand the need for trade rationalization and make voluntary efforts for such a purpose."

[96] MITI Business Bureau, Actual Conditions of Transaction Terms in the Wholesale Industry, 21 August 1971, US Ex. 20.

in use between manufacturers and each primary wholesaler (identified generically) and between each primary wholesaler and secondary wholesalers. In the US view, the publication of this specific information supported the standardization of transaction terms by allowing the primary wholesalers to know what terms their competitors were offering. The United States underscores that the republication of the survey under MITI's name emphasized that the survey and its recommendations reflected MITI policy.[97]

6.157 **Japan** notes that information such as examples of actual transaction terms is quite common in such factual surveys. There is no indication the survey evaluated any specific terms either favourably or unfavourably, and thus they could not be "targets."

6.158 The **United States** underlines that, as part of MITI's effort to systematize distribution, in 1971 MITI commissioned the Chamber of Commerce, along with the MITI-established Transaction Terms Standardization Committee and domestic photographic materials trade associations, to draft a "Model Contract" based upon the standardized transaction terms outlined in the 1970 MITI Guidelines for the photographic film sector. When publishing the standard transaction contract for photographic film in spring of 1972, the Chamber emphasized that its actions were pursuant to a MITI mandate.[98] For the United States, this emphasis on MITI policy was important, because the Chamber in Japan has broad authority to act on behalf of MITI in many government programs, including the administration of subsidies and other government benefits.

6.159 According to the United States, MITI continued to promote standardized transaction terms. In 1973, MITI published under its name materials by the quasi-governmental Transaction Terms Stabilization Committee.[99] In republishing this material from the Committee, MITI noted that it too "plan[ned] to move forward with measures for standardizing transactions". Accordingly, MITI commissioned the Chamber to publish, in 1975, a compilation and commentary, entitled "Recommendation on Standardized Contracts for Transactions" (the "Chamber Guidance").[100] The Chamber Guidance also addressed payment terms and discounts, among other terms of the standard contract. Regarding payment terms, the Chamber Guidance elaborated on the need for monthly payment in cash, and for the use of notes with fixed terms and interest - again pushing for short payment terms. It also called for cash discounts to reward the prompt payment of accounts. Regarding volume discounts and rebates, the Chamber Guidance stated that the volume discounts in the film sector operated "the same

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[97]The United States notes that the republished version of the survey bluntly notes that the photo film industry "has established a distribution system where oligopolistic manufacturers lead". It then continues to cite as two threats to this oligopolistic system: "As future problems, we can cite first the 'growth of retail routes (especially regular chains and supermarkets) other than the photo retail route and changes in transaction terms due to this leadership,' and secondly the 'effects of full participation of Eastman Kodak'". According to the United States, the survey focused on transaction terms as the response to these challenges. With respect to rebates, the survey stated that there was too much emphasis on rebates that accord significant discretion to the sellers, and not enough emphasis on progressive rebates with clear standards that function as volume discounts. However, the United States claims that there is a mistranslation of the passage on rebates in Japan Ex. B-1. The United States supplied the corrections in US Ex. 20, pp. 308-09.

[98]"The drafting of a standard transaction contract for photographic film, which was commissioned to the Japan Chamber of Commerce and based on MITI's 'Transaction Standardization Guidelines for Photographic Film,' was completed and published". Nihon Shashin Kogyo Tsushin, 1 July 1972, p. 20, US Ex. 24.

[99]The Committee's findings stated that "the standardization of transaction terms is essential for ... systematizing distribution activities as well as countermeasures against foreign capital".

[100]The Chamber Guidance reiterated that the reasons for promoting standardized transaction terms included, "to establish the standards for proper transaction terms in order to prevent disorder in transactions arising from capital liberalization". Japan Chamber of Commerce, Recommendations on Standardized Contracts for Transactions, Commission by Ministry of International Trade and Industry, July 1975, p. 3, US Ex. 32. The Chamber noted that it prepared the 14 standard contracts in cooperation with the "involved industries based on the [MITI] Guidelines" and expressed its "expectation that such measures will expand even more so that the idea underlying the Guidelines will become diffused among the general business community". Ibid., p. 4.

as rebates". The Chamber stated that the terms of such discounts should be stipulated, but it did not otherwise call for their alteration or elimination.[101]

6.160 The United States argues that, while the Chamber's standard contract did not mention standardization of transaction terms, the very publication of a standard contract by Japanese industry amounts in itself to an exercise in standardization. The United States notes that regarding payment terms, the Chamber's standard contract called for payment in cash on a monthly basis which is a short time frame for settling accounts. Regarding discounts, the standard contract called for the use of volume discounts, and for discounts to reward the prompt payment of accounts. Moreover, to follow up on dissemination and implementation of the standard contract, in 1974 and 1975 the Chamber, in cooperation with trade associations, conducted "Standardized Contract Dissemination Explanation Sessions" in several cities.

6.161 In the US view, the implementation and standardization of the transaction terms advocated by the Japanese Government was in the manufacturers' interest. However, unifying the transaction terms of different manufacturers can be difficult, as competition for wholesalers can lead manufacturers to strike different bargains. The United States emphasizes that Government monitoring of specific transaction terms and government support for their "standardization" can provide a discipline against any wholesaler or retailer resistance to these terms. Given that the particular transaction terms advocated by MITI did not necessarily serve the interest of wholesalers,[102] in the US view, the Japanese government would have to extend more effort at "concerted adjustment" with the wholesalers in order to implement standardized transaction terms at that level of the distribution process. The United States emphasizes that the implementation of MITI's transaction terms policies would least benefit the retailers.[103] Therefore, the strongest resistance could be expected from retailers and, accordingly, the greatest need for the Japanese Government to create strong rewards or punishments to retailers to earn their compliance in the system. Given this background, according to the United States, Japan took a variety of steps to implement and standardize the transaction terms in the photographic film and paper sector.

6.162 The United States emphasizes that the extensive interaction between government and the private sector, e.g., regarding transaction terms, demonstrates that the Japanese Government went to great lengths to ensure that its policies were adopted. The repeated advocacy and monitoring built peer pressure and served as a constant reminder that the Government was watching and pushing for these changes. Moreover, in the classic "concerted adjustment" method, MITI did not proclaim from on high, but involved the interested industry groups in the study, monitoring, and implementation process in order to build consensus. The United States claims that MITI also applied pressure to the process where necessary, completed with specific information on the transaction terms applied by individual companies that exposed the extent to which the industries were falling short of MITI's policies. The United States stresses that public exposure and embarrassment is one of the tools MITI uses to enforce its administrative guidance. Moreover, the exposure of this company-specific information facilitated standardization by allowing each company to have a sense of the terms offered by its competitors. In the US view, MITI also applied pressure through the Chamber of Commerce which disposes of significant authority to

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[101]The United States submits that in 1975, the Chamber published a commentary on standardized contracts, which discussed the connection between discounts and rebates in the photographic film sector. The standard contract also provided for dispute settlement by arbitration before the Japan Commercial Arbitration Association. The United States points out that the Chairman and executive director of the Arbitration Association are also executives of the Chamber, that its offices are located within the Chamber, and that the Arbitration Association has been a retirement entity for MITI officials. The Japan Commercial Arbitration Association, Dantai Meikan, p. 427, US Ex 86.

[102]The manufacturers' shortening of their payment terms would increase financial pressure on the wholesalers, and the use of rebates and volume discounts could tie them to a particular manufacturer and limit their supplier options. On the other hand, if the wholesalers were able to impose the same sort of system further downstream, they would reap the same benefits with respect to the retailers as the manufacturers would gain from applying those terms to the wholesalers.

[103]Retailers would suffer the upward shift of economic power and loss of autonomy without having another lower-down level in the distribution system to turn to.

influence the dispensing or withholding of government benefits, and frequently acts as an information-gathering arm for MITI. For these reasons, the United States maintains that medium and small enterprises would have thought twice before ignoring the Chamber's Guidance on transaction terms. Finally, the United States points out that MITI used widespread fear over liberalization of investment in the photographic sector, to pressure industry into adopting the transaction terms policies it advocated.[104] Therefore, the United States concludes that MITI very effectively ensured that industry implemented its guidelines.

6.163 **Japan** responds that no steps were taken to ensure that the 1970 Guidelines were followed, no monitoring of the extent to which the guidelines were adopted took place, and no sanction or other pressures were imposed by MITI even though the Guidelines were not followed. Japan notes, for example, that the "standard contract" presented by the Japan Chamber of Commerce and Industry was made to encourage the private sector to use written forms and to make contracts more transparent, and standardizing any specific transaction terms was not intended. Japan also notes that in any event, there is a serious timing problem to link the 1970 Guidelines and the actual reform of transaction terms or the development of single-brand distribution as alleged by the United States.

(ii) 1975 Manual

6.164 The **United States** further submits that in 1975 the MITI-affiliated Distribution Systemization Development Center published the Manual for the Systemization of Distribution by Industry (Camera-Film)[105] which was prepared in collaboration with industry groups, camera manufacturers, film manufacturers, camera and film wholesalers, camera and film retailers, and camera and film industry publishers. The 1975 Manual reported in detail on the distribution trends in the industry, and made several specific recommendations to combat increased competition from Kodak, including the standardization of transaction terms, including discounts and rebates, the establishment of the Photosensitive Materials Committee for the Systemization of Distribution by Industry (Camera-Film) under the Distribution System Promotion Council,[106] and the promotion of computer linkages (implemented by MITI in subsequent years).[107]

6.165 **Japan** points out that the 1975 Manual is a report prepared by a public corporation, but not by MITI, and thus cannot be considered either "administrative guidance" or a statement of official Japanese governmental policy. MITI commissioned the work in furtherance of its policy of encouraging distribution modernization. Japan points out that there is nothing either in the Manual itself or in the history of subsequent industry action to suggest that the recommendations of the report were adopted by MITI and then imposed as formally or informally binding obligations. Although the Manual was completed, Japan emphasizes that MITI never formally issued the Manual to the industry. According to Japan, the most compelling evidence of industry ambivalence about the 1975 Manual comes from the industry's response to information systemization. Fuji did not establish computer links with its primary wholesalers until 1989.

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[104]As an industry journal article from 1976 submitted by Japan states, "this is the year [of] 100 percent capital liberalization of the film manufacturing industry ... the most feared development by photosensitive material makers". The United States also reports that the article goes on to state that in anticipation of Kodak's possible investment in Japan, Japanese industry had implemented countermeasures "to the point of perfection".

[105]See sub-section II.B.2.(e) above, in particular paras. 2.23-2.25, and US Ex. 75-5.

[106]See sub-section II.B.2.(d) for a description of Distribution System Promotion Council, in particular para. 2.20.

[107]See sub-section VI.D.3.(f) on "Electronic information links" infra for a discussion of MITI's promotion of computer linkages, in particular paras. 6.380-381.

(b) Current effectiveness

6.166 With respect to the specific distribution measures at issue, Japan emphasizes that only one of the items specifically identified by the United States (i.e., international contract notification) was still in effect at the beginning of the Panel proceedings.

(i) Reports, surveys, plans and manuals

According to Japan, the following five reports or surveys were never government actions at all:

(3)1968 Sixth Interim Report of the Industrial Structure Council Distribution Committee;
(4)1969 Seventh Interim Report of the Industrial Structure Council Distribution Committee;
(5)1969 Survey on Transaction Terms;
(8)1971 Basic Plan of the Distribution Systemization Promotion Council;
(9)1975 Manual of the Distribution Systemization Development Center.

Moreover, any substantive relevance of these reports ended when the advice was either acted upon or ignored.

(ii)JDB/SMEA funding and international contract notification

6.167 With respect to four of the items challenged by the United States, Japan concedes that they were once "measures", i.e.,

(2) 1967 JFTC Notification 17;
(7) 1971 International contract notification;
(10) 1976 JDB funding;
(11) 1967 SMEA funding.

6.168 As to their current effectiveness, Japan points out that the allegations about SMEA financing in 1967 and the JDB loan to Konica in 1976 were both factually specific events that happened and were finished more than two decades ago.

6.169 According to Japan, the requirement for international contract notification was technically still in effect as of 20 May 1997, but there was already a pending proposal to repeal this measure. This law was in fact enacted and became effective in June 1997, making it unnecessary for any international contracts to be notified to the JFTC. Simultaneously, the JFTC Rule No. 1 under Article 6 of the Antimonopoly Law was abolished. Moreover, in Japan's view, this measure never favoured Japanese domestic film or paper.

6.170 The **United States** emphasizes that Japan can point to just two distribution countermeasures that it purportedly revoked, JFTC Notification 17 and the 1967 Cabinet Decision. The extent to which these measures are inoperative and no longer in force, however, is far less clear than Japan claims.

(iii) 1967 JFTC Notification 17

6.171 **Japan** submits that JFTC Notification 17 was formally abolished in April 1996, thus cannot be in effect and, therefore, falls outside the scope of the present proceedings.

6.172 While the **United States** concedes that Notification 17 has been repealed, it maintains that there are other provisions that make the repeal of Notification 17 meaningless. According to the United States, premiums from manufacturers to wholesalers are still subject to JFTC Designation 9 of JFTC Notification 15 of 1982, i.e., the provision governing the use of "unjust inducements" under the Antimonopoly Law. That designation prohibits premium offers in excess of "normal business practice". Given that

Notification 17 set industry practice for 19 years, for the United States, it is uncertain at best as to whether present restrictions under Designation 9 will differ at all from the situation under Notification 17.

6.173 **Japan** responds that JFTC Designation 9 does not violate the WTO Agreements. Moreover, Japan contends that the United States raises a measure or a policy that was not listed in its panel request. Thus Japan encourages the Panel to dismiss the US claims concerning all measures and policies that were not specifically identified in the US panel request, including the claims made concerning JFTC Designation 9.

(iv) 1967 Cabinet Decision

6.174 Japan submits that the 1967 Cabinet Decision was formally repealed on 26 December 1980.

6.175 While the **United States** concedes that the 1967 Cabinet Decision has been repealed, it argues that the repeal affects only that portion of the decision relating to controls on international investment in Japan. The United States is, however, unaware of any evidence to suggest that the 1980 decision revoked the distribution policies and liberalization countermeasures directed by the 1967 decision. The 1980 decision mentions only steps that will be taken to lift restrictions on inward foreign investment in line with the OECD, but not countermeasures or distribution policies. The distribution countermeasures arise from a much broader and more recent set of measures than only the 1967 Cabinet Decision. Finally, the United States claims that the 1990 MITI Guidelines have not changed MITI's restrictive policies and measures.

6.176 **Japan** responds that there is ample evidence demonstrating that none of the distribution policies by the United States are currently in effect, and it is impossible to adequately respond to this contention because the United States did not specify which measures it believes resulted from the 1967 Cabinet Decision. However, in Japan's view, if the United States implies that the Cabinet Decision resulted in government actions other than those listed in the US request for a panel, those actions are not properly before this Panel.

(v) 1970 Guidelines and 1990 Guidelines

6.177 While Japan concedes that the 1970 Guidelines[108] were a governmental act relating to the film industry, it explains the reasons why this specific past government action is no longer in effect as follows: In Japan's view, the 1970 Guidelines never had any binding effect, either formal or informal, and thus never were "measures" within the meaning of Article XXIII:1(b), because these guidelines were not "in effect" even from the beginning. In the alternative, even if it were accepted that the 1970 Guidelines were once "measures" within the meaning of Article XXIII:1(b), Japan argues that they are clearly no longer in effect given that after almost thirty years, the business environment has changed so much over this long period that neither MITI nor the private industry considers the 1970 Guidelines as having any current relevance or effect.

6.178 Japan further submits that subsequent events confirm that the 1970 Guidelines have long since lost any relevance. By 1984, rationalizing trade terms was no longer a priority issue. The Report by the Industrial Structure Council entitled, "Distribution in the 1980s"[109], does not even mention the various trade rationalization guidelines issued over the 1970 to 1972 period. The report puts special emphasis on responding to the needs of consumers and supporting small and medium-sized companies.

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[108]Japan Ex. B-24 and US Ex. 70-4. See sub-section II.B.2.(c) above.

[109]Industrial Structure Council, 80 Nendai no Ryuutsuu Sangyou Bijon (Distribution Vision for the 1980s) January 1984, Japan Ex. F-6.

6.179 According to Japan, during the talks on the United States - Japan Structural Impediments Initiative (SII), when the United States argued for a renewed effort to encourage the Japanese distribution system to abandon traditional practices for more economically rational practices, MITI issued a new set of distribution guidelines in 1990.[110] According to Japan, if the earlier 1970 Guidelines were still in effect in any sense, one would have expected the 1990 Guidelines to discuss the earlier suggestions, but they did not. In Japan's view, it is not credible that these MITI suggestions from 27 years ago continue to be a current government action properly subject to WTO review today.

6.180 The **United States** responds that none of the arguments raised by Japan leads to the conclusion that the distribution countermeasures are no longer in effect and that MITI's restrictive policies and measures have changed. The United States maintains that Japan has never stopped intervening in the distribution system for the photographic materials sector. According to the United States, Japan can point to just two distribution countermeasures that it purportedly revoked, i.e., JFTC Notification 17 and the 1967 Cabinet Decision. The United States asserts that the revocation of two distribution and promotion countermeasures does not mean that all of the measures falling within those two groups of measures are no longer in effect. Nor does the issuance of a later guideline retract the prior guidelines and distribution countermeasures. Accordingly, the United States does not agree that these specific measures, and in particular the policies underlying them, have been revoked.

6.181 In **Japan**'s view, the 1990 MITI Guidelines addressed exactly the same kinds of "irrational" business practices as those targeted by the 1970 Guidelines, e.g., rebates, returns and dispatched employees. Yet for the 1990 Guidelines, encouragement of imports was the guiding purpose for targeting these practices. Japan points out that these guidelines had their origin in the Structural Impediments Initiative (SII). In the Final Joint SII Report, MITI made the following commitment: "As to trade practices concerning distribution, an improved environment will be sought from the standpoint of promoting competition and securing market openness".[111] Later in the report, MITI elaborated its plans to issue guidelines on distribution practices.[112]

6.182 Japan emphasizes that in 1990, MITI issued distribution guidelines encouraging the reform of "irrational" trade practices, at the direct request of the United States, to render the Japanese market more accessible to imports. In the current dispute, however, the United States argues that guidelines from 20 years earlier, covering the same subject matter and making the same recommendations, were somehow involved in impeding imports. For Japan it is inconceivable that the same recommendations could be anti-import policies in 1970 and then somehow transform themselves into pro-import policies in 1990.

6.183 The **United States** rejects Japan's contention that MITI's 1990 Guidelines reveal that MITI's distribution policies for the last three decades have not aimed at promoting exclusive, vertically oligopolistic distribution. The United States confirms that the 1990 Guidelines arose out of international pressure on Japan to increase market access, including SII talks between Japan and the United States. Only in reaction to that pressure, the United States argues, Japan introduced guidelines indicating that "international harmony is required" and businesses "must give consideration so as not to have their business practices become obstacles to others [including foreign suppliers]".[113] The United States points out that this statement contrasts with Japan's repeated calls to take countermeasures "in order to prevent disorder arising from" the incursion of foreign capital enterprises, stated in many of the key documents from the late 1960s

[110]US Ex. 90-5, Japan Ex. B-22.

[111]Final Report on the Japan - US Structural Impediments Initiatives (SII), Actions on the Government of Japan Side, 28 June 1990, p. III-1", Japan Ex. B-30.

[112]Ibid. p. III-14, Japan Ex. B-30.

[113]1990 Guidelines, p. 2, US Ex. 90-5.

and early 1970s. The United States concludes that the 1990 Guidelines depart in an important respect from the many policy documents in the late 1970s addressing transaction terms.[114]

6.184 The United States explains that based on positive statements by Japan in the context of the SII, the United States has taken the position that the 1990 Guidelines have the potential to help improve market access in the distribution sector (as Japan promised), if Japan in fact implements the policies indicated in these positive statements. However, in the United States view, Japan has not implemented these policies in the photographic materials sector or in any other sector. In light of Japan's failure to implement these policies, the United States stated in its November 1996 submission to Japan on deregulation matters,[115] that Japan should implement the contents of these Guidelines. As a result of this failure of implementation, the United States has concluded that Japan in fact has not changed its basic policies on distribution, and in fact has not implemented the positions stated in the 1990 Guidelines to correct the restrictive structures in the distribution system for photographic film and paper.

6.185 For the United States, in considering the implementation of the 1990 Guidelines, it is important to bear in mind that Japan implemented its distribution policies, beginning in the 1960s and 1970s, not by a mere announcement of Guidelines in 1970, but based on the back-and-forth process of "concerted adjustment" between government and industry. That process spanned years and involved continuous government surveying and consulting with the domestic industry, building consensus, issuing reports and guidelines, following up with more surveys and guidance to industry. The United States emphasizes that it would take even greater efforts by MITI to undo what it has done, particularly because the formation of limited foreign access to the Japanese distribution system was in the interest of Japanese manufacturers, whereas its dismantling would pose a direct challenge to the two-company oligopoly of Fuji and Konica.

6.186 The United States claims that to the best of its knowledge, Japan has undertaken no actions in the photographic film and paper sector to follow-up on the 1990 Guidelines. Specifically, the United States submits that MITI has not pursued any meaningful actions to reverse its policies on transaction terms or to address the restricted structure of the distribution system for photographic film and paper in Japan. Moreover, according to the United States, the exclusionary distribution system remains in force in the form it existed in 1990, and an elaborate system of rebates and discounts continues at various levels of the distribution system in this sector.[116] Japan's interpretation of the Antimonopoly Law continues to provide that the use of transaction terms departing from standard industry terms can be an unfair trade practice, and the Antimonopoly Law continues to require reporting of all contracts between foreign manufacturers and Japanese distributors.

6.187 Therefore, the United States concludes that - although the 1990 Guidelines were different from the 1970 Guidelines in their intention to avoid some adverse effects of keiretsu - Japan has not implemented the Guidelines in a way to achieve results, as Japan did with the 1970 Guidelines. The United States takes the position that there is nothing inconsistent with the United States calling for Japan to implement the policies announced in the 1990 Guidelines, while noting that so far Japan has failed to do so.

6.188 As to the US view that the 1990 Guidelines are in direct conflict with the claim about the 1970 Guidelines, **Japan** refers to the US request to the Japanese Government in the latest US

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[114]Specifically, regarding rebates, the 1990 Guidelines emphasize that: "It is desirable for manufacturers to voluntarily refrain from offering rebates aimed at maintaining a keiretsu-based relationship in order to prevent manufacturers from exercising excessive influence over the business of retailers". 1990 Guidelines, p. 8, US Ex. 90-5.

[115]Submission by the US Government to the Japanese Government Regarding Deregulation, Administrative Reform and Competition Policy in Japan, 15 November 1996, Japan Ex. B-23.

[116]Actual Rebate Conditions: Fuji Photo Film Co., Ltd. Versus Eastman Kodak, Co., Toyo Keizai (24 July 1995), US Ex. 90.

recommendations on deregulation issued pursuant to the US - Japan Framework Agreement.[117] In Japan's view, the United States is simultaneously urging Japanese businesses to follow current administrative guidance on reforming irrational business practices of 1990 and urging before this Panel that similar guidance of 1970 has violated US rights under the GATT. In Japan's view, the 1990 Guidelines are no different from the 1970 Guidelines in promoting "a free, transparent and competitive distribution system".

(vi) Conclusions

6.189 In Japan's view, the US claims focus on the past, not the present. Japan contends that those specific items that the United States identified are no longer in effect. MITI's policies resulted in recommendations to industry in the 1960s and '70s on how to modernize distribution practices. These recommendations were made decades ago, and private businesses followed them or ignored them at their own choosing. According to Japan, the five reports or surveys were never government actions at all, and any substantive relevance of these reports ended when the advice was either acted upon or ignored.

6.190 Japan concedes that the requirement for international contract notification in JFTC Rule No. 1 was technically still in effect as of 20 May 1997, but there is a pending proposal to the Diet to repeal this measure that becomes effective June 1997. Japan adds that this law was in fact enacted in June 1997, making it unnecessary for any international contracts to be notified to the JFTC. Simultaneously, the JFTC Rule No. 1 under Article 6 of the Antimonopoly Law was abolished.

6.191 Japan points out that the allegations about SMEA financing (1967) and the JDB loan to Konica (1976) were both factually specific events that happened and were finished more than two decades ago. In Japan's view, the United States has not disputed this fact.

6.192 Japan further submits that the 1996 National Trade Estimate Report on Foreign Trade Barriers ("NTE Report") by the Office of the US Trade Representative provides that "[t]he liberalization countermeasures were implemented between 1967 and 1984".[118] Thus, in Japan's view, the United States implied that the distribution policies at issue ended about 13 years ago. Japan further notes that in this NTE Report, the term "liberalization countermeasures" appears to refer to MITI's distribution policies and investment restrictions.[119] However, according to Japan, the United States has not and cannot point to any current MITI action or policy concerning the distribution sector that in any way nullifies or impairs any tariff concessions. Japan points out that the United States does not identify a single item that occurred after 1977, i.e., almost twenty years ago, and before the first tariff concessions on colour film and paper in the 1979 Tokyo Round results.

6.193 The United States argues that the longevity of the distribution countermeasures does not dictate that they are no longer in effect. The United States contends that Japan's position would suggest that mandatory legislation codified long ago is to be deemed revoked if no enforcement actions are taken under it after some period of time has lapsed. The United States contest this proposition because it overlooks the possibility that a law can be self-enforcing if no party is violating it. Therefore, the United States rejects Japan's assertion that virtually all the distribution and promotion countermeasures are no longer in force.

6.194 In the view of the United States, Japan is continuing to reinforce and supplement these countermeasures in several key ways. First, it is continuing to enforce the Large Stores Law and

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[117]"Monitor and report on adherence by the Japanese business community to the MITI 1990 Guidelines on Business Practices in order to promote a free, transparent and competitive distribution system". Submission by the US Government to the Japanese Government Regarding Deregulation, Administrative Reform and Competition Policy in Japan, 15 November 1996, p. 7, Japan Ex. B-23.

[118]United States Trade Representative (USTR), National Trade Estimate Report on Foreign Trade Barriers (NTE Report) (1996) issued in March 1996, before the United States began this Panel proceeding,

[119]USTR, 1996 NTE Report, p. 209, Japan Ex. F-5.

promotion countermeasures which prevents erosion of the system by restricting the competitive pressures that large retailers and manufacturers attempting to break into the system would provide in the absence of these ongoing restrictions. Second, the Japanese government is continuing to support the structure of the system through business assistance programs. Third, Japan's passage of the Business Reform Law and its initial designation of the photographic materials sector for assistance under this broad measure demonstrates Japan's ongoing effort to reinforce the structure of the system established by the initial distribution countermeasures so that it remains a bulwark against penetration by imports.

6.195 The United States emphasizes that the actions needed to maintain the exclusionary distribution structure are different from the measures needed to create the structure in the first instance. For example, once Konica had received a JDB subsidy and built a new joint distribution center with its wholesalers, it had established a new, closer degree of integration with those wholesalers, accomplishing the purpose of the subsidy. From that point on, it no longer needed a subsidy for this purpose. Similarly, the amount of effort the Japanese Government expended to assist in the initial information link-up of Fuji with its wholesalers exceeds what is currently needed for Fuji to maintain those information links and the control over the distribution system.

6.196 The United States maintains that with respect to the promotion of joint distribution facilities and information links between manufacturers and distributors there is no indication that the policy underlying Japan's actions has changed and it continues to be governmental policy of Japan.[120] The fact that Fuji and Konica have built these systems and facilities in conformity with Japan's policies, and that they therefore currently might need less assistance and promotion from the Japanese Government, proves only that these companies have complied with their Government's wishes. According to the United States, there were no meaningful efforts by Japan to suggest to either of these companies to change its course regarding information links and joint distribution facilities.

6.197 The United States further argues that in the case of transaction terms, there is no indication that Japan has changed its policies in favour of standardized transaction terms, and Japan has made no meaningful efforts to implement any changes in rebate and discount practices in the photographic film sector. According to the United States, Fuji continues to maintain a highly complex rebate and discount scheme. In the absence of forceful implementation of a change in policy by Japan, Fuji's rebate scheme will continue to favour "channel exclusivity", standardized transaction terms will continue to provide a benchmark against which to judge whether non-standard terms are "unfair trade practices", and the JFTC's international contract notification rules will continue to allow automatic scrutiny of contracts between foreign manufacturers and Japanese wholesalers.[121]

6.198 In summary, the United States concurs with Japan on the proposition that a finding of non-violation nullification and impairment may be based only on measures that are currently in force. The United States does not believe, however, that Japan has presented credible evidence that its intervention in photographic material distribution is merely a fact of the past.

6.199 **Japan** argues that the United States may be of the position that the alleged measures, even if not in effect any more, are still actionable, because their "effects" or "consequences" are sustained by other items which are not included in the terms of reference. In Japan's view, however, the United States should not be allowed to make such an argument. Japan stresses that what matters should be whether the alleged measures listed by the United States are *themselves* in effect or not. Any items outside the terms of

[120]The United States notes that the JDB program that provided the loan to Konica remains in place, and Japan generally has continued to advocate and financially support joint distribution facilities and electronic information ties between manufacturers, wholesalers and retailers. See e.g., MITI's 1990 Guidelines, p. 9, US Ex. 90-5 and Photo Industry Information System Manual, US Ex. 96.

[121]Japan contends that a bill to repeal the international contract notification requirement was passed in June 1997, and simultaneously JFTC Rule No. 1 under Article 6 of the Antimonopoly Law was abolished.

reference for this panel cannot substitute for the items within them. Japan notes that the United States did not argue that the alleged measures inside the terms of reference and items outside of it in combination have had certain alleged effects. If the United States believes that the alleged measures (in the terms of reference) are still in effect, it should have presented a "detailed justification" for claiming the alleged measures remain in effect by themselves. In Japan's view, the US attempt to point out other items does not meet the requirement of "detailed justification."

3. PROMOTION "COUNTERMEASURES"

(a) The Councils and Codes

6.200 As far as the JFTC related issues are concerned, **Japan** agrees with the United States that the following are governmental "measures" within the meaning of Article XXIII:1(b):

(i) the Premiums Law (as amended);
(ii) the JFTC Notifications; and
(iii) the approval by the JFTC of fair competition codes.

6.201 The **United States** submits that the private sector plays an important role in enforcing Japan's promotion countermeasures by virtue of the system of so-called fair competition codes and fair trade councils. Japan is alleged to have deputized fair trade councils as enforcement surrogates for the JFTC under the Premiums Law. The United States asserts that industry trade associations play an important role in the fair trade councils and, in some instances, dominate the affairs of a particular council. The United States clarifies that in this dispute it is concerned with the actions of trade associations only as they relate to a code or council. In the US view, Japan should bear responsibility for a council whose formation it promoted and approved, as well as the rules and codes which that council promulgated.

6.202 The United States argues that, even though individual aspects of Japan's promotion countermeasures approximate facets of measures elsewhere, the United States is unaware of any nation with a regime that is equal to Japan's. In particular, no nation has an enforcement mechanism of government/industry cooperation akin to Japan's system of "fair trade councils" and "fair competition codes." This system allows powerful businesses and trade associations to formulate a set of competition rules and, with the assistance of the government, impose those standards not only on members of their groups but on non-members as well.[122] The United States argues that industry "fair competition codes" played a critical role in the JFTC's assessment of what constituted "normal business practices" in applying the promotion countermeasures. If there is a fair competition code, then the code will be used as the standard. If none exists, the JFTC will make a determination after investigating the business practices of that industry or issue guidance to the industry to establish a fair competition code. This close government/industry relationship has been used to stifle foreign competition such as when the Promotion Council worked with the JFTC to undermine Kodak's VR campaign before it even began.[123]

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[122]Severe Restrictions Placed on Businesses for Premium Offers: Shatokuren Hears JFTC Explanations at Jyosui Kaikan on the 12th, Nihon Shashin Kogyo Tsushin, 20 June 1967, US Ex. 67-8.

[123]In the US view, Japan failed to provide any evidence contradicting the US recitation of events regarding the VR campaign. Japan contends that statements contained in Mr. Ishikawa Sumio's affidavit of the United States are not substantially objective evidence and therefore are not trustworthy.

6.203 According to the United States, Japan's photographic materials sector has four relevant councils:

(1)the Manufacturers Fair Trade Council,
(2)the Wholesalers Fair Trade Council,
(3)the Photographic Industry Fair Trade Promotion Council, and
(4)the Retailers Fair Trade Council.

The United States emphasizes that with respect to the two councils most relevant to the US case, i.e., the Promotion Council and the Retailers Fair Trade Council, trade associations dominate the activities and policies of each council.

6.204 **Japan** argues that a fair competition code does not by itself constitute a "measure" of the Government of Japan for the following reasons. A fair competition code is an agreement, or a contract, among non-government industry members. Its enforcement will have to be affected, ultimately, by the judiciary, and the JFTC has no role to play in the enforcement process. It is only when parties to the code fail to observe the Premiums Law, Notifications, or other JFTC regulations, that the Commission takes any action. Industry members may freely choose whether or not to participate in a code. The JFTC does not demand membership. According to Japan, the rationale for such a mechanism is well understood overseas as well: For example, the "guidelines on codes of practice" prepared by the United Kingdom's Office of Fair Trade state that "[t]he code or articles will also set out the penalties for non-compliance up to and including dismissal from the association."[124] Similarly, the Annual Report 1987-1988 of Australia's Trade Practices Commission states that "[c]odes should include commercially significant and realistic sanctions for their enforcement."[125]

(i) Manufacturers' Council

6.205 The **United States** argues that prior to the establishment of the Retailers Council, Japan established two fair trade councils in cooperation with the manufacturers and wholesaler associations. Pursuant to Article 10 of the Premiums Law, the JFTC approved on 15 October 1965 the "Fair Competition Code Regarding Restrictions Premiums Offers by the Cameras and Related Products Manufacturers' Industry" ("Manufacturers' Code") "to enable this Code to be enforced smoothly and effectively". Article 4 of the Manufacturers' Code established the Camera Manufacturers Fair Trade Council ("Manufacturers' Council"). Article 4 further defines the duties of the Manufacturers' Council, which include the responsibility to "investigate those who may be in violation of the code" and to "take necessary measures against those who have violated the Code".

6.206 **Japan** notes that Kodak Japan Limited (Nagase Sangyo, until 1988) has been participating in the Manufacturer's Council as a camera manufacturer since 1988.

(ii) Wholesalers' Council

6.207 According to the **United States**, the JFTC similarly approved the "Fair Competition Code Regarding Restrictions of Premium Offers by the Cameras and Related Products Wholesalers Industry" ("Wholesalers' Code") on 29 October 1966. Article 4 of the Wholesalers' Code established "the Cameras and Related Products Wholesale Industry Fair Trade Council ("Wholesalers' Council"). Article 4-3 defines the duties of the Wholesalers' Council. Articles 5 and 6 authorize the Wholesalers' Council to investigate violations and to take measures against violators, including the imposition of fines.

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[124]Japan Ex. D-72 and Ex. D-73.

[125]Trade Practices Commission, Annual Report 1987-1988, p. 114, Japan Ex. D-74 and Ex. D-44.

(iii) Promotion Council

6.208 The United States further submits that the Photographic Industry Fair Trade Promotion Council ("Promotion Council") is a vertically-integrated industry association representing every stage of the distribution of photographic materials and equipment, with the photosensitive materials distributors' association (Shashoren) and the Retailers Association (Zenren) being the primary beneficiaries of the organization. The United States points out that the JFTC created the Promotion Council by administrative guidance.[126]

6.209 According to the United States, the fact that the JFTC oversees the fair trade council is illustrated by Article 17 of the Promotion Council's articles of association which provides:

"Establishing or abolishing the provisions of these Articles of Association and the responsibilities of this Council shall require prior approval from the Japan Fair Trade Commission".[127]

6.210 In the view of the United States, the delegation of authority from the JFTC to the Promotion Council is made explicit in Article 4 which confers upon the Promotion Council a number of enforcement powers. Article 4 provides:

"In order to achieve the objectives which were described in Article 3 above, the Council will create a committee which will be responsible for the following: ... secure fair transaction order between all elements of the distribution system, manufacturers, wholesalers, and retailers. Take the necessary actions against those who violate the Self-Regulating Measures. Liaise with the competent governmental authorities. All other responsibilities necessary to achieve the Council's objectives".

Accordingly, the same association-council dynamic exists between the Promotion Council and the JFTC as it is true with respect to the Retailers Council and the JFTC, which is described below. The Promotion Council has received a similar delegation of authority from the Japanese Government.

6.211 **Japan** responds that industry self-regulation is private-sector conduct, and not a government "measure". Japan explains that the Promotion Council is a private-sector organization, which was established by the camera industry to implement voluntary standards on dispatched employees, and that has no governmental authority.

6.212 The **United States** responds that the Promotion Council and its first set of rules, governing dispatched employees, were established under guidance from the JFTC.[128] According to the United States, Japan admitted that "the Promotion Council was established after consultation with the JFTC" and conceded that "[t]he Promotion Council refers to the JFTC's 'approval' or 'guidance' for its action in its rules."[129] Regardless of whether the Promotion Council is a purely private trade association or a quasi-governmental association, Article 8-2 of the Antimonopoly Law requires that "[e]very trade association ... file a report [with the JFTC] within thirty days as from the date of its formation". JFTC

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[126]The official directive of the Promotion Council states: "This council was established under the guidance of the Japan Fair Trade Commission in December of 1982 for the purpose of securing a fair trade system in the photographic industry, deepening the exchange of ideas and understanding among businesses, and contributing to the development of the industry". National Photographic Industry Fair Trade Promotion Council, No. 1, 29 August 1992, US Ex. 92-7.

[127]Fair Trade Promotion Council Establishment: An Attempt to Improve the Structure of the Industry, Zenren Tsuho, January 1983, pp. 46-47, US Ex. 83-3.

[128]US Ex. 92-7. ("the council was established under the guidance of the JFTC in December of 1982"); US Ex. 83-3 ("the JFTC expressed an understanding [about] establishing the Council").

[129]At the time of the formation of the Promotion Council, the Council's chairman stated that the council had "the stamp of approval of the Fair Trade Commission." Shashin Kogyo Junpo, 20 October 1982, US Ex. 46.

Notification 2 of 1953, as amended, requires such associations to file basic information such as the copy of the articles of association, business plan, membership, and self-regulating measures.[130]

6.213 **Japan** further points out that the JFTC has no statutory authority to approve agreements underlying the Promotion Council. Its action with regard to their agreements on dispatched employees or "develop-print" price representations[131] was a non-binding expression of the view that the agreements would not immediately violate the Antimonopoly Law. In that respect, the status of the Promotion Council is no different from that of their "ordinary" industry associations. Accordingly, Japan concludes that the Promotion Council's individual activities cannot constitute "measures" for purposes of non-violation complaints.[132]

6.214 The **United States** responds that the exemption created by section 5 of Article 10 of the Premiums Law applies not only to the establishment of a fair competition code, but also to "such acts of entrepreneurs or a trade association as have been done in accordance therewith." The United States also was unaware of any reason to view the Promotion Council differently from the other councils relevant to this dispute.

(iv) Retailers' Council

6.215 According to the United States, the example of the Retailers Fair Trade Council ("Retailers Council") displays the relationship between a trade association and a fair trade council and is illustrative of the powers effectively delegated to a trade association by the Japanese Government:

6.216 The United States submits that, since its inception, the Retailers Fair Competition Code ("Retailers Code")[133] has essentially been administered by the photographic retailers trade association, or Zenren, acting as the Retailers Council. According to the United States, it was Zenren that asked the JFTC to approve the establishment of the Retailers Code and since then Zenren officials have dominated the Fair Trade Council's board of directors.[134] Moreover, Zenren's official journal, Zenren Tsuho, is used to disseminate information relating to activities of the council.[135] Zenren and the Retailers Council hold annual meetings at the same time and in the same location, and they even occupy the same offices.[136]

6.217 **Japan** points out that the Retailers Council, which is responsible for the observance of the Industry Code, is established separately from "Zenren," a national federation of prefecture-wide photographic products retailers organizations. The Retailers Council has an independent assembly and an independent board, as well as its own secretariat and budget. In foreign countries, industrial organizations often serve as an implementation organ for voluntary restraints.

6.218 The **United States** submits that the Retailers Code specifies sweeping enforcement powers for the Retailers Council, including enforcement authority under the Premiums Law and other "fair trade" laws.[137]

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[130]The United States mentions that it has requested the Japanese Government to provide copies of the report filed by the Promotion Council. Although the report would not normally contain business confidential information, the Japanese Government refused to provide any documentation relating to the Promotion Council.

[131]Japan states that Kosei Torihiki Joho, the publication the United States cites as an official publication, is in fact not an official publication.

[132]The United States confirmed that the Council actions which they believe are problems are their reaction to the VR campaign, and the 1996 Circular. Japan notes that the 1996 Circular, however, is only an inquiry and does not instruct members to suspend the service of dispatched employees.

[133]US Ex. 87-4.

[134]See, e.g., Zenren Tsuho, June 1987, p. 6-11, US Ex. 87-5.

[135]See the Retailers Fair Trade Council's 1994 and 1995 fiscal year business plans.

[136]Zenren Tsuho, August 1987, pp. 16-20, US Ex. 87-7.

[137]Article 14 of the Retailers Code provides: "The Retailers Fair Trade Council shall perform the following:
(1)Activities pertaining to causing the Code to be thoroughly understood.
(2)Activities pertaining to offering consultation and directions in connection with the Code.

Article 15 of the Code outlines the Retailers Council's powers to investigate suspected violations[138] and Article 16 specifies penalties[139] in the case of a business operator's non-compliance with the Code.

6.219 **Japan** contends that the Retailers' Code, constitutes self-regulation among business entities approved by the JFTC in accordance with the Premiums Law. In Japan's view, the Retailers Council is a voluntary organ established by the Code to implement the self-regulation. Nor does Article 14, paragraph 7 of the Retailers Code serve as a basis to confer on the Retailers Council authority to enforce the Premiums Law. It only gives the Council the task of making the Premiums Law or the Antimonopoly Law more widely understood and observed.

(v) Federation of Fair Trade Councils

6.220 The **United States** further points out that the JFTC has delegated certain authority to an umbrella organization of fair trade councils, i.e., the Federation of Fair Trade Councils (the "Federation"), to manage the operation of Codes. The Federation was established by the Japanese Government in 1979 to promote, coordinate, and cooperate in the implementation of fair competition codes, conduct surveys on the degree of compliance with them, and perform other duties pertaining to the prevention of violations of the Premiums Law.[140] The JFTC convenes the Federation annually to determine policy relating to fair competition codes and fair trade councils, and reports on the Federation activities in its legally mandated Annual Report to the Japanese parliament.[141] According to the United States, the Retailers Council executive director regularly participates in policy meetings with senior officials of the JFTC. Furthermore, the JFTC regularly issues awards through the Federation to reward the activities of the fair trade councils.

(b) Attributability to the government

(i) Fair Competition Codes

6.221 The United States claims that the Japanese Government should bear responsibility for the effects of fair competition codes and the activities of fair trade councils, including trade associations acting under aegis of a code or council because the codes and councils are the creation of Japanese law, specifically Article 10 of the Premiums Law. Subsection (1) of that provision provides:

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(3)Activities pertaining to making adjustments pertaining to how the Code is being observed.
(4)Activities pertaining to investigating the facts when there is suspicion of violation of the Code.
(5)Activities pertaining to taking the necessary steps against those who have violated the Code.
(6)Activities pertaining to processing complaints received from the general consumer.
(7)Activities pertaining to making the Act Against Unjustifiable Premiums and Misrepresentations and other laws and ordinances pertaining to fair trade widely understood and preventing violations thereto.
(8)Activities pertaining to liaison with competent authorities.
(9)Activities pertaining to providing information to the members.
(10)Activities pertaining to other activities connected with implementing the Code".

[138]Article 15 of the Retailers Code provides:

"the Fair Trade Council may summon the parties involved to hear their explanations, send out the necessary inquiries, obtain the opinions of witnesses, and conduct the necessary investigations for other circumstances".

[139]Article 16 of the Retailers Code states:

"[w]hen a business operator is found to be in violation ... the Fair Trade Council may serve a written warning ... When the business operator served with the warning as per the above is found not to obey the same, the Fair Trade Council may levy on the business operator a penalty of up to 500,000 yen, or dismiss it from the membership of the Fair Trade Council, or when necessary, request that the Japan Fair Trade Commission take the necessary measures".

[140]The Fair Competition Code System and Status of Establishing Fair Competition Codes, Kosei Torihiki, No. 390, April 1983, pp. 37-38, published by Japan Fair Trade Institute, JFTC, Trade Practice Department, US Ex. 83-8.

[141]1995 JFTC Annual Report Antimonopoly White Paper, July, 1996, pp. 247-251.

"Businesses or a *trade association* may, upon obtaining authorization from the Fair Trade Commission in accordance with the Rules of the Fair Trade Commission, with respect to matters relating to premiums or representations, conclude or establish an agreement or a code, aiming at preventing unjust inducement of customers and maintaining fair competition. The same shall apply in the event alterations thereto are attempted".[142]

In the view of the United States, Article 10(1) makes clear that the establishment of the code is subject to approval by the JFTC. Similarly, Article 10(3) states that the operation of the codes and councils is subject to JFTC supervision.

6.222 The United States emphasizes that the power of the Retailers Council and Zenren - like all other councils and trade associations - is even greater because Article 10 of the Premiums Law exempts their activities from antitrust enforcement. Article 10(5) of the Premiums Law states that:

"The provisions of Section 48 [recommendation, recommendation decision] and Section 49 [initiation of hearing procedures], Section 67(1) [urgent injunction] and Section 73 [accusation] of the [Antimonopoly Law] shall not apply to the fair competition code that has been authorized under Subsection (1), and to such acts of entrepreneurs or a trade association as have been done in accordance therewith".

6.223 **Japan** replies that council actions under an approved code are not exempt from the operation of the substantive provisions, e.g., prohibitions of unfair trade practices, of the Antimonopoly Law. For the JFTC, anything a council does is actionable, just as activities of other associations. The only legal consequence of the JFTC approval is that it must first revoke the approval before it enforces the Antimonopoly Law against an approved code or implementation thereof.

6.224 Japan explains that according to Article 10 of the Premiums Law entrepreneurs or a trade association may conclude or establish a code ("fair competition code"), aiming at the prevention of unjust inducement of customers and maintaining fair competition. The Law also provides that such code be concerned with matters related to premiums or representations, and that it must be approved by the JFTC.[143] Accordingly, with regard to other matters, such as the dispatch of employees, entrepreneurs cannot conclude a "code". Japan submits that the JFTC may approve a "code" only when it is found to meet strict conditions.[144] Before deciding whether or not to approve a "code", the JFTC holds public hearings to receive opinions from general consumers, people of learning and knowledge as well as representatives from enterprises concerned. The Premiums Law further provides the JFTC with oversight authority, allowing the JFTC to subsequently revoke its approval. When the JFTC approves a "code", it is published in the official gazette. Japan argues that the approval by the JFTC has the effect of a confirmation that the content of the "code", as well as acts done in compliance with the code, does not violate the Antimonopoly Law.[145]

(ii) Fair Trade Councils

6.225 Japan explains that, for the purpose of implementing and observing the code effectively, the parties (entrepreneurs) to the "code" usually organize themselves into a private body called a fair trade council, composed of the members of the code, which are legally distinct from the existing trade association.

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[142]US Ex. 62-6 (emphasis added).

[143]Article 10 (1) of the Premiums Law.

[144]According to Article 10 (2) Premiums Law a "code" may be approved only if:
(i) it is appropriate for preventing unjust inducement of customers and to maintain fair competition;
(ii)it is not likely to impede unreasonably the interests of consumers in general or the related entrepreneurs;
(iii) it is not unjustly discriminatory; and,
(iv)it does not restrict unreasonably the participation in or withdrawal from the fair competition code.

[145]Article 10 (5) Premiums Law.

Although approved codes may contain provisions on the establishment and operation of councils, in Japan's view, the councils remain private organizations because the approval of the establishment of an organization composed of private parties does not render the organization a governmental entity. Many codes provide that the council may or must take the following actions:

(a)The council is to report to the JFTC the decisions made at the annual meetings of the council.
(b)The council is to report to the JFTC the fact of having taken such actions as
(i) requiring breach-of-contract damages for the disobedience of the code, or
(ii) expulsion of a member who did not obey the code.
(c)The council may request the JFTC to take necessary measures against those members who did not obey the fair competition code.

The actions in (a) and (b) above are intended to ensure that the JFTC is informed of main developments regarding the operation of the code. With regard to actions in (c) above, the JFTC is not obliged to take any action in response to such approaches from the councils.

6.226 Japan states, however, that it is not obligatory for a code to have provisions regarding the above-mentioned actions. They are included in the code based on the voluntary decision of the members of the code. Japan further notes that councils are not required to, and actually do not, seek the JFTC's approval on such matters as its annual business plan or budget, appointment of personnel, or its individual actions. Japan further emphasizes that fair trade councils are not governmental or even semi-governmental organizations, and their executive committee members or its staff are not government officials.

6.227 The **United States** alleges that, in effect, the Japanese Government has delegated enforcement authority under the Premiums Law to fair trade councils and the industry trade associations that comprise them. According to the United States, by its very terms, the Premiums Law delegates enforcement authority to trade associations acting as fair trade councils, empowering them to implement JFTC-approved fair competition codes. According to the United States, in this light, the director of the JFTC's division on premiums has explained that

"[t]he approval of the Code means that the role we play to take enforcement actions on violations will be left to the Fair Trade Council. If this expectation is not met, [the approval] will have no meaning".[146]

According to the United States, e.g., Members of the Retailers Council have echoed his sentiments, stating that "[t]he retailers fair trade council is just like a subcontractor for the JFTC".[147]

6.228 The United States further points out that the JFTC, through its approval of the code, confers not only broad authority on private parties to act as surrogate enforcers, but also exempts them from prosecution for their activities. As the JFTC has explained, "even if the contents of the codes or the activities based on the codes violate the Antimonopoly Law, no control measures will be taken based on the Antimonopoly Law".[148]

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[146]Zenren Tsuho, July 1987, p. 7, US Ex. 87-5. Japan contends that "teki-hatsu" should be translated as "discovery" rather than as "enforcement action". See translation issue 20.

[147]Shukan Shashin Sokuho, 7 August 1987, p. 3, US Ex. 87-9.

[148]Jirei Dokusen Kinshi Ho, 15 December 1995, p. 442, US Ex. 95-20.

6.229 **Japan** contends that the enforcing authority of the JFTC may not be delegated to a private body. The kinds of actions which the United States cites as examples of delegation of power are the ones which a council may undertake on its own.[149]

6.230 As to the nature of the relationship between the JFTC and the fair trade councils, Japan notes that the JFTC enforces only the Premiums Law and not the codes. Since fair competition codes are agreements among private entrepreneurs, the specific performance of the codes to the members is ultimately effected by the court. Japan explains that the JFTC is empowered by Article 10 of the Premiums Law to approve a fair competition code drafted by entrepreneurs or a trade association. The amendment of the code also requires the JFTC's approval. The Premiums Law has no provision referring to the council as such. Although codes approved by the JFTC usually contain provisions on councils, the JFTC's legal relationship with the councils is the same as that with ordinary private organizations or enterprises. The JFTC would be ready to take appropriate steps, should the councils be found to be obstructing fair competition.

6.231 Japan emphasizes that fair trade councils are not delegated any powers from the JFTC. With regard to the relations between the JFTC and the prefectural governments, Articles 9:2 to 9:5 of the Premiums Law provide that certain powers are delegated to the latter. However, no such provision exists in Article 10 of the Premiums Law, which deals with fair competition codes. From that, it is clear for Japan that the JFTC cannot delegate any power to non-governmental bodies without explicit authorization by the law.

6.232 Japan points out that the self-regulation codes are not enforceable to members without being approved and published by the JFTC. They are naturally not enforceable to non-members, either. Japan points out that such self-regulatory codes are effective so long as they do not contravene the Antimonopoly Law.[150] However, JFTC-approved codes are applicable to members and can be enforced by courts. According to Japan, many codes have a provision that enables the council to take certain actions against those who do not obey the codes, such as requiring a breach-of-contract damages or expulsion from the code. In this sense, one may be able to say that the code is "enforceable" by the fair trade council. However, Japan emphasizes that the JFTC has no power to approve individual actions taken by the organization composed of the members of the code (the fair trade council). Moreover, many codes provide that the works of the council include:

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[149]Japan states that, e.g., anybody may establish "self regulation for fire prevention", and take enforcement actions, such as a survey, imposition of a penalty, or a request for an action with the appropriate authorities.

[150]The JFTC will regulate self-regulatory agreements when they fall upon one of the following:

(i)the self-regulatory agreements constitute "unreasonable restraint of trade" by entrepreneurs, such as cartel, (Article 3 of the Antimonopoly Law)

(ii)the self-regulatory agreements constitute either

(a) substantial restraint of competition by a trade association, or

(b) unjust restriction of the function or activities of the members of the code.

(Article 8 of the Antimonopoly Law).

(i) making the code better known,
(ii) looking into the possible disobedience of the codes and taking certain actions against it, and
(iii) preventing the violation of the Premiums Law.[151]

In Japan's view, since all of these are actions taken in conformity with an agreement among private parties (i.e., the code) with a view to complying with the rules in the code and the Premiums Law, they cannot be regarded as the use of powers delegated to the council by the JFTC.

6.233 In Japan's view, the fact that councils are authorized to impose "penal fines" on members who violated the codes, is not a case of delegated power. Private persons are basically free to agree (a) that they abide by a certain rule and (b) that those who have broken the rule pay breach-of-contract damages. It takes no delegation of governmental power to make and comply with such an agreement. In many instances, the code provides that when the council has required breach-of-contract damages for the disobedience of the code, the council is to report the fact to the JFTC. Such a provision is intended to make sure that the JFTC is informed of main developments regarding the operation of the code. It is nothing but an "ex post facto" notification, and does not indicate the JFTC's "involvement in" or "responsibility for" the activities of the councils.

(iii) Conclusions

6.234 The **United States** contends that the Japanese Government established its private-sector-enforced code system, at least in part, to counteract the perceived superior marketing abilities and promotion budgets of foreign firms. The United States quotes a leading Japanese antitrust scholar who explained that "[F]air competition codes can also be effective in controlling firms if they disturb the market.[152] Given these circumstances, the United States takes the position that the activities of these councils and associations are attributable to the Japanese Government and fall within the purview of the WTO and this Panel.

6.235 The United States emphasizes that Japan's present position, i.e., that the effects of the codes and councils cannot be attributed to the government, contradicts the position it took in the 1987 *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages* case.[153] In its submission to that panel, Japan stated that "labelling of alcoholic beverages in Japan is *regulated* by a range of *legal controls* as follows: ... (iii) fair competition codes in accordance with the said Act [against Unjustifiable Premiums and Misleading Representations]."[154] Japan further explained:

"Article 10 of the [Premiums Law] establishes the fair competition code system. While the code is a rule voluntarily set by the industry concerned with a view to contributing the correct selection by consumers and assuring fair competition, it requires approval by the Fair Trade Commission. This fair competition code provides for sanctions (imposition of a

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[151]The items usually listed in the code as the works of the council are as follows:
(i) making the codes better known;
(ii) consultation and giving advice on matters related to the code;
(iii) surveys on the situation regarding the compliance of the code;
(iv) surveys regarding possible disobedience of the code;
(v) taking actions against members who did not obey the code;
(vi) dealing with complaints from consumers;
(vii) making the Premiums Law and other laws related to fair trading better known, and preventing the violation of such laws; and
(viii) getting in contact with the government agencies concerned.

[152]Matsushita Mitsuo, Antimonopoly Law and International Transactions, 25 May 1970, pp. 83-84, US Ex. 70-2.

[153]Panel Report on *Japan - Customs Duties,Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages ("Japan - Liquor Taxes and Labelling Practices")*, adopted on 10 November 1987, BISD 34S/83.

[154]Submission of Japan to the panel in *Japan - Liquor Taxes and Labelling Practices*, Annex 9, p. 15 (emphasis added).

> penal sum) against disobedience of the stipulated obligations, in order to ensure its proper enforcement."[155]

6.236 In this regard, the panel on *Japan - Liquor Taxes and Labelling Practices* stated in the section on "factual aspects":

> "Japan enacted various legal regulations in order to prevent the use of trade names in such a manner as to misrepresent the true origin of a product, including the Law for the Prevention of Unfair Competition, the Act Against Unjustifiable Premiums and Misleading Representations, a range of "fair competition codes" voluntarily laid down by each industry concerned pursuant to Article 10 of the latter Act and approved by the Fair Trade Commission, and the Law Concerning Liquor Business Association and Measures for Securing Revenue of Liquor Tax".[156]

6.237 According to the United States, Japan took this position to demonstrate that it had met its obligations under Article IX:6 of GATT, which requires Members to cooperate with one another to protect the trade names of foreign products. In the US view, Japan should not be able to take credit for its system of codes and councils to suit its position in an earlier proceeding only to later claim that the codes and councils have nothing to do with the government.

6.238 **Japan** responds that a "fair competition code" is an agreement among private parties for autonomous control. The passage in the quoted panel report specifically states that "fair competition codes [are] voluntarily laid down by each industry concerned". At the same time, a code approved by the JFTC is also an enforceable agreement. In Japan's view, the expression of "legal regulations" in the above-mentioned report was used in this sense.

6.239 Japan further contends that a fair competition code does not by itself constitute a "measure" of the Japanese Government for the following reasons:

(i) A fair competition code is an agreement, or a contract, among non-government industry members. Its enforcement will have to be effected, ultimately, by the judiciary, and the JFTC has no role to play in the enforcement process. It is only when parties to the code fail to observe the Premiums Law, Notifications, or other JFTC regulations, that the Commission takes any action.

(ii) Industry members may freely choose whether or not to participate in a code. The JFTC does not demand membership.

6.240 Japan further submits that also individual activities carried out by a fair trade council or other industry association are not "measures". Japan notes that a fair trade council is not granted a particular status in the law, nor is it subject to special control or guidance of the Government:

(i) The concept or the status of a fair trade council is not defined or regulated by the law. It is an establishment defined and provided for in a code. It is treated as an "industry's association" in no way differently from other such organizations.

(ii) There is no *de jure* or *de facto* presumption of lawfulness conferred on individual activities of a fair trade council. Conversely, unless the council commits an unlawful activity, the JFTC is not authorized to require reporting from the body.

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[155] Ibid. p. 26.

[156] Panel Report on *Japan - Liquor Taxes and Labelling Practices*, adopted on 10 November 1987, BISD 34S/83, 86-87 para. 2.7.

(iii) Participation in a fair trade council is not mandatory.

6.241 Japan further emphasizes that there is no fair competition code which is applicable to photographic film and paper.

6.242 In summary, Japan concludes that activities of fair trade councils or other industry association of this type cannot constitute a governmental "measure" within the purview of Article XXIII:1(b).