

## VII. LEGAL ARGUMENTS CONCERNING VIOLATION CLAIMS

### A. ARTICLE III OF GATT

#### 1. INTRODUCTION

7.1 The **United States** argues that at the beginning of the Kennedy Round, foreign and domestic photographic materials manufacturers sold film and paper to Japan's primary wholesalers who, in turn, distributed these products to secondary wholesalers, photo finishing laboratories and retailers. At that time, manufacturers competed with one another to do business with wholesalers. When the Kennedy Round was concluded, the Japanese Cabinet directed that a framework should be established for "countermeasures to be taken by the Government".<sup>1036</sup> According to the United States, the Japanese Government feared as it reduced formal market barriers that foreign photographic materials manufacturers would establish and expand relationships with domestic wholesalers in order to use the Japanese distribution system to penetrate the Japanese market. The Cabinet specifically called for countermeasures to restrain foreign enterprises and strengthen Japanese competitors.<sup>1037</sup> The purpose of those policies was to foster single-brand distribution for film and exclusive arrangements or affiliations between domestic manufacturers, primary photospecialty wholesalers and photofinishing laboratories, and thereby to exclude imported film and paper from traditional distribution channels. By the mid-1970's, all of the primary wholesalers exclusively handled domestic film and paper. Foreign manufacturers were left with less efficient alternatives such as distribution through smaller, more regional secondary wholesalers or direct-to-retail sales.

7.2 The United States alleges that the Japanese Government has promulgated laws, regulations and requirements that have effectively excluded imported photographic materials from a key distribution channel, i.e., primary wholesalers, and have maintained this exclusion for more than 20 years. Foreign photographic material manufacturers were denied essential opportunities to distribute and sell their products in the Japanese market contrary to Article III:4 which mandates that the conditions for sale and distribution of imported products be no less favourable than those for domestic goods. The Japanese Government is alleged to have engineered this exclusionary distribution system by applying a combination of formal measures with a series of closely-related, informal measures. The fact that Japan at times has employed untraditional and even opaque methods of according less favourable treatment should not stand as an impediment to a legal review under Article III:4.<sup>1038</sup> The United States requests the Panel to examine all the facts surrounding the imposition of the distribution countermeasures, taking into consideration any unique features of the Japanese system of government, in order to determine whether Japan has failed to provide equality of competitive conditions for imported products. Regardless of whether Japan sought to hinder imports or merely help domestic producers, the direct consequences of its actions were to diminish opportunities for foreign photographic material manufacturers to distribute their products. The United States claims that by creating distribution channels open exclusively to domestic manufacturers, Japan intentionally enhanced competitive opportunities for domestic manufacturers to the detriment of imports in violation of Article III:4. By restructuring the photographic

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<sup>1036</sup>1967 Cabinet Decision, pp. 3-4, US Ex. 67-6.

<sup>1037</sup>"Modernization lags behind most in the distribution sector. Here, the power of resistance against the inroad of foreign capital is weak and the impact of foreign capital advancing into this sector will also pose a significant impact in the production sector". "[I]t would be necessary to restrain foreign enterprises coming into Japan after liberalization, from disturbing order in domestic industries by resorting to the strength of their superior power, and from advancing into the non-liberalized sectors by evading control". "The establishment of countermeasures for strengthening the capacity of our enterprises for international competition and for preventing foreign enterprises from disturbing order in our industries and market would be a basic necessity if the liberalization is to be promoted and if our people are to enjoy its economic benefits". Ibid., p. 4.

<sup>1038</sup>The US points out that GATT/WTO jurisprudence, above all the Appellate Body's decision in *Japan - Taxes on Alcoholic Beverages*, makes clear that the protective nature and application of a measure may be discerned not only from the very language of the measure itself, but also revealed from its design, architecture and structure, and from an understanding of the practical realities of the relevant market.

materials distribution system, Japan applied distribution countermeasures so as to afford protection to domestic manufacturers, contrary to the principle stated in Article III:1 of GATT.

7.3 **Japan** argues that the United States fails to identify "laws, regulations, or requirements" that would serve as the appropriate subject matter for an Article III claim. Furthermore, Japan stresses that since none of the alleged specific distribution policies cited by the United States is still in effect, they are not properly before the Panel. Japan rejects the contention that MITI's distribution modernization policies during the 1960s and 1970s were imbued with a protectionist purpose<sup>1039</sup>, afforded protection to domestic production and thereby accord "less favourable treatment" to imports in violation of Article III. According to Japan, MITI set out to encourage distribution modernization through rationalization of transaction terms and systemization of distribution practices well before capital liberalization became an issue. These goals were pursued to raise the productivity of the relatively backward distribution sector, and thereby alleviate the growing labour shortage and upward pressure on consumer prices. Once capital liberalization got underway, distribution modernization came to serve another policy objective, namely promoting the international competitiveness of the distribution sector. There is no evidence that the Japanese Government sought to block foreign goods from traditional distribution channels. Rather, Japan sought to enhance the efficiency and competitiveness of the domestic distribution sector with a view to enabling it to compete more effectively with new foreign entrants.

7.4 Japan notes the United States does not cite a single government document or advisory council report which articulates any kind of policy of encouraging vertical integration of domestic manufacturers into distribution in film, paper, or any other industry for that matter. According to Japan, the evidence shows that as mass production developed ahead of mass distribution in Japan, some leading manufacturers did seek to modernize their distribution channels through instituting single-brand distribution or engaging in outright vertical integration. The response of the Japanese Government was not to encourage this trend, but to monitor it on a case-by-case basis, allowing the competitive benefits of vertical integration while seeking to control the anti-competitive consequences. With respect to the United States claims that the alleged "distribution countermeasures" and their purported ongoing effects on the market structure for film and paper accord less favourable treatment to imports in contravention of Article III:4, and that they are applied so as to afford protection to domestic production in violation of Article III:1, Japan contends that the United States overlooks the established principle that Article III:1 does not create any independent obligations, and that the United States fails to establish any violation of Article III:4.

7.5 As a preliminary matter, Japan notes that several of the alleged measures that Japan believed to be part of the United States claims are not included in the list of alleged "distribution countermeasures"<sup>1040</sup> that the United States provided in response to a Panel question. Accordingly, Japan requests the Panel not to consider these claims as being within the scope of the claims raised by the United States under Article III.<sup>1041</sup>

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<sup>1039</sup>Japan notes that a recent GATT panel has specifically rejected the "aims and effects" test with respect to Article III, noting the difficulty of determining the intent of a government in enacting a law based on the legislative history. See *Japan - Taxes on Alcoholic Beverages*, WT/DS8, 10, 11/R, para. 6.16. Thus, Japan contends, the United States allegations regarding the subjective intent of the Government of Japan are irrelevant to this analysis.

<sup>1040</sup>Japan mentions specifically that the United States does not list the Ninth Interim Report (1971) or the Tenth Interim Report (1972). In paragraph 10 of its third party submission, the EC points to the creation of the Natural Colour Photography Promotion Council in 1963, the 1990 Guidelines, and the Business Innovation Law (1995) in support of its theory that Japan has violated Article III. However, these actions, were also not cited by the United States and, in Japan's view, are therefore not a part of the US Article III claims. Japan notes that the United States mentioned the Business Innovation Law in passing but the law was not included in its list of distribution measures provided by the US in response to a Panel question.

<sup>1041</sup>Japan also emphasizes that only the "distribution countermeasures" are subject to both Article III and Article XXIII challenges; the "Large Stores Law" and "promotion countermeasures" are subject only to Article XXIII and limited Article X challenges.

2. **ARTICLE III:1**

7.6 Article III:1 of GATT provides:

"The [Members] recognize that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, and internal quantitative regulations requiring the mixture, processing or use of products in specified amounts or proportions, should not be applied to imported or domestic products so as to afford protection to domestic production".

7.7 The **United States** underscores that the Appellate Body has explained that the "broad and fundamental purpose of Article III" is to avoid protectionism in the application of internal tax and regulatory measures. More specifically, the purpose of Article III "is to ensure that internal measures not be applied to imported or domestic products so as to afford protection to domestic production."<sup>1042</sup> Thus the United States argues that the Appellate Body has indicated that sentences 1 and 4 of Article III are inextricably linked, finding that Article III:1 "informs the rest of Article III" and establishes "part of the context" for interpreting the other paragraphs in Article III.<sup>1043</sup>

7.8 **Japan** points out that Article III:1 of GATT is only a statement of general principles and does not impose any obligation on Members in addition to those specified elsewhere in Article III.<sup>1044</sup> In Japan's view, this conclusion follows from the ordinary meaning of the language of the provision and from GATT precedent. Article III:1 provides that laws and regulations "should" not be applied so as to afford protection to domestic production. By using "should" instead of "shall,"<sup>1045</sup> Article III:1 is meant to serve as a statement of general principles for the rest of Article III, and is to be used as a guide to interpreting the specific obligations contained in the other paragraphs of Article III, including paragraph 4 thereof. In Japan's view, GATT precedents support this interpretation. The panel on *Japan - Taxes on Alcoholic Beverages*<sup>1046</sup> specifically held that "Article III:1 does not contain a legally binding obligation but rather states general principles". The Appellate Body upheld this interpretation.<sup>1047</sup> As Article III:1 does not contain any specific obligations, it is impossible for any Japanese measure to violate Article III:1.

7.9 The **United States** responds that it is not requesting this Panel to find an independent violation of Article III:1. Rather, the United States views the general principle embodied in Article III:1 as being an integral aspect of Article III as a whole and Article III:4 in particular. The United States, along with the EC, believes that Article III:4 can be understood fully only if read in connection with Article III:1. The United States argues that its position in this regard is consistent with the leading decision on the issue, the Appellate Body's recent decision in *Japan - Taxes on Alcoholic Beverages*. In that matter, the Appellate Body noted that the general principle embodied in Article III:1 "informs" and constitutes part of the context of the rest of Article III.<sup>1048</sup>

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<sup>1042</sup> Appellate Body Report on *Japan - Taxes on Alcoholic Beverages*, adopted on 1 November 1996 WT/DS8/10,11/AB/R, p. 16 (quoting *United States - Section 337 of the Tariff Act of 1930*, adopted on 7 November 1989, BISD 36S/345, pp. 385-386, para. 5.10).

<sup>1043</sup> *Japan - Taxes on Alcoholic Beverages*, op. cit., p. 18.

<sup>1044</sup> Japan notes that only recently the United States agreed with Japan's interpretation. In *United States - Gasoline* the United States argued that Article III:1 was "only hortatory and could not form the basis of a violation". *United States - Gasoline*, WT/DS2/R, op. cit., para. 6.17.

<sup>1045</sup> Japan notes that the other provisions of Article III, each of which contain specific obligations, use the word "shall".

<sup>1046</sup> *Japan - Alcoholic Beverages*, WT/DS8, 10, 11/R, p. 107, para. 6.12.

<sup>1047</sup> Appellate Body Report on *Japan - Alcoholic Beverages*, WT/DS8,10,11/AB/R, AB-1996-2, p. 18.

<sup>1048</sup> *Ibid*, p. 18. Although *Alcoholic Beverages* involved Article III:2 rather than Article III:4, the United States believes that much of its reasoning is pertinent to the present dispute.

7.10 The United States notes that, based on this analysis, the Appellate Body found that the "broad and fundamental purpose of Article III is to avoid protectionism in the application of internal tax and regulatory measures. ... Article III obliges Members of the WTO to provide equality of competitive conditions for imported products in relation to domestic products".<sup>1049</sup> Quoting an earlier panel report, the Appellate Body stated: "[T]he intention of the drafters of the Agreement was clearly to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise, indirect protection could be given".<sup>1050</sup> The Appellate Body further ruled that panels should examine the various factors surrounding the promulgation of a measure to determine whether it serves protectionist purposes.<sup>1051</sup> The Appellate Body emphasized the fact-specific nature of the inquiry, stating that a measure's "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 a given case".<sup>1052</sup> The Appellate Body cautioned against adopting a formulaic approach: "WTO rules are not so rigid or inflexible as not to leave room for reasoned judgments in confronting the endless and ever-changing ebb and flow of real facts and real cases in the real world".<sup>1053</sup>

7.11 The United States believes that Japan apparently agrees with the EC<sup>1054</sup> and the United States that Article III:1 does not form the basis of an independent cause of action but that it provides essential interpretive guidance for all the provisions of Article III which must be read with this principle in mind. Where the parties appear to part company, the United States suggests, is in their understanding of how Article III:1 affects Article III:4. Whereas the United States believes that Article III:4 must be applied in a sufficiently broad manner to effectuate the general principle of paragraph 1<sup>1055</sup>, in the US view, Japan essentially would limit Article III:4 to cases of *de jure* discrimination achieved through the most formal government action. In the US view, Japan's position does not advance the principles of paragraph 1, nor does it comport with well-established GATT jurisprudence, especially the Appellate Body's decision in *Japan - Alcoholic Beverages*.

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<sup>1049</sup>Ibid., p. 16, citing *United States - Taxes on Petroleum and Certain Imported Substances*, adopted on 17 June 1987, BISD 34S/136, 158-159, para. 5.1.9; *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, adopted on 10 November 1987, BISD 34S/83, 113-114, para. 5.5(b).

<sup>1050</sup>Ibid., quoting *Italian Discrimination Against Imported Agricultural Machinery (Italian Agricultural Machinery)*, BISD 7S/60, 63-64, para. 11.

<sup>1051</sup>Ibid., pp. 28-29. In doing so, the Appellate Body was not adding a legal element to other paragraphs of Article III. Rather, the Appellate Body was instructing panels to give Article III sufficient breadth to reach measures imposed by WTO Members that protect domestic production. See, e.g., *United States - Section 337*, op. cit., paras. 6.2-6.3 (panel found that less favourable treatment was accorded even though there was no deliberate attempt to discriminate against imports).

<sup>1052</sup>Ibid.

<sup>1053</sup>Ibid., p. 31.

<sup>1054</sup>According to the United States, in its third-party submission, the EC indicated their support for the position of the United States and reaffirmed the WTO precedent described above. Specifically, the EC maintained that "Japanese internal policies concerning [consumer photographic film and paper] products were in fact designed to afford protection to domestic products on top and independently from their facial objective of pursuing general internal policies under their jurisdiction".

<sup>1055</sup>The Appellate Body in *Japan - Alcoholic Beverages* made clear that it viewed paragraph 1 as supplying a "broad and fundamental purpose ... Otherwise indirect protection could be given" (op. cit., p. 16, quoting *Italian Agricultural Machinery*, op. cit., para. 11). This position reaches back to doctrine established in the early days of the GATT, when the panel in the *Italian Agricultural Machinery* dispute read Article III expansively, determining that it covers "any laws or regulations which *might* adversely modify the conditions of competition between the domestic and imported products on the internal market" (op. cit., p. 64, para. 12, emphasis added).

3. **ARTICLE III:4**

7.12 Article III:4 of GATT provides in the relevant part:

"The products of the territory of any [Member] imported into the territory of another [Member] shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use".

7.13 The **United States** submits that the national treatment principle, as it applies to the facts of this dispute, derives from two commitments made by GATT contracting parties and subsequently by WTO Members:

- (1) to refrain from impairing the conditions of sale or distribution of imports for the purpose of protecting domestic production; and
- (2) to treat imported products no less favourably than like domestic products.

7.14 **Japan** underscores that to prove that any of the policies cited above are in violation of Article III:4, the United States must establish the existence of each of the following two elements:

- (1) There is a "law", "regulation" or "requirement" affecting the sale or distribution of the products in question; and
- (2) that law, regulation or requirement accords "less favourable" treatment to imported products than that accorded to like domestic products.

(a) **"Laws, regulations or requirements" within the scope of Article III:4**

(i) **The legal test**

7.15 The **United States** explains that the Japanese Government restructured the photographic materials distribution system through its system of "concerted adjustment",<sup>1056</sup> working closely with the private sector to formulate a plan of inherently coercive nature for counteracting international competition.<sup>1057</sup> Specifically, the government planned, promoted, facilitated and contributed essential direction, guidance, technical expertise, and financing to coordinate establishment of narrow vertical lines of distribution, with primary wholesalers' handling the products of a single domestic manufacturer. In implementing the restructuring plan, the government employed formal as well as informal methods, often providing direction through administrative guidance. According to the United States, Japan has long used informal methods of government-private sector cooperation and administrative guidance to direct industry adjustment.<sup>1058</sup> Viewed as a whole, with its formal and informal components, and with its underlying structure of cooperation between government and industry, the Japanese regime is the embodiment

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<sup>1056</sup>MITI, Formation of a New Industrial Order, 9 May 1962, MITI History, Volume 17, pp. 403-407, US Ex. 62-5.

<sup>1057</sup>The United States also refers to the EC's statement in its third party submission: "[T]he *Semiconductors* Panel Report was considering not only the formality but the reality of a very peculiar system, the Japanese interconnection between government and industry. This particular situation is characterised by a significant capability of the Government to directly influence the behaviour of private companies through the traditional peer structure of the society and the strong pressure that it can produce without the need of adopting legally binding instruments". Based on this analysis, the EC characterized Japan's measures as "requirements" pursuant to Article III:4 but, given the extraordinary array of measures at issue in this dispute, in the US view, the Panel need not restrict its inquiry to that one term.

<sup>1058</sup>Yamanouchi Kazuo, *Kokka Komuin No Tame no Gyosei Shidoron* [Administrative Guidance Theory for Government Officials], 1986, pp. 1-2, US Ex. 86-1.

and effectuation of Japanese Government policy and falls within the scope of "all laws, regulations and requirements" in the meaning of Article III:4.

7.16 **Japan** contends that there was nothing in MITI's distribution modernization policies of the 1960s and 1970s that amounted to a "law", "regulation" or "requirement" in the meaning of Article III because they were not enacted by the Diet as a "law", nor were they promulgated as "regulations" under the relevant administrative procedures, nor do they qualify as "requirements" given that the ordinary meaning of a government "requirement" refers clearly to some form of government mandate.

7.17 The **United States** deems Japan's definition of the types of measures covered by Article III:4 as too restrictive if the term "laws" is understood to refer only to the command of a legislature inscribed in a statutory code, and the term "regulations" is limited to a series of codified rules promulgated by an administrative agency. The United States explains that the phrase "all laws, regulations and requirements" speaks to government actions, i.e., action taken in the name of a WTO member, by government officials or parties authorized to act on the government's behalf, in pursuit of government policies. The very language of Article III:4 indicates, that it was intended to cover "all" government action which would include the formulation of government policy and its implementation.

7.18 In referring to Article 31 of the Vienna Convention, the United States argues that the object and purpose of Article III is to "avoid protection in the application of internal tax and regulatory measures". If the phrase "laws, regulations and requirements" would be interpreted to encompass only highly formalized, mandatory rules, Article III would fail to prohibit a significant amount of government action affording protection to domestic production and according less favourable treatment to imports. Accordingly, for the United States it is unnecessary to qualify the types or forms of government actions that are susceptible to being deemed "laws, regulations and requirements". A Member should bear responsibility, if its governmental action accords less favourable treatment to imported products than to domestic products, regardless of the method used by the Member to achieve this result. The question thus becomes whether any such less favourable treatment may be attributed to the actions of a WTO Member, as opposed to non-governmental entities. In the US view, no single or set of criteria should be dispositive, an approach that comports with the Appellate Body's preference for case-specific, fact-intensive inquiries as reflected in its admonition in *Japan - Alcoholic Beverages* to refrain from applying WTO rules in a way that ignores "real facts and real cases in the real world".<sup>1059</sup>

7.19 **Japan** submits that, for a party to be subject to a government requirement, it must either (1) be legally obligated to carry out the request, or (2) receive some advantage from the government in exchange for compliance. Thus there must be either a government sanction or the withholding of a government benefit that is attached, formally or substantively, to non-compliance. In this regard, Japan notes that the panel report on *EEC - Regulation on Imports of Parts and Components* ("*EEC - Parts and Components*") found that undertakings in anti-circumvention proceedings under the EC antidumping law could be considered "requirements" within the meaning of Article III even though the undertakings were voluntarily accepted because the government made the granting of an advantage, i.e., the suspension of the anti-circumvention proceedings dependent on the acceptance of the undertakings.<sup>1060</sup>

7.20 The **United States** notes that the panel on *EEC - Parts and Components* found that the EC's acceptance of "undertakings" by private parties fell within the scope of Article III:4,<sup>1061</sup> even though the government action in question was an informal one, derived from no formal legislation or regulatory code specifically authorizing or requiring the acceptance of such "undertakings".<sup>1062</sup> That panel noted

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<sup>1059</sup>*Japan - Taxes on Alcoholic Beverages*, op. cit., p. 31.

<sup>1060</sup>Panel Report on *European Economic Community - Regulation of Imports of Parts and Components*, adopted on 16 May 1990, BISD 37S/132, 197, para. 5.21.

<sup>1061</sup>*Ibid.*

<sup>1062</sup>*Ibid.*, pp. 134-135, paras. 2.3-2.7; p. 197, para. 5.20.

that there was "no obligation under the EEC's anti-dumping regulation to offer parts undertakings, to accept suggestions by the EEC Commission to offer such undertakings and to maintain the parts undertakings given".<sup>1063</sup>

7.21 According to **Japan** MITI's 1970 Guidelines are clearly distinguishable from the undertakings in *EEC - Parts and Components* because compliance with these non-binding recommendations was a matter of purely voluntary decision and no government sanction or withholding of a government-provided benefit was attached, either formally or substantively, to non-compliance.

7.22 The **United States** points out that nowhere in GATT jurisprudence has a panel ever articulated a definition of the phrase "laws, regulations and requirements" to be applied in all Article III:4 cases. This would be inappropriate since each WTO Member has a unique form of government and legal system and no one definition could adequately encapsulate "all laws, regulations and requirements" as those terms relate to the WTO's more than 120 Members. In this respect, the United States points out that prior panels have looked at a variety of factors in examining whether government action may be deemed a law, regulation or requirement under Article III:4. These factors include, i.e., whether a Member threatened punishment or offered an inducement, but also other considerations. Moreover, the panel report on *Canada - Administration of the Foreign Investment Review Act ("Canada - FIRA")*, found "undertakings," or contractual commitments, made by private investors with the Canadian Government to be "requirements"<sup>1064</sup> and expressly rejected Canada's argument that a "requirement" could not be found where the contractual relationship involved was essentially a private one.<sup>1065</sup> The panel on *Canada - FIRA* explained that it did not feel constrained to limit the types of measures that could be deemed "laws, regulations and requirements" to those previously recognized as such by other panels: "Any interpretation which would exclude case-by-case action would, in the view of the Panel, defeat the purposes of Article III:4".<sup>1066</sup> Therefore, the United States emphasizes, the panels in these cases in no way suggested that they had formulated or were following any set of generally applicable criteria.

(ii) **Japan's "administrative guidance" in the light of GATT precedents**

7.23 The United States submits that the need for case-by-case review of whether government action has occurred is particularly strong in this dispute because Japan carries out its policies through a complex, opaque system in which traditional legal measures are interwoven with administrative guidance and other informal measures. Given its unusual character, the Japanese regime is not easily compared to those found in other nations. The United States quotes one of Japan's leading trade scholars who defined that "administrative guidance is a *de facto*, rather than a *de jure*, directive issued by government officials ... In a broad sense, administrative guidance is a form of government regulation which imposes some kinds of rules of conduct on private individuals or enterprises".<sup>1067</sup> Noting the peculiarity of the Japanese system, the trade scholar also stated that "the degree of pervasiveness and the importance of administrative guidance in the Japanese governmental process is probably unique to Japan".<sup>1068</sup>

7.24 The United States points out that the *Japan - Semiconductors* panel found Japan's regime of formal and informal measures to be "prohibitions or restrictions" for purposes of Article XI of GATT

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<sup>1063</sup>Ibid., p. 54, para. 5.20.

<sup>1064</sup>*Canada - FIRA*, adopted on 7 February 1984, BISD 30S/140, 159, para.5.6.

<sup>1065</sup>Ibid.

<sup>1066</sup>Ibid., p. 159, para. 5.5.

<sup>1067</sup>Matsushita Mitsuo, *International Trade and Competition Law in Japan*, 1993, p. 60, US Ex. 93-1.

<sup>1068</sup>Ibid.

even though no formally binding or mandatory measures had been imposed.<sup>1069</sup> The panel relied upon the following analysis in reaching this conclusion:

"Government-industry relations varied from country to country, from industry to industry, and from case to case and were influenced by many factors. There was thus a wide spectrum of government involvement ranging from, for instance, direct government orders to occasional government consultations with advisory committees. The task of the Panel was to determine whether the measures taken in this case would be such as to constitute a [violation]".<sup>1070</sup>

"The Panel considered that the complex of measures exhibited the rationale as well as the essential elements of a formal system of export control. The only distinction in this case was the absence of formal legally binding obligations in respect of exportation or sale for export of semi-conductors. However, the Panel concluded that this amounted to a difference in form rather than substance because the measures were operated in a manner equivalent to mandatory requirements ... ".<sup>1071</sup>

7.25 The United States explains that the conclusion of the *Semiconductors* panel comports with those of the panel on *Japan - Certain Agricultural Products* which found that "the practice of 'administrative guidance' played an important role" in the enforcement of the Japanese supply restrictions, that this practice was "a traditional tool of Japanese government policy based on consensus and peer pressure" and that administrative guidance in the special circumstances prevailing in Japan could therefore be regarded as a governmental measure.<sup>1072</sup> In that case, Japan had taken the position that while "it was irrelevant whether or not [its] measures were mandatory and statutory," it was significant whether the measures "were effectively enforced by detailed directives and instructions to local governments and/or ... organizations". Japan had explained that "such centralised and mutually collaborative structure of policy implementation was the crux of government enforcement in Japan".<sup>1073</sup>

7.26 **Japan** responds that the *Japan - Semiconductors* panel noted explicitly that "Article XI:1, unlike other provisions of the General Agreement, did not refer to laws or regulations but more broadly to measures"<sup>1074</sup> and thereby established strict criteria for when Japanese administrative guidance constitutes a "measure".<sup>1075</sup> Items which do not qualify even as "measures" in the context of Article XI:1 are not "requirements" within the meaning of Article III because "requirements" must satisfy a stricter test than "measures". In Japan's view, the EC supports this interpretation in its third party submission.

7.27 The **United States** explains that in the present case Japan resorted to a variety of measures such as administrative guidance, coupled with more formal measures, in accomplishing the "systemization" and "rationalization" of distribution in the photographic materials sector. Japan attempts to minimize the importance of any administrative guidance in this context claiming it was just "promotional" or merely advisory. The United States requests the Panel not to accept such labels or technical distinctions but to scrutinize the Japanese Government's actions in the totality of the circumstances in which they occurred. The government planned, promoted and facilitated the consolidation of the primary distribution channels in the photographic materials market. The

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<sup>1069</sup>Panel on *Japan - Trade in Semiconductors* ("*Japan - Semiconductors*"), adopted on 4 May 1988, BISD 35S/116, 157-158, para. 117.

<sup>1070</sup>*Japan - Semiconductors*, pp. 154-155, para. 108.

<sup>1071</sup>*Ibid.*, p. 155, para. 109.

<sup>1072</sup>*Japan - Restrictions on Imports of Certain Agricultural Products* ("*Japan - Certain Agricultural Products*"), adopted 22 March 1988, BISD 35S/163.

<sup>1073</sup>*Japan - Semiconductors*, p. 154, para. 107, citing Panel on *Japan - Certain Agricultural Products*.

<sup>1074</sup>*Ibid.*, pp. 153-154, para. 106.

<sup>1075</sup>*Ibid.*, p. 155, para. 109.



government's actions viewed collectively or individually constitute "laws, regulations and requirements" as those terms are used in Article III:4. The United States emphasizes that Japan should bear responsibility for the actions of its government.

**(iii) Are specific distribution measures "laws, regulations and requirements"?**

7.28 **Japan** takes the position that an examination of the list of "distribution countermeasures" challenged by the United States reveals that most of the cited items do not constitute a "law" or a "regulation", nor do they qualify as "requirements" within the meaning of Article III. In Japan's view, the United States has only broadly claimed that the alleged distribution countermeasures are within the scope of that provision without being precise in identifying any "law", "regulation" or "requirement" in a manner that gives, in its interpretation, proper weight to the terms of Article III.<sup>1076</sup>

7.29 The **United States** considers some of the Japanese Government's actions have been formal, others not. The formal measures bear the typical characteristics of "laws, regulations and requirements":

- (1) The 1967 Cabinet Decision;
- (2) the international contract notification provision of Japan's Antimonopoly Law;
- (3) JFTC Notification 17 of 1967; and
- (4) loans to the domestic photographic industry by the Japan Development Bank (JDB) and the Small and Medium Enterprise Agency (SMEA).

are, in the US view, conventional legal measures. They were promulgated with all of the procedures traditionally associated with conventional legal measures. Although the United States does not subscribe to the criteria proposed by Japan, these measures would satisfy those criteria because each is (i) mandatory, (ii) imposes obligations or (iii) involves the grant of a government benefit.

7.30 The United States emphasizes that the distribution countermeasures emanated from a formal policy of the Japanese Government, as established by a decision of the Japanese Cabinet, and they are embodied in a series of concrete actions taken by MITI and its committees to carry out the government's policy as reflected in their reports and guidelines. The restructuring of Japan's photospecialty distribution system emanated directly from the 1967 Cabinet Decision to establish a framework of "countermeasures to be taken by the Government" to offset the effects of trade liberalization and to prevent foreign manufacturers from penetrating the Japanese market through its distribution system. To implement this policy in the photographic sector, the United States contends, MITI created a host of joint government-industry committees dedicated to establishing standardized transaction terms designed to cement exclusive relationships between domestic producers and wholesalers and retailers. To ensure compliance from the private sector, the government monitored the implementation of such standardized transaction terms, revised those terms and other methodologies over time, and contributed technical expertise and financing. The government, through the JDB and SMEA, gave financial support for domestic manufacturers, wholesalers and photo finishing laboratories to achieve "systemization".

7.31 **Japan** responds that there was nothing in MITI's distribution modernization policies that amounted to a "law", "regulation" or "requirement" in the meaning of Article III because they were not enacted by the Diet as a "law", nor were they promulgated as "regulations" under the relevant administrative procedures, nor do not qualify as "requirements" given that the ordinary meaning of a government "requirement" refers clearly to some form of government mandate. In Japan's view, since the 1970 Guidelines do not meet criteria set out in the panel report on *Japan - Semiconductors*,

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<sup>1076</sup>Japan only concedes that (1) the international contract notification requirement, and (2) SMEA financing and the JDB loan to Konica, are "measures" for purposes of Article XXIII:1(b), but not for purposes of Article III:4. Japan further recalls that it has raised procedural objections against these items.

and since the criteria for when administrative guidance constitutes a "law" "regulation" or "requirement" for purposes of Article III are, if anything, stricter than those for "measures" in the context of Article XI:1, it follows that the policies in question fall outside the scope of Article III. Moreover, in Japan's view, several items raised by the United States such as advisory council and public reports, are not even official statements of government policy. Japan argues that for the same reasons that such reports cannot constitute "measures" for purposes of non-violation complaints, they cannot be considered "laws, regulations, or requirements" within the meaning of Article III.

7.32 The **United States** responds that the informal measures used by Japan to institute the restructuring of distribution were equally important as formal measures in fulfilling the government's objectives given that MITI and its committees steered the industry through years of complicated problems on how to reform distribution operations. Under MITI supervision, the committees observed practices in the industry, enforced compliance with government-industry recommendations and refined strategy over time. Prior panel decisions such as the panel reports on *Japan - Semiconductors* and *Japan - Certain Agricultural Products*, have discussed the Japanese system of administrative guidance in ways that prove illuminating in this case. The same reasoning should be applied to Japan's use of "concerted adjustment" in the photographic materials sector in which the government formulates and monitors the alteration of fundamental aspects of an industry and which involved official action on the part of the Japanese Government and the execution of definitive government policies. For the United States, through MITI and other government agencies, "the government acts as the formulator of a master plan within which private enterprises make specific business decisions".<sup>1077</sup> The United States maintains that this informal guidance had the force and effect of laws, regulations, or requirements.

**(iv) Measures 'no longer in effect'**

7.33 In the alternative, **Japan** argues that on the assumption that the alleged "distribution countermeasures" would ever have constituted "laws, regulations, or requirements" within the scope of Article III, they are no longer in effect and therefore cannot be found to violate Article III. Each and every one of MITI's alleged distribution policies of the 1960s and '70s occurred decades ago and has been superseded by more recent policies and industry actions. In particular, MITI's 1990 Guidelines target many of the same "irrational" distribution practices (e.g., rebates, returns, dispatching of sales employees to customers), as were addressed in the 1970 Guidelines. However, Japan contends that now the MITI's recommendations are explicitly identified by the United States as improving market access. According to Japan, the United States recently urged the Japanese industry to follow the recommendations of the 1990 Guidelines.

7.34 Japan takes the view that since virtually all of the items and policies included in the United States claims under Article III are no longer in effect<sup>1078</sup>, it appears that the United States claims boil down to the argument that the continuing effects of the "distribution countermeasures", i.e., the current market structure for the distribution of film and paper, are "laws", "regulations" or "requirements" capable of violating Article III. Japan requests the Panel to reject this argument based on its reasoning

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<sup>1077</sup>The United States points out that to the extent MITI or another relevant regulatory agency is dissatisfied with private sector intentions or performance, the government may recommend modification of an industry's plan. MITI has many tools at its disposal to strengthen a domestic industry. It may aid in the creation of a cartel, regulate price or production, promote mergers and acquisitions among competitors and create joint buying or selling agencies. Coercive measures are rarely necessary because, at the heart of MITI's reorganization efforts, is a diminution in competition that is likely to benefit participating enterprises. Whereas government scrutiny likely would be an impediment if private actors were to attempt to effectuate such a plan on their own, MITI's role all but ensures that no enforcement action will be taken by the JFTC or other government agencies.

<sup>1078</sup>Japan notes that Notification 17 was repealed in April 1996. Furthermore, Japan submits that a bill to repeal the International Contract Notification requirement has been introduced to the Diet, in light of the globalization of the Japanese economy and for the reduction of the administrative burden. The bill to repeal the international contract notification requirement was passed in June 1997. Simultaneously, JFTC Rule No. 1 under Article 6 of the Antimonopoly Law was abolished.

presented in relation to the US non-violation claims against the above-mentioned "measures" which, in Japan's view, applies with equal if not greater force in respect of a violation claim under Article III. Moreover, Japan notes that the United States concedes that "MITI's systemization program was largely complete" by 1975<sup>1079</sup>, and explicitly acknowledges that market structure is not even a "measure" within the meaning of Article XXIII:1(b).

7.35 The **United States** emphasizes that it alleged at no point during this proceeding that the market structure was a "law, regulation or requirement". To the extent that the United States referred to private sector activities, it did so only to demonstrate how the private sector acted in the manner planned and orchestrated by the Japanese Government. The United States, however, regards Japan's bottle-necked distribution system to be compelling evidence of the Japanese Government's systematic efforts to erect a bulwark against foreign competitors. In the US view, that market structure is the direct result of numerous actions by the Japanese Government to strengthen ties between domestic manufacturers and the primary photospecialty wholesalers.

7.36 **Japan** recalls that Article XXIII:1(a) authorizes dispute settlement in violation cases only when a benefit "is being nullified or impaired" by "the failure of another contracting party to carry out its obligations under this Agreement". The use of the present tense indicates that, in the context of Article III, some present and ongoing law, regulation, or requirement must be at issue. Specifically, Article 3.7 of the DSU contemplates three possible outcomes in the absence of a negotiated settlement: (1) withdrawal of the offending measure, which is explicitly the preferred alternative<sup>1080</sup>; (2) provision of compensation as a temporary measure pending withdrawal of the offending measure; and (3) suspension of concessions or other obligations by the aggrieved Member if the offending measure is not withdrawn. Article 19.1 of the DSU further confirms that withdrawal of the offending measure is the primary remedy: "Where a panel or the Appellate Body 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". In Japan's view, this language supports the conclusion that only measures that are currently in effect are properly before the Panel, since only measures that are currently in effect can be brought into conformity with the relevant agreement. Japan emphasizes that the latter two options presuppose the unavoidable continuation of the offending measure and that, accordingly, - if the measure in question is no longer in effect -, the complaining party has its remedy and the most that dispute settlement could accomplish has already happened. Japan further points out that even if the Panel were to find past violations, there would be no viable remedy available under the DSU. Japan maintains that it is beyond the scope of WTO dispute settlement to punish parties for alleged transgressions of the past, or to order "affirmative action" in an attempt to undo the past.

7.37 In responding to Japan's argument on measures no longer in effect, the **United States** relies upon its position, described above in Part VI.C.1. on "Governmental Measures", in particular on section (d), entitled "Measures applied and measures in effect".<sup>1081</sup>

7.38 **Japan** notes that Notification 17 was repealed in April 1996. Therefore, Japan argues that it should not be the subject of the present proceeding. Nor will the general designation of unfair trade practices under the Antimonopoly Law operate to continue the content of the regulation. The JFTC will not act automatically against the premium offers in excess of 100,000 yen; it will take measures only when specific harm to fair competition is proven. "Normal business practice" refers not to 100,000 yen, but to the practice acceptable from the point of fair competition. Furthermore, Japan submits that a bill to repeal the International Contract Notification requirement has been introduced in March

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<sup>1079</sup>Japan notes that the United States uses the term "systemization" to cover both rationalization policies (the 1970 Guidelines) and systemization policies (reflected by the 1975 Manual).

<sup>1080</sup>Article 3.7 of the DSU specifies that the primary remedy in violation cases is withdrawal of the offending measure.

<sup>1081</sup>See paras. 6.119-6.126 above.

1997 to the Diet. The bill was enacted in June 1997, and thus this requirement has been abolished. Simultaneously, JFTC Rule No. 1 under Article 6 of the Antimonopoly Law was abolished.

**(b) "Less favourable treatment" in the meaning of Article III:4**

**(i) The legal test**

7.39 The **United States** argues that the requirement in Article III:4 that imports are to receive "treatment no less favourable than that accorded to like products of national origin" has been construed to mean that, at a minimum, government actions affecting the distribution or sale of goods must apply to imports in the same way that they apply to like domestic products. "[T]he intention of the drafters ... was clearly to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise indirect protection could be given".<sup>1082</sup> Though different treatment may in some instances afford equal or better conditions for imports, and thus may be permissible under Article III:4<sup>1083</sup>, any narrowing of trade opportunities or the imposition of additional burdens for imports runs afoul of the national treatment principle.<sup>1084</sup> A WTO Member may not improperly "tip the balance" of competitive conditions in favour of domestic products.<sup>1085</sup> Article III:4 serves to protect "expectations on the competitive relationship between imported and domestic products."<sup>1086</sup> The extent to which restrictions have impaired actual trade flows are unimportant.<sup>1087</sup>

7.40 **Japan** notes that the proper limits of the requirement to accord "no less favourable" treatment are framed by the *language* of Article III:4 which concerns governmental measures. Therefore, the "treatment no less favourable" must flow from the "laws", "regulations" or "requirements" in dispute, not from acts of private parties or other general circumstances. The plain meaning of the provision thus demands that the focus of Article III analysis be on the provisions of government measures, not on the happenstance of market conditions.<sup>1088</sup>

7.41 Japan further responds that the element of "no less favourable" treatment should be interpreted in view of the general *purpose* of Article III to protect the equal competitive relationship between imported and domestic products by preventing discriminatory treatment by governments, and not to guarantee any particular results in the marketplace. The Appellate Body report on *Japan - Taxes on Alcoholic Beverages* recently reconfirmed that "Article III protects expectations not of any particular trade volume, but rather of the equal competitive relationship between imported and domestic products".<sup>1089</sup>

7.42 Japan submits that the phrase "no less favourable" must be read in the *context* of the general principle contained in Article III:1 that government measures should not be applied "so as to afford protection to domestic production". The Appellate Body report in *Japan - Taxes on Alcoholic Beverages*

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<sup>1082</sup>Panel Report on *Italian Discrimination against Imported Agricultural Machinery*, adopted on 23 October 1958, BISD 7S/60, 63-64, para. 11.

<sup>1083</sup>See Panel Report on *United States - Section 337 of the Tariff Act of 1930 ("United States - Section 337")*, adopted on 7 November 1989, BISD 36S/345, p. 386, para. 5.11.

<sup>1084</sup>See Panel Report on *United States - Imports of Certain Automotive Spring Assemblies*, adopted on 26 May 1983, BISD 30S/107.

<sup>1085</sup>Panel Report on *Canada - FIRA*, adopted on 7 February 1984, BISD 30S/140, 166, para. 6.3.

<sup>1086</sup>*United States - Section 337*, BISD 36S/345, 387, para. 5.13, citing Panel Report on *United States - Taxes on Petroleum and Certain Imported Substances*, adopted on 17 June 1987, 34S/136, 158-159, para. 5.1.9.

<sup>1087</sup>*United States - Section 337*, op. cit. p. 387, para. 5.13.

<sup>1088</sup>As Japan discussed in relation to the US non-violation claims, whether a particular government policy accords "no less favourable treatment" to imports than to a domestic like product is to be judged based on the law, regulation, or requirement itself, and not on the alleged consequences, i.e., the allegedly "closed" distribution network in the Japanese film market today.

<sup>1089</sup>*Japan - Taxes on Alcoholic Beverages*, WT/DS8, 10, 11/AB/R, AB-1996-2, p. 16.

recently affirmed that "[t]his general principle informs the rest of Article III".<sup>1090</sup> The focus of Article III:1 on protectionism confirms that Article III:4 is concerned with discriminatory treatment, not incidental burdens unrelated to the actual provisions of the measures in dispute.

7.43 The **United States** emphasizes that Article III:4 makes clear that Members may not accord less favourable treatment in respect of "all laws, regulations and requirements ... affecting ... distribution" and, therefore, does not permit WTO Members to deny foreign manufacturers access to distribution channels that are available to domestic manufacturers. Prior panels have found that government measures limiting distribution opportunities for imports violated Article III:4. In particular, this was made clear in two panel reports that previously addressed limitations applied on the distribution and sale of imported alcoholic beverages: *Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies* ("*Canada - Alcoholic Drinks*")<sup>1091</sup> and *United States - Measures Affecting Alcoholic and Malt Beverages* ("*United States - Alcoholic Beverages*").<sup>1092</sup>

7.44 **Japan** distinguishes the panel reports on *Canada - Alcoholic Drinks* and *United States - Alcoholic Beverages* from the present case on the grounds that in those cases, imports were legally forbidden from using certain distribution channels that were open to domestic products.

7.45 The **United States** rejects Japan's argument because it goes to the nature of the measures underlying the disputes, i.e., whether the governmental action constitutes a law, regulation or requirement. The United States maintains that these cases stand for the proposition that government action resulting in a diminution of distribution opportunities for imported products constitutes less favourable treatment under Article III.

7.46 In the US view, in *Canada - Alcoholic Drinks* the panel examined whether provincial liquor-board restrictions on access for imported beer to certain points of sale were consistent with the national treatment principle of Article III:4. The panel concluded that imported beer had not been afforded less favourable treatment because it did not have access to the same distribution channels as domestic beer. In reaching this outcome, the panel rejected an argument proffered by Canada that was in certain respects similar to the one currently being made by Japan. Canada maintained that many of the points of sale denied to foreign beer were controlled by private businesses and that any hardship befalling imports was the result of private conduct.<sup>1093</sup> The panel, however, did not find persuasive Canada's contention that private distribution systems were free to carry foreign beer and, thus, the government should not be held responsible for private business decisions to refrain from doing so. The panel decided that "imported beer had access to fewer points of sale than domestic beer because domestic brewers were authorized to establish private retail stores or had access to retail outlets in which imported beer could not be sold".<sup>1094</sup>

7.47 In reaching this conclusion, the panel relied on the standard set forth by the panel on *United States - Section 337* which explained that "the words 'treatment no less favourable' call for 'effective equality of opportunities for imported products in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use.'"<sup>1095</sup> In particular, the panel reasoned that whether imports enjoy "equal opportunities" turns "on the distinctions

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<sup>1090</sup>Ibid., p. 18.

<sup>1091</sup>Panel on *Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies* ("*Canada - Alcoholic Drinks*"), DS21/R, adopted on 18 February 1992, BISD 39S/27.

<sup>1092</sup>Panel Report on *United States - Measures Affecting Alcoholic and Malt Beverages* ("*United States - Alcoholic Beverages*"), DS23/R, adopted on 19 June 1992, BISD 39S/206.

<sup>1093</sup>*Canada - Alcoholic Drinks*, op. cit., pp. 44-45, para. 4.9.

<sup>1094</sup>Ibid., p. 75, para. 5.5.

<sup>1095</sup>*United States - Section 337*, BISD 36S/345, 386, para. 5.11.

made by the laws, regulations, or requirements themselves and on their potential impact, rather than on the actual consequences for specific imported products".<sup>1096</sup>

7.48 The United States further refers to the panel on *United States - Alcoholic Beverages* which concerned state laws requiring imported beer and wine to be sold only through wholesalers while some in-state like products were permitted to be sold directly to retailers. The panel found that establishing different distribution channels for imported and domestic beer and wine constituted less favourable treatment of imported products within the meaning of Article III:4.<sup>1097</sup> The panel "considered as irrelevant ... that many - or even most - in-state beer and wine producers preferred to use wholesalers rather than market their products directly to retailers ...". The panel explained that, unlike imported beer, certain domestic producers located in the states in question "have the opportunity to choose their preferred method of marketing. The panel considered that it is the very denial of this opportunity in the case of imported products which constitutes less favourable treatment".<sup>1098</sup>

(ii) **"Less favourable treatment" based on product origin or product characteristics**

7.49 **Japan** explains that there have been only two kinds of cases in which laws, regulations, or requirements have ever been found to violate national treatment. The first type of case involves laws, regulations, or requirements in which different treatment was accorded to similar or "like" products explicitly based on their origin. In these cases, the question before the panel was whether imported products were treated any less favourably than domestic products due to differences in the legal provisions.<sup>1099</sup> Japan underlines that the distribution measures at issue do not make any distinctions between goods based on country of origin. According to Japan, this line of cases does not support the US claims.

7.50 The second type of case in Japan's understanding involves laws, regulations or requirements in which different treatment was accorded to products based on characteristics other than origin. In these cases, certain measures apply to one product and not another, even though the products may be considered as similar or "like" products. When such measures are deemed to accord less favourable treatment to imported products, these measures may be found to violate Article III.<sup>1100</sup> However, Japan emphasizes that the alleged Japanese distribution measures do not draw any line at all between products based on any product characteristics.

7.51 The **United States** responds that if in Japan's view GATT precedent confines "treatment less favourable" to mean either overt discrimination based on the country of origin of products or discrimination based on artificial or immaterial distinctions between products, Japan in effect argues that only cases of *de jure* discrimination fall within the prohibition of Article III:4. In the US view,

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<sup>1096</sup>Ibid., pp. 386-387, paras. 5.11 and 5.13.

<sup>1097</sup>*United States - Alcoholic Beverages*, op.cit., p. 279-281, para. 5.31-5.32, 5.35, citing Panel Report on *Canada - FIRA*, BISD 30S/140, 160-61.

<sup>1098</sup>*United States - Alcoholic Beverages*, op. cit., p. 279, para. 5.31.

<sup>1099</sup>See e.g., *United States - Standards for Reformulated and Conventional Gasoline*, adopted on 21 May 1996, WT/DS2/8; *United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco*, adopted on 4 October 1994, DS44/R; *United States - Taxes on Automobiles*, dated 29 September 1994, (unadopted); *United States - Alcoholic Beverages*, adopted on 19 June 1992, BISD 39S/206; *Canada - Alcoholic Drinks*, op. cit.; *United States - Section 337*, adopted on 7 November 1989, BISD 36S/345; *Canada - FIRA*, adopted on 7 February 1984, BISD 30S/140; *EEC - Measures on Animal Feed Proteins*, adopted on 14 March 1978, BISD 25S/49; and *Italian Discrimination against Imported Agricultural Machinery*, adopted on 23 October 1958, BISD 7S/60.

<sup>1100</sup>See e.g., *Japan - Taxes on Alcoholic Beverages*, WT/DS8, 10, 11/R; *United States - Alcoholic Beverages*, op. cit.; *United States - Taxes on Petroleum and Certain Imported Substances*, adopted on 17 June 1987, BISD 34S/136; *Japan - Customs Duties, Taxes, and Labelling Practices on Imported Wines and Alcoholic Beverages*, adopted on 10 November 1987, BISD 34S/83. Japan notes that most Article III "like product" cases involve taxes under Article III:2 rather than regulations under Article III:4. The general principles are the same, however, regardless of whether taxes or regulations are at issue.

Japan articulates an unduly narrow construction of Article III that is not supported by the language of the article, prior GATT cases or the general principle of Article III:1. Given that Article III:4 makes clear that "all" laws, regulations and requirements resulting in "treatment less favourable" to imported products than domestic products are impermissible, the United States maintains that this provision contains no limitation in this regard and cannot be said to indicate a requirement that a measure be discriminatory on its face.

7.52 The United States contends that, while many GATT cases have involved overt discrimination, these cases in no way suggest that a dispute must fall into one of the two categories described by Japan. Panels have articulated the expansive nature of Article III:4 by recognizing correctly that Article III:4, "informed" by Article III:1, must be sufficiently flexible to reach the vast array of situations in which WTO Members may attempt to afford protection to domestic production by according imports less favourable treatment.<sup>1101</sup> The United States points out that the panel on *United States - Section 337* made precisely this point in stating that "the 'no less favourable' treatment requirement set out in Article III:4, is unqualified".<sup>1102</sup> That panel went on to explain that the presence of facial discrimination or overtly different treatment, while an important consideration, is not in and of itself dispositive of the question of whether less favourable treatment has been accorded. The panel stated that "it has to be recognized that there may be cases where application of formally identical legal provisions would in practice accord less favourable treatment to imported products".<sup>1103</sup> Only by looking to how measures actually apply "in practice" will a panel be able to determine whether imported goods receive "effective equality of opportunities".<sup>1104</sup>

7.53 In this light, the United States submits that panels have gone beyond the face of measures, examining the practical competitive opportunities available in the market, to determine whether measures in dispute accord less favourable treatment.<sup>1105</sup> The panel on *Canada - Alcoholic Drinks* addressed seemingly even-handed minimum price provisions,<sup>1106</sup> which applied both to foreign and domestic beer and stated that the national treatment requirement "was normally met by applying to imported products legal provisions identical to those applied to domestic products, but that there may be cases where the application of formally identical legal provisions would in practice accord less favourable treatment".<sup>1107</sup> That panel found:

"that minimum prices applied equally to imported beer did not necessarily accord equal conditions of competition to imported and domestic beer; whenever they prevented imported beer from being supplied at a price below that of domestic beer, they accorded in fact treatment to imported beer less favourable than that accorded to domestic beer; when they were set at the level at which domestic breweries supplied beer ... they did not change the competitive opportunities for domestic beer but did affect the competitive opportunities of imported beer which could otherwise be supplied below the minimum price".<sup>1108</sup>

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<sup>1101</sup>These cases make plain that Article III:4 requires Members to "treat the imported products in the same way as the like domestic products once they had been cleared through customs." Appellate Body Report on *Japan - Alcoholic Beverages*, p. 16.

<sup>1102</sup>*United States - Section 337*, op.cit., p. 386, para. 5.11.

<sup>1103</sup>*Ibid.*

<sup>1104</sup>The US emphasizes that the panel made clear that the analysis of whether a measure accords less favourable treatment is prospective, looking at whether the provision in question "may lead" to less favourable treatment (*Ibid.*, para 5.13). That no harm had yet been shown on market access for imports did not necessarily effect the outcome of the panel's review.

<sup>1105</sup>*Ibid.*, p. 394, para. 5.30.

<sup>1106</sup>"The panel took note of the fact that the minimum price was set at the lowest price at which certain domestic beers were sold." *Canada - Alcoholic Drinks*, BISD 39S/27, 83-84, para 5.27.

<sup>1107</sup>*Ibid.*, p. 84, para. 5.29.

<sup>1108</sup>*Ibid.*, pp. 84-85, para. 5.30.

(iii) **Impact on competitive conditions for imported film and paper**

7.54 **Japan** argues that - even if the Panel accepts the US argument that the so-called "distribution countermeasures" constitute laws, regulations, or requirements within the meaning of Article III -, it must still determine whether those laws, regulations or requirements accord less favourable treatment to imports than to like domestic products.

7.55 The **United States** alleges that by promoting the restructuring of the photographic materials distribution system, the Japanese Government modified the conditions of competition in the industry. Whereas the majority of photospecialty wholesalers formerly carried multiple brands of film, not one of these wholesalers continued to handle foreign film after Japan implemented the distribution countermeasures. The United States explains that, in cooperation with the domestic industry, MITI used three methods to tie wholesalers to individual domestic manufacturers of photographic materials. MITI instructed the latter to use:<sup>1109</sup>

- (1) standardized transaction terms, such as volume discounts, rebates and common credit terms;
- (2) joint activities between domestic manufacturers and wholesalers, including joint warehouses and distribution routes; and
- (3) mutual computer links, data bases and commercial orders.

In the view of the United States, each of these policies was intended to minimize competition among domestic manufacturers and to make wholesalers more dependent on the domestic manufacturer with which it primarily did business.

7.56 The United States alleges that the rationale underlying the *Canada - Alcoholic Drinks* and *United States - Alcoholic Beverages* panel reports applies with equal force in the present circumstances. Due to Japan's restructuring of the distribution system and the creation of exclusive arrangements among domestic photographic materials manufacturers and primary photospecialty wholesalers, domestic manufacturers have access to a significant method of distribution that has been denied to foreign manufacturers. It is irrelevant whether some alternative distribution channels may be available for foreign producers because primary wholesalers have considerable advantages with respect to infrastructure and ties to retailers. Distribution opportunities have been denied to foreign producers as a result of its policies and actions because Japan may not create a system in which domestic producers are given greater avenues of distribution than their foreign competitors. Accordingly, Japan's restructuring of the distribution system for photographic materials in effect denies access to *any* distribution channel - let alone the most valuable one in the market as in this case - and amounts to less favourable treatment in violation of Article III:4.

7.57 **Japan** submits that the panel reports cited by the United States are not applicable to the circumstances of the present case because in those cases, imports were legally forbidden from using certain distribution channels that were open to domestic products. In response to the US argument that imported film and paper have likewise been excluded from distribution channels, and thus have been denied "effective equality of opportunities" required by Article III, Japan argues that even if the domestic manufacturers' primary wholesalers were to be defined as a separate distribution channel,

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<sup>1109</sup> According to the United States, MITI established committees comprised of government and industry officials dedicated to forming vertical distribution channels in order to implement its plans. MITI and its committees issued many reports urging photographic materials industry to accept "systemization". These documents repeatedly called for use of standardized practices to act as liberalization countermeasures combating foreign competition. To ensure compliance from the private sector, the government coordinated the efforts of various participants and contributed expertise and financing. In particular, the United States describes that the government, through JDB and SMEA, gave financial support for domestic manufacturers, wholesalers, and photo finishing laboratories to achieve systemization.



imports are not legally excluded from it. Japan asserts that the United States has not pointed to any governmental prohibition that prevents those wholesalers from carrying other brands of film if they so choose.

7.58 With respect to *film*, Japan stresses that foreign brands are not prohibited from using any distribution channel. The major foreign brand, Kodak, uses exactly the same three basic channels of distribution through which domestic film brands are sold. Japan explains that Kodak sells all its product to a primary single-brand national wholesaler (i.e., Kodak Japan, formerly Nagase and then Kodak-Nagase), which then sells (1) directly to large retailers, (2) through secondary wholesalers, and (3) through affiliated photofinishing laboratories. Given that Kodak, Fujifilm, and Konica all sell through *single-brand* primary wholesalers, it is necessarily the case that they do not sell through the same particular primary wholesalers because, by definition, a single-brand wholesaler is only carrying the products of a single manufacturer at a particular point in time. This does not mean, though, that imports have been excluded from a distribution channel.

7.59 With respect to *paper*, Japan contends that imported paper is sold through the same distribution channels as domestic paper.<sup>1110</sup> Since paper customers only use one brand of paper at a time, for Japan it follows of necessity that foreign and domestic paper producers do not share the same customers at any given time; nevertheless, they all use the same basic channels of distribution. In Japan's view, there has been no exclusion. In the alternative, even if the specific customers of the domestic paper manufacturers are defined as constituting a separate distribution channel, Japan argues that there is no governmental prohibition that prevents those customers from switching paper brands if they so choose.

7.60 The **United States** responds that Kodak Japan, which was created through a merger with a division of a Japanese import-export company, is not a "primary photospecialty wholesaler." Kodak Japan is the local subsidiary that Eastman Kodak established to distribute its products after the company lost access to all main photospecialty wholesalers in Japan.<sup>1111</sup> Unlike the primary photospecialty wholesalers, Kodak Japan does not have longstanding relationships with customers nationwide, does not carry a wide array of photospecialty products such as cameras and accessories, does not have a large nation-wide sales force, and therefore does not have the same economies of scale and scope as the primary photospecialty wholesalers. The United States also notes that the Japanese photographic industry does not consider Kodak Japan to be a wholesaler, as reflected in the standard industry diagram of film distribution in Japan.<sup>1112</sup> Fuji, by contrast, has exclusive access to all of the primary wholesalers. Simply allowing a foreign manufacturer to establish a local subsidiary does not mean that the foreign manufacturer has equivalent access to the country's domestic distribution system. With regard to photographic *paper*, foreign and domestic firms market directly to photographic laboratories which the United States argues were induced to affiliate with Fuji through SMEA programs explicitly identified as "liberalization countermeasures."<sup>1113</sup>

#### (iv) Causal connection

7.61 The United States emphasizes that the less favourable treatment afforded by the closing of the primary distribution system to imports is manifest because the Japanese Government's role in fundamentally altering the way photographic materials are sold decisively tips the balance of competitive conditions in favour of domestic producers. While foreign manufacturers may resort to smaller wholesalers or direct sales to retailers, these alternatives are wholly inadequate. Smaller wholesalers offer a narrow customer base and tend to be dominated by primary wholesalers and Japanese

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<sup>1110</sup>Japan elaborates that paper is sold through an affiliated sales company to (1) affiliated photofinishing laboratories, (2) a small amount to multibrand secondary wholesalers, and (3) directly to retail minilaboratories.

<sup>1111</sup>US Ex. 89-2 and US Ex. 97-1 and 2.

<sup>1112</sup>Second US Submission, Figure 3, referenced, p. 85, para. 240.

<sup>1113</sup>See section VI.D.3.(e)(ii) on "SMEA loans to photoprocessing laboratories" above, in particular paras. 6.368- 6.369.

manufacturers. Moreover, even if the alternatives were equally desirable, domestic manufacturers would continue to have a broader range of distribution channels. Not only do domestic manufacturers have access to the alternate routes available to foreign producers, but they alone have access to the primary distribution network.

7.62 **Japan** submits that apart from the fact that any alleged "less favourable treatment" does not flow from "laws," "regulations" or "requirements," an examination of the alleged measures at issue shows that none of them makes any distinction between imported and domestic products on the basis of their origin, either explicitly or implicitly. More significantly, they do not distinguish products based on any characteristics at all:

(i) MITI recommendations contained in the 1970 Guidelines apply equally to wholesalers and retailers regardless of what brand of film they sell.

(ii) Similarly, JDB loans and SMEA financing do not distinguish between businesses that sell domestic products and those that sell imported products.<sup>1114</sup> Therefore, Japan concludes that these provisions establish "equal competitive opportunities" for imported and domestic film and paper.

(iii) With respect to JFTC Notification No. 17,<sup>1115</sup> Japan claims that it accorded "treatment no less favourable than that accorded to like products of national origin": First, imported products and domestic products are not categorized separately. Second, the concept of "premium offers to business entrepreneurs" is neither inherently related to domestic products nor to imported products. Restriction of such offers is, therefore, in Japan's view, not inherently less restrictive for domestic products than for imported products.

(iv) Japan explains that the International Contract Notification is also consistent with Article III:4 because: First, the same procedure under the Antimonopoly Law applies to enforcement actions against these contracts and to actions against domestic contracts. Second, the JFTC has not enforced, and will not enforce, MITI's policy through administrative guidance under the notification requirement.<sup>1116</sup>

7.63 The **United States** does not accept that none of the alleged measures of Japan makes any distinction between products, either explicitly or implicitly, based on their country of origin. It argues that Japan studied the Japanese distribution sector and designed and implemented the liberalization countermeasures to protect domestic manufacturers from increased foreign competition, i.e., making domestic manufacturers more resistant to and competitive with foreign competition, as Japan liberalized its tariffs, import quotas, and investments restrictions.

7.64 The United States further argues that irrespective of the facial neutrality<sup>1117</sup> of Japan's distribution countermeasures the true significance of these measures can be assessed only in the context of the Japanese photographic materials market at the time they were imposed and have been applied since.

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<sup>1114</sup>According to Japan, photofinishing laboratories affiliated with Kodak receive SMEA financing, just like Fujifilm- and Konica-affiliated laboratories. JDB Annual Report, 1995, pp. 26-27.

<sup>1115</sup>Japan states that Notification 17 was repealed in April 1996. Therefore, Japan argues that it should not be the subject of the present proceeding. Nor will the general designation of unfair trade practices under the Antimonopoly Law operate to continue the content of the regulation.

<sup>1116</sup>A bill to repeal the International Contract Notification requirement has been introduced to the Diet, in light of the globalization of the Japanese economy and for the reduction of the administrative burden.

<sup>1117</sup>The United States notes that the panel on *Thailand - Cigarettes* acknowledged the argument that a facially neutral ban on advertising could violate Article III:4 in that such a restriction might preserve the market superiority of a dominant domestic supplier. *Thailand - Importation of and Internal Taxes on Cigarettes*, adopted 7 November 1990, BISD 37S/200, 224, para. 78.

Prior to the implementation of the countermeasures, foreign photographic materials were distributed through primary wholesalers largely in the same way as domestic photographic materials. However, after the government intervened in the market, primary wholesalers no longer handled foreign film and paper but instead exclusively handled the products of domestic manufacturers and foreign film remains cut off from all of the primary wholesalers and, as a result, more than half of all retailers selling film.

7.65 **Japan** maintains that the US claim of an Article III violation before this Panel is utterly novel and has no precedent. In Japan's view, the burden is on the United States to demonstrate that application of the alleged measures, which do not distinguish between imports and domestic products, constitutes less favourable treatment for imports. Japan emphasizes that there is nothing inherently unfavourable to imports about encouraging more rational transaction terms, or promoting computerization. In the alternative, even if the MITI's distribution policies sought to encourage single-brand wholesale distribution of film and affiliations between domestic manufacturers and photofinishing laboratories, there is nothing inherently discriminatory against imported products in promoting vertical integration<sup>1118</sup> because imports are fully capable of competing through single-brand distribution channels.<sup>1119</sup>

7.66 The **United States** insists that whenever imported products are subject to less favourable treatment pursuant to government action, the national treatment obligation is violated. The United States contends that according to Japan's interpretation Article III is applicable only in the event that a WTO Member overtly discriminates against the products of other Members through highly formalized legal activity. Such an interpretation would permit less favourable treatment to be accorded as long as it is done in a subtle manner or through informal methods. In the US view, if the Panel accepted Japan's argument this would mean that Article III:4 does little or nothing to guard against hidden trade barriers.

7.67 **Japan** asserts that the current market structures for photographic film and paper do not result from any government action, and cannot be considered "laws", "regulations" or "requirements." Japan recalls that Article III applies only to government actions, and not private conduct. It quotes from the panel report on *United States - Alcoholic Beverages* which states that "[t]he Article III:4 requirement is one addressed to relative competitive opportunities created by the government in the market, not to the actual choices made by enterprises in that market".<sup>1120</sup> Japan concedes that the United States may allege that the distribution arrangements in the Japanese film and paper markets constitute restrictive business practices but maintains that such private practices are outside the scope of current WTO rules.

**(c) Causation of market structure by governmental measures or private practices**

7.68 Japan submits that the Article III argument of the United States collapses due to fundamental factual inaccuracies. In Japan's view, a careful analysis of the "distribution countermeasures" during the 1960s and '70s and the allegedly exclusionary market structures for imports of film and paper imports shows that there is no causal connection between the one and the other. For Japan, single-brand wholesale distribution of film is the standard practice throughout the world. Japan explains that the various alleged distribution measures did not create single-brand distribution. In the Japanese market, single-brand distribution resulted from private business decisions and not from governmental actions because it evolved naturally due to the fact that the production sector developed more rapidly than

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<sup>1118</sup>As Japan discusses in relation to the United States non-violation claims, vertical integration may be procompetitive or anticompetitive, depending on the unique circumstances of each particular case.

<sup>1119</sup>Japan refers to Kodak's success in the Japanese market with respect to x-ray film, motion picture film and microfilm, and Polaroid's success in the instant film market despite the fact that these products are sold through the same kinds of single-brand distribution channels as consumer photographic film.

<sup>1120</sup>*United States - Alcoholic Beverages*, BISD 39S/206, 279-280, para. 5.31. See also *Review Pursuant to Article XVI:5*, adopted on 24 May 1960, BISD 9S/188, 192, para. 12 ("the GATT does not concern itself with such action by private persons acting independently of their governments").

the distribution sector. To compensate for the inefficiencies in the distribution sector, Japanese manufacturers, following the lead of manufacturers in other advanced countries such as the US, decided to integrate forward into distribution to promote the efficient distribution and marketing of their products. Given that single-brand distribution emerged as a predominant industry trend already in the mid 1960s and was virtually complete by 1968 before virtually all of the alleged "distribution countermeasures" were implemented, it would be logically impossible for subsequent government actions to be the cause of single-brand distribution. Therefore, in Japan's view, the current market structure is the result of private business decisions and thus not within the scope of Article III.

7.69 The **United States** responds that it does not predicate its claim under Article III on the notion that Japan's market structure for photographic materials is a "law, regulation or requirement", nor does the United States contend that purely private conduct may trigger a violation of Article III. The United States emphasizes that its claims are based solely on the fact that the Japanese Government intervened in the market to aid its domestic industry in excluding foreign competitors from the most desirable distribution channels which falls squarely within the purview of Article III.

7.70 **Japan** argues that there are absolutely no governmental or legal obstacles that prevent the primary wholesalers of the domestic manufacturers from carrying multiple brands of film,<sup>1121</sup> or that prevent photofinishing laboratories from switching brands of paper.<sup>1122</sup> Japan concludes that thus there is no causal connection between the current market structure and the alleged measures. In Japan's view, what the United States complains about is the divergent competitive impact between a new brand against a dominant brand, and not that between imported products and domestic products.<sup>1123</sup> Japan alleges that the United States has not identified any governmental or legal obstacles, nor has the United States identified any ongoing active government involvement in allegedly encouraging the maintenance of these market structures.<sup>1124</sup>

7.71 Japan also emphasizes that ample evidence demonstrates that imported film and paper enjoy unimpeded access to the Japanese market. Foreign manufacturers are not only allowed to sell through, but in fact do sell through, the same distribution channels used by domestic manufacturers. While the United States argues that these routes are "not viable alternatives", according to Japan, the empirical reality shows widespread availability of Kodak brand film. In Japan's view, Kodak Japan *currently functions as a primary wholesaler* because Kodak Japan sells Kodak brand film to secondary wholesalers and retailers, just like the other primary wholesalers do for other brands. Japan also points out that Asanuma abandoned its dealing with Kodak film in 1975 because Kodak required Asanuma, one of Fuji's current primary wholesalers, to deal with Nagase, Kodak's agent and primary wholesaler then, and Asanuma's competitor.<sup>1125</sup>

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<sup>1121</sup>Japan claims that independent primary wholesalers carrying Fuji brand film are free to carry other brands. Their choice to handle only Fuji brand film is a purely voluntary private business decision. Affidavit of Kaoru Konno, Japan Ex. A-15. Affidavit of Yuki Yoshi Noro, Japan Ex. A-14. Affidavit of Takenosuke Katsuoka, Japan Ex. A-11. Affidavit of Tomihiko Asada, Japan Ex. A-12.

<sup>1122</sup>Japan claims that their choice to affiliate with a particular manufacturer is a purely voluntary private business decision.

<sup>1123</sup>In Japan's view, relaxation of the regulations would not necessarily have operated to the advantage of a new brand, because of the readiness of a dominant brand to counter.

<sup>1124</sup>Japan points out that in the context of its non-violation claims, the United States does not mention any "distribution countermeasures" occurring after the conclusion of the Tokyo Round in 1979. Although the United States does refer to the "ongoing application of distribution countermeasures" after the end of the Uruguay Round in 1994, the only elaboration is a reference to "foreclosure from the primary wholesale channels of distribution" which for Japan does not amount to the mentioning of any government action.

<sup>1125</sup>Japan argues that Asanuma could not buy from Nagase, and then compete with Nagase for the same customers. Today, as Kodak Japan has succeeded Nagase's business to wholesale Kodak film, other primary wholesalers choose not to buy from Kodak Japan, with which they would have to compete for the same customers. Fuji only sells to the primary wholesalers and does not compete with them. Competition among the four primary wholesalers carrying Fuji brand film is at the same level, they all buy from Fuji, and compete with each other on equal terms.

7.72 The **United States** notes its earlier responses to Japan's erroneous claims that Kodak has access to the Japanese market on the grounds that Kodak Japan "currently functions as a primary wholesaler."<sup>1126</sup> The United States further asserts that Japan tries to attribute impeded access to the distribution channels exclusively to private conduct by arguing that the move to single-brand distribution was beginning to occur and would have occurred regardless of the government's measures. If the Panel were to endorse such a rationale, it would signal that WTO Members may aid and abet the development of market forces disadvantaging imported products. In the view of the United States, this result would run counter to the purpose of Article III.

**(d) Conclusions**

7.73 In summary, the United States alleges that Japan implemented the distribution countermeasures to accord less favourable treatment to imported photographic materials. The 1967 Cabinet Decision and numerous other documents reflect a concern that Japanese manufacturers were particularly vulnerable to inroads by foreign producers making effective use of Japanese wholesalers to distribute their products. As a consequence, the Japanese Government adopted a series of measures specifically designed to consolidate the primary distribution channels under the control of Japanese film and paper manufacturers, and thereby severely restricted the opportunities for foreign manufacturers to distribute and sell their products in Japan. Such actions constitute improper protection of domestic products and less favourable treatments of imports in violation of Article III.

7.74 The United States points out that in determining whether Japan's distribution countermeasures violate Article III:4, the Panel need find only that these measures "tend to tip the balance in favour of" Japanese producers of film and paper," whereas in this case, Japan's laws, regulations and requirements have done far more. As a result of Japan's actions, imported photographic materials have been excluded from the primary distribution system and thus have been substantially impaired in their ability to reach a broad segment of retail outlets.

7.75 **Japan** responds that the United States has failed to identify any "laws", "regulations", or "requirements" that would serve as the appropriate subject matter for a claim under Article III, since it identifies only the continued existence of single-brand wholesale distribution for film and affiliations between domestic paper manufacturers and photofinishing laboratories as "distribution countermeasures". Japan's recalls that purely private conduct is outside the scope of Article III. As to the MITI distribution modernization policies of the 1960s and '70s, Japan emphasizes that the administrative guidance subject to US challenge is not within the scope of Article III. Furthermore, given that none of the specific distribution policies from that period is still in effect, Japan contends that they are not properly before this Panel.

7.76 In the alternative, assuming that there "laws", "regulations" or "requirements" in the meaning of Article III at issue, Japan argues that the United States has failed to show that the alleged measures in dispute extend "less favourable treatment" to imported film and paper. Japan emphasizes that the general purpose of this phrase is to protect the equal competitive relationship between imported and domestic products and that Article III:4 does not require any particular results in the marketplace. Furthermore, none of the policies of the Japanese Government was applied so as to afford protection to domestic production within the meaning of Article III:1. Therefore, Japan requests the Panel to reject the claims raised by the United States under Article III.

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<sup>1126</sup>See para. 7.60 above.

## **B. ARTICLE X OF GATT**

### **1. INTRODUCTION**

7.77 According to the **United States**, in devising and implementing its broad set of liberalization countermeasures to protect its market from foreign competition, Japan followed the approach of "concerted adjustment" between government and industry. The Japanese Government acted behind a shield of opacity, deputizing or instructing industry to carry out policies, with incentives and leverage from the government standing behind private industry behaviour. In this context, foreign film and paper manufacturers encountered impenetrable market restrictions of imperceptible origin. In the US view, the restrictions originated with government policy and actions, and the Japanese Government bears responsibility for preventing its trading partners and private businesses attempting to compete in Japan's market from understanding the precise nature of the Government's actions and their consequences. These informal, non-transparent practices remain in place and continue to restrict market access for foreign firms.

7.78 The US claims focus essentially on the following specific measures:

(1) In the context of the Premiums Law and relevant fair competition codes, Japan's failure to publish the JFTC's and the fair trade councils' enforcement actions that establish or modify criteria applicable in future cases violates Article X:1.

(2) In the context of the Large Stores Law and relevant local regulations, Japan's failure to publish guidance through which regional MITI offices, prefectural governments and local authorities make applicants for a new or expanded store under the Large Stores Law coordinate their plans with local competitors before submitting a notification for government review, and continue to impose a "prior explanation" requirement, violates Article X:1.

7.79 As a preliminary matter, **Japan** notes that, while the US request for the establishment of the Panel mentioned violations of Article X:3 of GATT,<sup>1127</sup> the United States has made no legal claims under Article X:3 in its submissions to the Panel. Accordingly, Japan requests the Panel to evaluate the US claims under Article X with exclusive reference to Article X:1 of GATT.

7.80 Japan further responds that the obligations of Article X:1 do not apply to fair trade councils' and JFTC enforcement actions because these are not measures of "general application," but only applications of legal principles to specific factual circumstances which do not establish or modify criteria applicable to future cases. Thus, in Japan's view, the practices alleged by the United States does not exist.

7.81 Further, Japan contends that none of the MITI branches, prefectural governments, or other local governments may either require or recommend that store openers provide prior explanations to, or hold prior consultations with, local retailers. Japan emphasizes that it has corrected and is prepared to correct any such practice upon discovery.

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<sup>1127</sup>Letter from US Ambassador Booth Gardner to WTO Dispute Settlement Body Chairman H.E. Mr. Celso Lafer Requesting the Establishment of a Panel on 20 September 1996.

## 2. **THE LEGAL TEST**

7.82 Article X:1 provides in the relevant part as follows:

"Laws, regulations, judicial decisions and administrative rulings of general application, made effective by any [WTO Member], pertaining to the classification or the valuation of products for customs purposes, or to rates of duty, taxes or other charges, or to requirements, restrictions or prohibitions on imports or exports or on the transfers of payments therefore, or affecting the sale, distribution, transportation, insurance, warehousing, inspection, exhibition, processing, mixing or other use shall be published promptly in such a manner as to enable governments and traders to become acquainted with them".

7.83 The **United States** submits that the purpose of this provision is to ensure a degree of transparency in the imposition of governmental measures that may affect the competitive opportunities of WTO members. Such measures must be "published promptly" in order "to enable governments and traders to become acquainted with them".<sup>1128</sup> The United States explains that, when a WTO Member fails to fulfil its obligations under Article X:1, foreign firms and their governments are unable to understand the "rules of the road" in that market and are impeded in their ability to assess whether fundamental GATT rights, e.g., the right to no less favourable treatment under Article III and the right to benefits arising out of tariff concessions in accordance with Articles II and XXIII:1(b), are being nullified or impaired by that WTO Member.

7.84 **Japan** explains that in order to prove a violation of Article X:1, the United States has to establish the existence of the following elements:

- (i) There is a law, regulation, judicial decision or *administrative ruling*
- (ii) of *general application*,
- (iii) *made effective* by any [WTO Members],
- (iv) pertaining to ... requirements, restrictions or prohibitions on imports, ... or affecting their sale, distribution [of products] ...
- (v) [that] has not been published promptly in such a manner as to enable governments and traders to become acquainted with them.

Only when a measure meets all of these elements stipulated in the provision, does a government owe an obligation to publish under Article X:1.

### (a) **"Laws, regulations, judicial decisions or administrative rulings"**

7.85 In Japan's view, it is clear that none of the alleged measures in dispute amounts to a "law" or "regulation" since none of them was enacted by the Diet, or was promulgated as a regulation under the relevant administrative procedures. Likewise, for Japan it is obvious that none of the alleged measures qualifies as a "judicial decision".

7.86 With respect to "administrative rulings", Japan underscores that it is critical to remember that Article X:1 requires publication only of administrative rulings of "general application". This requirement is crucial especially in evaluating the US claims under Article X relating to the Premiums Law. In Japan's view, the US allegation lacks specificity, and it is difficult to discern by what criteria the United States concludes that certain enforcement actions are administrative rulings of "general application" to be published under Article X:1. Thus Japan claims that the United States has failed to identify any

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<sup>1128</sup>See Panel Report on *EEC - Restrictions on Imports of Dessert Apples, Complaint by Chile*, adopted on 22 June 1989, 36S/93, 133, paras. 12.29-12.30.

appropriate subject matter to be published under Article X:1. Although, the US claim is based on "administrative rulings", the United States fails to specify which administrative rulings are in violation of Article X.

7.87 The **United States** confirms that its Article X:1 claims are based on administrative rulings and not on "laws, regulations, or judicial decisions. The United States agrees that the obligations of Article X:1 apply only to administrative rulings of *general* application. It asserts that Japan enforced the Premiums Law and the Retailers Fair Competition Code as well as the Large Stores Law primarily through informal, unpublished enforcement actions in a manner inconsistent with Article X.

7.88 **Japan** notes that the panel report on *United States - Restrictions on Imports of Cotton and Man-made Fibre Underwear* interpreted the phrase "general application" as meaning that "[i]f, for instance, the restraint was addressed to a specific company or applied to a specific shipment, it would not have qualified as a measure of general application".<sup>1129</sup> From that Japan concludes that the informal actions concerning the Premiums Law and the Retailers Code are not of "general application".

7.89 The **United States** maintains that Japan's failure to publish notice of "administrative rulings of general application" runs counter to Article X:1. Although, no GATT or WTO precedent squarely addresses the issue, the United States submits that Japan has previously taken the position that the publication requirement of Article X:1 extends to the disposition of individual matters by an administrative agency, especially where principles applicable to future decisions are established. In the 1990 panel report on *EEC - Regulation on Imports of Parts and Components*, Japan challenged the EEC's practices regarding the acceptance of undertakings pursuant to the EEC's anti-dumping regulation and the determination of the origin of parts used in assembly operations. Japan argued that:

"[t]he EEC had not made public the criteria used in the consideration of offers of undertakings ... . While the conditions under which duties could be imposed were defined ... the only available information regarding the conditions under which the EEC would consider undertakings acceptable consisted of letters and oral explanations by the EEC officials to companies involved in proceedings".<sup>1130</sup>

"[T]he issue of the determination of the origin of parts or materials used in assembly operations in the EEC had led to difficulties ... . It was only after an investigation ... started that companies engaged in assembly operations within the EEC were in a position to ascertain how the EEC Commission would determine the origin of the parts used in these operations ... [I]n practice, there existed the possibility of changes in the criteria to determine origin ... This had led to problems for certain Japanese producers".<sup>1131</sup>

7.90 The United States notes that because the panel in *EEC - Parts and Components* resolved the matter on other grounds, it chose not to address Japan's Article X argument. Nonetheless, the United States suggests that Japan's previous articulation before that panel of the type of administrative rulings that are subject to Article X should govern in the present case. The United States explains that it does not contend that Article X requires all enforcement actions, no matter how limited in scope or insignificant in developing new doctrine, be made public. However, Article X:1 mandates the publication

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<sup>1129</sup>Panel Report on *United States - Restrictions on Imports of Cotton and Man-Made Fibre Underwear*, WT/DS24/R, adopted on 25 February 1997, para. 7.65. This finding is upheld by the Report of the Appellate Body. Appellate Body Report on *United States - Restrictions on Imports of Cotton and Man-Made Fibre Underwear*, WT/DS24/AB/R, adopted on 25 February 1997.

<sup>1130</sup>Panel Report on *EEC - Regulation of Imports of Parts and Components*, adopted on 16 May 1990, BISD 37S/132, 155, para. 3.53.

<sup>1131</sup>*Ibid.*, p. 156, para. 3.54.



of administrative rulings that establish or substantially revise criteria which subsequently may be applied in other cases in the future, recognizing of course that all disputes should be analyzed on a case-by-case, fact-specific basis. This is particularly significant in the present instance because of the multiple enforcement bodies involved, each of which may follow criteria differing from the others. Thus, the United States claims that Japan's lack of transparency in the frequent use of unpublished enforcement actions fails to make public applicable criteria and guidance that may be relied upon as precedent in future cases. Japan's complaint about the EC' measures in *EEC - Parts and Components* applies with equal force in the present dispute and thus Japan should be instructed to publish Premiums Law and Large Retail Store enforcement actions of general applicability so that traders and WTO Members may become acquainted with them.

7.91 While **Japan** maintains the position it took in *EEC - Parts and Components*, i.e., that Article X:1 mandates the publication of administrative rulings that establish or substantially revise criteria which subsequently may be applied in other cases<sup>1132</sup>, it emphasizes that its position does not apply to the present case. Japan considers that it has duly published all laws, regulations, judicial decisions or administrative rulings of general application relating to the Premiums Law or Large Retail Stores Law in a manner that enables governments and traders to become acquainted with them. Japan maintains that the United States fails to identify any particular unpublished enforcement actions that fall in the definition of "general application" and, therefore, has failed to discharge its burden of proof in this regard. Therefore, the United States has failed to identify any proper subject matter for an Article X:1 claim, and it is thus irrelevant whether any of these alleged measures have been published in accordance with Article X:1.

### 3. MEASURES TAKEN IN THE CONTEXT OF THE PREMIUMS LAW

#### (a) Premiums Law enforcement actions

7.92 The **United States** alleges that Japan contravenes the publication requirement of Article X:1 because Japan's enforcement of its premium and representation provisions is shrouded in secrecy resulting from the use of informal mechanisms. Accordingly, Japan is alleged of having established a complex, multi-tiered enforcement system for its premium and representation restrictions. Under the Premiums Law, the JFTC, the prefectures and deputized private sector councils have authority to enforce the law. The number of entities involved in policing promotional activities results in substantial confusion for enterprises doing business in Japan. Not only are regulated businesses at times unsure as to which enforcement body is likely to take action on a particular matter, but those subject to the restrictions have access to little or no public record reflecting how the JFTC, a prefecture or a council may have addressed similar facts in the past and, thus, how it is apt to rule in the future. This confusion principally arises from Japan's failure to publish a large percentage of administrative rulings and enforcement actions taken and the difficulty in obtaining what little information may be available. Therefore, the United States alleges that Japan's practice of failing to publish enforcement actions of general application concerning premiums and representations violates Article X:1.

7.93 **Japan** contends that the enforcement system of the Premiums Law is sufficiently transparent and consistent with Article X:1.<sup>1133</sup> Enforcement regulations for the Premiums Law are published and readily available, and the Premiums Law itself as well as numerous general and specific notifications

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<sup>1132</sup>Ibid.

<sup>1133</sup>According to Japan, one scholar notes that "[i]n the United States, Federal, State and even local governments independently regulate advertising. Each level of government enacts its own legislation and had its own separate administration to carry out this legislation." James R. Maxeiner and Peter Schotthöfer (eds.), *Advertising Law in Europe and North America* (1992), p. 317. It was also noted that "[s]elf-regulation is an important source of advertising regulation, especially for national advertising." Ibid., p. 321, Japan Ex. E-13.

interpreting it have also been published.<sup>1134</sup> Japan further responds that there is an ample public record from which one can discern how the Premiums Law will be applied. Specific enforcement actions simply apply general norms to the facts of a particular case.

7.94 Japan points that the United States itself specifically identifies and refers to numerous JFTC notifications which explain how the Premiums Law is applied: (i) Notification 17, identified by the United States as "[o]ne of [the JFTC's] most significant restriction on premiums."<sup>1135</sup>; (ii) Notification 34, which allegedly reflected "a distinctly new way" of applying the Premiums Law; (iii) Notification 5, which allegedly "tightened [JFTC] control on the use of premiums offered to consumers".<sup>1136</sup> The JFTC has also published detailed notifications whenever it has announced "significant restrictions", "a distinctly new way," or "tightened" control. In addition, recent decisions by the JFTC to revise and clarify the regulations on excessive premiums have also been published.

7.95 In response, the **United States** submits that since the Premium Law was enacted in 1962, the JFTC has initiated relatively few formal enforcement actions, but it has issued many "administrative guidances" or warnings. Japan has failed to publish the overwhelming majority of its enforcement actions under the Premiums Law. By one estimate,<sup>1137</sup> between 1962 and 1994, the JFTC issued warnings or administrative guidances in 11,362 cases, as opposed to 683 formal cease and desist orders. The JFTC has handled a large number of Premiums Law cases through informal means, presumably resulting in unpublished findings in almost every instance.<sup>1138</sup> This lack of transparency is compounded by the fact that Japan's 47 prefectural governments take thousands of informal enforcement actions, for which the United States has been unable to find a publication or written description.<sup>1139</sup>

7.96 **Japan** replies that almost 700 cease and desist orders have been published and have further clarified the general principles behind the enforcement of the Premiums Law. The relevant issue under Article X:1 is not whether informal action is ever taken. The only issue is whether any new policy is being applied without adequate disclosure. These case discussions are also included in the JFTC's annual reports since 1967. Furthermore, since 1985 the JFTC has published the outlines of major cases where warnings were given, which is another source of information concerning how the Premiums Law is applied in specific factual situations. Finally, the JFTC answers questions posed by interested enterprises concerning the interpretation of the Premiums Law. The record of important questions and answers, which may be of some use to businesses, are published as "Actual Examples of

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<sup>1134</sup>Kanpo, 15 May 1962. The law and its notifications are published not only in Kanpo, but also in the Genkou Houki Souran. Enforcement standards are published in the Keihin-koukoku Housei Binran.

<sup>1135</sup>Japan states that Notification 17 has been abolished.

<sup>1136</sup>Japan underscores that the US Appendix provides extensive documentation of JFTC notifications and other explanations of Premiums Law enforcement.

<sup>1137</sup>20 Years of Promulgation of the Act Against Unjustifiable Premiums and Misleading Representations, Kosei Torihiki Joho, 30 August 1982, pp. 14-17, US Ex. 82-10. If two other categories of JFTC action - "cautions" and "instructions" - are included, the total number of informal actions rises to 120,000. 1992 JFTC Annual Report, pp. 84-85, US Ex. 73; 1995 JFTC Annual Report, p. 242, US Ex. 85. There appear to be only two sources, *ad hoc* press releases and the Annual Compilation of Major Requests and Warnings, that carry discussions of warnings, the most formal of administrative guidance measures. However, the selection of which actions are covered seems to be random.

<sup>1138</sup>The United States quotes from a former senior JFTC official's statement who explained that: "Informal ways of enforcement had the problem of lack of transparency. By making the FTC "warning" public, effectiveness of the warning as an informal way of enforcement would increase. It should be remembered that public announcements or disclosure has an aspect of an effective remedy in such a country as Japan where bad publicity is a very serious concern to business". "Too much reliance on informal enforcement could produce a lack-of-transparency problem. Sometimes, non-disclosure becomes an important component of informal enforcement, that is, non-disclosure makes it easy to get the compliance of the related entrepreneurs. On the other hand, non-disclosure has a problem of its own, namely, it does not educate other businessmen who engage in the same conduct, and the general public will not have sufficient information concerning enforcement of the [Antimonopoly Law] Act." Iyori Hiroshi and Uesugi Akinori, The Antimonopoly Laws and Policies of Japan, 1994, pp. 213-214, 216-217, US Ex. 94-1.

<sup>1139</sup>According to the United States, more than 85 percent of all informal actions taken are cautions issued by prefectural governments.

Consultations Regarding Premiums and Representations". Japan claims that the JFTC has thus consistently published all administrative rulings of "general application". Japan considers as significant that the United States does not make a single specific allegation of any JFTC enforcement action at odds with already published policies.

7.97 The **United States** responds that while Japan maintains that the JFTC has met the obligations of Article X:1 by publishing cease and desist orders and other formal actions taken under the Premiums Law, it offered no explanation as to why it has not published thousands of the JFTC's informal enforcement actions. Japan alleged that none of the unpublished enforcement actions involves the establishment or modification of criteria that may be applied in future cases. In the US view, it is not credible that more than 90 percent of the JFTC's enforcement actions have no effect on the shaping of doctrine or the case law subsequently to be applied. In this regard, the United States recalls that Japan took the position that the publication requirement of Article X:1 should be applied "not only to mandatory laws, but also provisions of laws that have the character of a recommendation or exhortation."

**(b) Actions under "Fair Competition Codes"**

7.98 The United States reports that none of the four private sector surrogate enforcement bodies to which the JFTC has delegated authority, i.e., (1) the Retailers Fair Trade Council, (2) the Promotion Council, (3) the Manufacturers Fair Trade Council and (4) the Wholesalers Fair Trade Council, publishes its enforcement actions so that traders and governments may become familiar with them. The Promotion Council's rules on dispatched employees and representations, as well as both the camera Manufacturers and Wholesalers Codes, contain no requirement that enforcement actions be recorded, let alone published. Only the Retailers Code requires that a written record be made of enforcement actions but publication is not mandatory.<sup>1140</sup>

7.99 **Japan** pointed out that fair competition codes and fair trade councils are irrelevant because no codes or councils cover photographic film and paper. Japan responds that the private sector "fair trade councils" have no power as an enforcement body. Therefore, Japan takes the position that the industry self-regulation codes in dispute are purely private action and that no government action is required or even authorized to make it public. Moreover, fair competition codes are published in the Official Gazette when the JFTC approves them, although they fall, in Japan's view, outside the scope of Article X.

7.100 Japan explains that the "fair competition codes" reflect the general norms of the Premiums Law, not some illicit, collusive purpose. Although the codes are initially drafted by industry groups, no code comes into effect until it has received official review and approval from the JFTC in accordance with Article 10 of the Premiums Law. The general principles to be applied are all clearly stated in the codes themselves, which are published in the Official Gazette. In Japan's view, the United States has not even alleged any action taken that was at odds with basic principles set for in the codes.

7.101 In the view of the **United States**, Japan did not contest that enforcement actions taken by "fair trade councils" are unpublished. In response to Japan's argument that the actions of these councils are purely private conduct and thus outside the scope of Article X, the United States emphasizes that the "fair trade councils" and "fair competition codes" are creations of Japanese law, in particular section 10 of the Premiums Law, and they remain under the supervision of the JFTC. The United States urges Japan to accept responsibility for the actions of these councils in this matter just as it did in 1987 before the panel on *Japan - Liquor Taxes and Labelling Practices*, where Japan referred to its system of "fair competition codes" under the Premiums Law as a form of "legal regulation".

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<sup>1140</sup>The Retailers Council informed the US Government that it does not publish a monthly magazine, but referred the United States to the Zenren Tsuho, the official publication of the photographic retailers association.

7.102 The United States also rejects Japan's alternative argument, that the published "fair competition codes" specify all generally applicable criteria and that, accordingly, the publication of enforcement actions taken under these codes is unnecessary. In the US view, Japan's position seems to be that publication of a set of rules negates any obligation under Article X:1 to publish subsequent interpretations and actions taken pursuant to those rules. The United States emphasizes that Article X:1 requires not only initial publication of a law or regulation, but also the publication of any subsequent actions taken under such provisions. Otherwise, the term "administrative rulings" in Article X:1 would remain devoid of meaning.<sup>1141</sup>

7.103 **Japan** emphasizes that no fair competition code is covering film products, and that no code in a somewhat related field, such as that covering cameras, has ever been extended to apply to film. Thus, in Japan's view, there are no codes for photographic film or paper that must meet Article X:1 transparency requirements.

**(c) Requests for information and disclosure of confidential information**

7.104 The **United States** explains that the problems inhering in Japan's failure to publish the results of these enforcement activities are exacerbated by the difficulty of obtaining information about them. The United States has made repeated requests to receive such information from the Japanese Government, the respective enforcement councils and relevant photographic trade associations.<sup>1142</sup> Almost without exception, these requests for information were denied.

7.105 **Japan** responds that in 1996 the JFTC received requests from the US Embassy in Tokyo for information on certain matters related to the regulations on excessive premiums and misleading representations, with the explanation that it was being sought in connection with the WTO proceedings. The JFTC provided the Embassy with the information that had been made available to the public, but declined to provide non-public information. It is the JFTC's understanding that the kind of information the JFTC did not provide to the US Embassy is outside the scope of the obligations under Article X:1.

7.106 Japan notes that as a general matter, requests for information are granted as long as there are no concerns about disclosure of confidential information. However, Article X:1 sets out a specific exception under which this Article will "not require any [WTO Member] to disclose confidential information which would impede law enforcement or otherwise be contrary to the public interest or would prejudice the legitimate commercial interests of particular enterprises, public or private".<sup>1143</sup>

7.107 With respect to the specific exception in Article X:1, the **United States** responds that the types of information that Japan should be disclosing in the context of the Premiums Law do not implicate confidentiality concerns. The United States explains that other countries publish information concerning specific enforcement actions and that company-specific commercial information which deserves protection can be protected on a case-by-case basis by redacting the critical information from the public version of the document without withholding the entire document.

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<sup>1141</sup>For the United States, it bears noting that Article X:1 distinguishes between "administrative rulings" and "regulations".

<sup>1142</sup>The United States elaborates that between July 1996 and November 1996, an official at the US Embassy in Tokyo sent five letters to the JFTC, four letters to individuals and entities associated with the Retailers Council, and one letter to the Promotion Council. The letters asked for information about implementation and enforcement of the Premiums Law, and related matters. None of the responses provided the requested information.

<sup>1143</sup>Japan points out that under US law there is a specific exception to the Freedom of Information Act to allow authorities to refuse such disclosure.

#### **4. MEASURES TAKEN IN THE CONTEXT OF THE LARGE STORES LAW**

##### **(a) MITI's "prior explanation" procedures**

7.108 The United States submits that from the inception of the Large Stores Law, MITI has increasingly expanded the role and leverage of local retailer interests in reviewing the proposed opening or expansion of a large store. As their opportunities to influence the large store adjustment process increased, local retailers increasingly employed their influence to impose delays, floor space reductions, and other "adjustments" on large stores. The United States describes that in 1982, Japan formally required the builder of a large store to consult with local retailers and seek their agreement for a new or expanded store even before the builder or retailer had formally notified the government of its intention to build or expand a large store. This "prior adjustment" process became a very powerful means for the local retailers to wield influence over large stores because the formal large store review procedures accord decisive weight to the views of local business interests in determining whether a new or expanded large store will be forced to "adjust" its plans (e.g., reduce its floor space or hours operation).

7.109 According to **Japan**, the United States limits its claims under Article X regarding the Large Stores Law to an allegedly unpublished policy of requiring new store openers to make prior explanation or consultation. Japan points out that in 1992 MITI formally eliminated the requirement under the Large Stores Law that large store planners provide a prior explanation to local retailers before the initial notification that commences the law's formal review and adjustment process. Procedural requirements for notifications of new stores were published, e.g., in the 1992 Public Briefing Circulars and the 1994 Public Briefing Circulars. They describe in detail what is expected of large store planners under the law and reflect the 1992 policy decision to abolish the previous "prior explanation" procedures<sup>1144</sup> Japan contends that none of the MITI branches, prefectural governments, or other local governments may either require or recommend that store openers provide prior explanations to or prior consultations with local retailers. Japan emphasizes that it has corrected and is prepared to correct any such practice upon discovery.

7.110 The **United States** confirms that an administrative directive from MITI of 29 January 1992 addresses the elimination of the prior explanation requirement under the Large Stores Law. In the US view, MITI formally revoked this prior adjustment requirement in response to pressure from foreign governments to liberalize large store restrictions. However, the United States contends that the circulation of pamphlets does not amount to a publication "in a manner as to enable governments and traders to become acquainted with [legal requirements]" within the meaning of Article X:1.<sup>1145</sup>

##### **(b) "Local explanation" procedures**

7.111 According to the United States, studies by the Japanese Government<sup>1146</sup> document that in practice MITI regional offices and prefectural and local governments continue in many cases to require, urge, advise or request large stores pursuant to informal administrative guidance to consult and undertake prior consultation and effectively to make adjustments with local retailers and small stores competitors before submitting their formal notification under Article 3 of the Large Stores Law to the government. In numerous cases, retailers proposing to open or expand large stores continue to feel compelled to

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<sup>1144</sup>Japan submits that one of the 1992 Public Briefing Circulars explicitly abolished the authority of any MITI official to require a prior explanation to local retailers. Similarly, the other abolished this same authority with respect to the prefectural governors. MITI, Public Briefing Nos. 25 and 26, Japan Ex. C-17.

<sup>1145</sup>The United States points out that the authorities themselves did not admit in the survey by Japan's Management and Coordination Agency that they had such pamphlets.

<sup>1146</sup>In support of its argument, the United States refers to studies by the JFTC and Management and Coordination Agency (MCA) indicating that the authorities continue to guide large retailers to consult with local business interests before filing an Article 3 notification.

negotiate with small retailers because the law and MITI guidance give the local retailers ample opportunity and power to force severe adjustments on large retailers who do not negotiate with them in advance. Local retailers continue to succeed in extracting restrictive agreements from large stores as a condition for allowing the formal new store opening procedures to proceed "smoothly".<sup>1147</sup> Japan is alleged not to have published the instances in which it has imposed the requirement. Therefore, Japan's continued application of the "prior explanation" requirement is unpublished, leaving foreign traders and WTO Members uncertain as to the relevant criteria government entities rely upon in imposing it in a given case.

7.112 **Japan** responds that neither MITI nor any local government maintains any rule which "requires or recommends" that store openers provide prior explanations of store opening plans to local retailers or undertake prior consultations. As a deregulation measure to shorten the examination period under the Large Stores Law, and to clarify when that period officially began, MITI explicitly repealed the practice of prior explanation and prior consultation and affirmatively promulgated this repeal among the regional MITI branches and the prefectural governments.<sup>1148</sup> MITI has also specifically encouraged the prefectural governments to ensure that the municipalities within their jurisdiction comply with these deregulation measures.<sup>1149</sup> In addition, based on its authority under Article 15(5) of the Large Stores Law, Japan has explicitly prohibited all prefectural and local governments from requiring or recommending prior explanation through additional local regulations based upon their regulatory authority delegated by the Local Autonomy Law.<sup>1150</sup> Accordingly, Japan ordered that corrective action be taken against "excessive local regulations," including any rules for prior explanation, and that by 1993, such local regulations be brought into conformity with the national law.

7.113 In the view of the **United States**, Japan merely argues that the Large Stores Law itself does not require prior consultation. That the practice is no longer required under the law does not mean that Japanese officials are not imposing it. The United States underlines that the prior consultation requirement appears not in the text of the law but in the practice of numerous MITI regional offices and prefectural and local governments. The requirement has never been written in the text of the law. While from 1982 to 1992 it at least was written with transparency in a MITI directive, the requirement has now become a non-transparent burden on large stores. The United States emphasizes that Japanese Government studies amply document the continuation of an effective prior consultation requirement.

7.114 **Japan** concludes that where store planners are still offering a prior explanation to local retailers, the decision to do so is based not upon any government requirement, but upon the store planners' own and purely private business decision,<sup>1151</sup> such as the need to obtain information that might help the store planner to develop business from local retailers or the wish to accelerate the completion of public briefing procedures under the law. Japan explains that upon receipt of Article 3 Notifications, a relevant MITI branch or prefectural government has to select consumers and local retailers (or other associations)

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<sup>1147</sup>"Concerning the Reevaluation of Government Regulations in the Distribution Sector," Government Regulation and Competition Policy Research Council, JFTC, June 1995, pp. 22-23, US Ex. 95-11.

<sup>1148</sup>In 1982, MITI issued circulars guiding MITI branches and prefectural governments to request that store openers would give prior explanation to "municipal governments, etc. governing planned sites" (subsequent circulars specified "municipal governments, Chambers of Commerce and Industry, small and medium-sized retailers, and consumers"). Immediate Measures Regarding Notification to Establish Large Scale Retail Stores, Sankyoku, No. 36, issued by Director-General for Commerce and Distribution Policy [hereinafter "Director-General"], 30 MITI January 1982, Japan Ex. C-16. However, in 1992, MITI issued circulars instructing both MITI branches and prefectural governments (1) to abolish any proceedings prior to Article 3 Notifications, and (2) to request that store openers give public briefings, similar proceedings, however, subsequent to Article 3 Notifications. Instructing Parties Filing Notifications of New Type-I Large Scale Retail Stores etc. to Hold Public Briefing, Sankyoku, Nos. 25 and 26, issued by Director-General, MITI April 1, 1992, Section 1, Japan Ex. C-17.

<sup>1149</sup>The Circulars issued by MITI instruct both MITI branches and prefectural governments to abolish any proceedings prior to Article 3 Notification. 1990 Prior Explanation Circular, Japan Ex. F-11.

<sup>1150</sup>See Additional Local Regulations on New Store Openings, etc. by Local Governments, Sankyoku, No. 24, issued by Director-General, MITI, January 29, 1992, Section III, Japan Ex. C-13.

<sup>1151</sup>MCA Report, pp. 13-14, US Ex. 95-15.

who are to receive public briefings after consulting with relevant Chambers of Commerce and related local governments, if necessary.<sup>1152</sup> The fact that store planners offer prior explanation to local retailers does not in any way mean that government entities "request or recommend" prior explanation as a matter of general policy.

**(c) Specific examples: The MCA and JFTC studies**

7.115 The **United States** elaborates that according to the 1995 survey by Japan's Management and Coordination Agency (MCA), several MITI regional offices and prefectural governments require or recommend such prior explanations as a matter of general policy.<sup>1153</sup> For example, in 1995, the MCA surveyed the prior consultation practices at six MITI regional offices and six prefectural or local governments. Nine of the twelve jurisdictions regularly required or urged large stores to undertake prior consultation and adjustment. The United States identified seven specific instances in which the "prior explanation" was imposed after it had purportedly been revoked:

- (i) The Tokyo Municipal government published two pamphlets regarding the Large Stores Law process which "direct retailers to provide the MITI regional office, the prefecture, the local town and ward governments and the Chamber of Commerce with an explanatory outline of their plans".
- (ii) The Osaka Prefectural government "requires prospective applicant retailers to provide concerned town governments and ward councils with a pre-notification explanation of its application and to obtain a stamp as a proof that it had provided such explanation. Some cities and chambers of commerce [in the prefecture] indicate that providing local retailers' associations with a pre-notification explanation is a condition for accepting the application".
- (iii) The Chugoku regional office of MITI has published a manual that "directs prospective retailers to provide pre-notification explanation to concerned local and ward governments and Chambers of Commerce".
- (iv) The Kinki regional office of MITI "directs applicants to provide pre-notification explanation to concerned local parties in order to make the process go smoother".
- (v) The Kanto regional office of MITI (Tokyo area) "instructs" retailers "to consider the advantages of meeting with local retailers' associations in order to make the process go smoothly".
- (vi) The Tohoku regional office of MITI and the Miyazaki prefectural government advise large stores that "prior explanation would make the process go more smoothly".
- (vii) The Hiroshima prefectural government orally requests "that the office, prefecture, town and ward governments and Chambers of Commerce be provided with pre-notification Article 3 explanation".

7.116 With respect to the MCA Report, **Japan** explains that all MITI branches and prefectural governments subject to the report responded that they did not instruct store planners to provide a prior explanation.<sup>1154</sup> The discussion of prior explanation procedures in the MCA Report is based on the

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<sup>1152</sup>1994 Public Briefing Circulars, Japan Ex. C-18, Section VI.

<sup>1153</sup>Results of the Survey Regarding the Liberalization of Regulations: Application of Laws Dealing with Adjustment of Retail Business Activities in the Area of Large Scale Retail Stores, Management and Coordination Agency, October 1995, pp. 11-12, US Ex. 95-15.

<sup>1154</sup>MCA Report, p. 11, US Ex. 95-15.

limited responses of only 11 large stores that primarily offered prior explanations based on their own private business decisions.<sup>1155</sup> Specifically, of the 11 large stores that responded, 8 replied that they conducted prior explanation at their own choosing. The remaining three explained that their decision to provide prior explanation stemmed primarily from some undefined form of "administrative guidance" or "local custom". It is Japan's understanding that the three cases described loosely as "administrative guidance" are actually instances in which officers in the relevant authority, in response to store planners' specific inquiries for consultation on this point, simply responded with the suggestion that it might be beneficial for them to contact with, e.g., relevant local governments, as early as possible in the process. Moreover, the Report never suggests that any local customs that may exist are at the behest of a government entity. Japan stresses that nothing in the MCA Report suggests that any MITI branch or prefectural government suggests either prior explanation or prior consultation as a general policy.

7.117 According to Japan, the MCA survey indicates that guidance by MITI branches and local governments to provide "prior explanations" occurred only in exceptional cases when the survey was conducted in 1995. Japan has recently taken corrective measures against all inappropriate practices identified in the MCA Report. For example, when MITI learned in 1995 that the Chugoku MITI branch<sup>1156</sup> and Hiroshima prefecture<sup>1157</sup> were issuing guidance for large store planners to provide "prior explanation," MITI ordered that these authorities cease issuing such guidance, and the situation has been redressed. Moreover, as of 31 March 1997, the Osaka Prefectural Government<sup>1158</sup> no longer requires the receipt of seal impressions from concerned municipal governments and Chambers of Commerce as a condition for the acceptance of Article 3 Notifications. In addition, the Chugoku MITI Branch no longer provides store openers with the pamphlets described in the MCA Report.<sup>1159</sup> Japan has been making a continued effort to find and correct any such excessive local regulations and practices. To facilitate this effort, Japan has established ombudsman's offices in MITI and MITI branches since April 1994 to deal with problems that store planners encounter in the context of the administration of the Large Stores Law.

7.118 According to the **United States**, a 1995 Ad Hoc Study Group Report from the JFTC's Government Regulation and Competition Policy Research Council further confirms that "some local offices of MITI have orally demanded that they [stores] lay the ground work following local rules or customs, and they have been forced into what amounts to an adjustment process due to demands from existing local retailers". According to the United States, the JFTC report found that MITI regional offices "orally demand" that new large stores consult with local retailers. The MCA survey identified several MITI regional offices or prefectural or local authorities who admitted to at least suggesting or advising large retailers to consult with local retailers. When MCA in turn asked large retailers for their experiences regarding such authorities, in some cases the retailers were able to produce pamphlets from the authorities directing large retailers to consult with local business interests.<sup>1160</sup>

7.119 **Japan** contends that the JFTC Ad Hoc Study Group Report does not substantiate the US arguments that local government entities are requiring store planners to provide prior explanations to local retailers. Like the MCA Report discussed above, the JFTC Report is limited in scope and presents no concrete example of a prior explanation or consultation offered to local retailers at the request of a government entity. Japan notes that the US citation from this Report addresses only consultations requested by local Chambers of Commerce and local retailers at the public briefing stage,

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<sup>1155</sup>Ibid., pp. 11-14.

<sup>1156</sup>See US example (iii) in para. 7.113 above.

<sup>1157</sup>See US example (vii) above.

<sup>1158</sup>See US example (ii) above.

<sup>1159</sup>See US example (iii) above.

<sup>1160</sup>Results of the Survey Regarding the Liberalization of Regulations: Application of Laws Dealing with Adjustment of Retail Business Activities in the Area of Large Scale Retail Stores, Management and Coordination Agency, October 1995, pp. 11-12, US Ex. 95-15.



subsequent to Article 3 Notifications.<sup>1161</sup> Hence, Japan argues that the JFTC Report does not document any instances of prior explanation requested by a MITI branch, a prefectural or local government.<sup>1162</sup>

7.120 The **United States** maintains that the MCA and JFTC studies indicate that such recent application of the prior consultation/adjustment requirements or recommendations are not isolated incidents, but are widely and consistently applied measures cutting across many, if not a majority of jurisdictions in Japan. In the US view, this requirement, urging or request to large stores is a law, regulation, or administrative ruling of general application within the meaning of Article X:1. The basis of the US claim under Article X:1 regarding the Large Stores Law is precisely the fact that Japan continues to require informally and non-transparently what it previously required formally.

**(d) Administrative rulings 'made effective'**

7.121 **Japan** submits that the US claims fail to meet the textual requirements of Article X:1 because it does not point to any administrative ruling of general application which has yet to be published. In particular, as the central government has either corrected or will correct local policies that deviate, these policies do not constitute general rules "made effective" by the government as required by Article X:1. Since the text of Article X:1 focuses on measures "made effective" by any [WTO Member]", it is a central government's action that determines whether or not the trade regulations within the meaning of Article X:1 have been "made effective". The only rule promulgated by Japan is that set forth in the relevant MITI circulars explicitly abolishing any prior explanation procedures and instructing MITI branches and local governments not to guide for prior explanation. In Japan's view, given that the alleged administrative guidance does not even exist, there is no administrative ruling that has been "made effective" and thus there is nothing that must be published under Article X:1.

7.122 The **United States** accepts that the term "made effective" is part of the text of Article X:1, but contends that the measures subject to US allegations under Article X are measures that have been made effective by Japan.

**(e) "Affecting the sale or distribution of imports"**

7.123 The United States notes that Article X:1 requires a Member to publish its laws, regulations, judicial decisions and administrative rulings of general application that "affect" the "sale" or "distribution" of imports. The United States contends the term "affecting", as it was intended by the drafters of Article X:1, and as it has been repeatedly applied by panels in the context of Article III, means "not only the laws and regulations which directly governed the conditions of sale or purchase but also any laws or regulations which might adversely modify the conditions of competition between the domestic and imported products on the internal market".<sup>1163</sup>

7.124 More specifically, the United States argues that Japan's measures governing the opening or expansion of large stores, i.e., the prior consultation process under the Large Stores Law, clearly affect the sale and distribution of imported photographic film within the meaning of Article X:1 because this process often results in a large store feeling compelled to make downward adjustments in its operating plans. These downward adjustments limit the scope and operation of large stores in Japan which in turn reduce the opportunity for foreign products to reach the market in Japan, given that large stores are more likely to deal in foreign products than small stores because large stores (a) have more shelf

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<sup>1161</sup>JFTC Ad Hoc Study Group Report, Concerning the Reevaluation of Government Regulations in the Distribution Sector, June 1995, p. 18, US Ex. 95-11.

<sup>1162</sup>For any governmental body to request this consultation is directly contrary to the explicit Japanese Government policy that a public briefing held after an Article 3 notification is explicitly *not* to be used as a mechanism for prior consultations with approval from local retailers. 1992 Public Briefings Circular, Japan Ex. C-17.

<sup>1163</sup>Panel on *Italian Discrimination Against Imported Agricultural Machinery*, BISD 7S/60, 64, para.12.

space to devote to multiple brands of a product, and (b) are more likely to deal directly with manufacturers, including foreign manufacturers, by-passing the wholesalers which tend not to deal in foreign film. Moreover, large stores are more likely to price lower than small retailers. According to the United States, the Japanese Government itself has concluded that large stores generally increase competition in the distribution sector in Japan and are a challenge to the exclusive distribution structures fostered by Japanese government policy. By restricting the most favourable channel for distribution and sales of imported film, Japan's restrictions on large stores "affect" the sale and distribution of film within the meaning of Article X:1. Therefore, the United States claims that Japan's failure to publish such requirements in a manner as to enable governments and traders to become acquainted with them is inconsistent with Japan's obligations under Article X:1.

7.125 **Japan** submits that the Large Stores Law, and consequently, any of its enforcement actions, including the previously existing practice of "prior explanation," do not affect the sale and distribution of film in the way alleged by the United States. Japan contends that the provisions of the Large Stores Law do not draw distinctions between imported and domestic products. Determinations whether and how to apply the law's four adjustment factors are in no way based on the origin of products carried or not carried by a large retailer. Likewise, Japan emphasizes that none of the adjustment factors has any necessary relation to decisions by large retailers as to which products to carry.

7.126 Japan also states that these general conclusions with respect to the Large Stores Law apply with added force to any alleged administrative guidance. Japan cannot conceive of any connection between whether or not large store planners must conduct "prior explanation" and competitive conditions for imported film. In Japan's view, the alleged administrative guidance does not change the competitive relationship between domestic and imported film, and therefore does not "affect" the sale and distribution of film in violation of Article X:1.

## 5. *CONCLUSIONS*

7.127 The **United States** concludes that "fair competition codes", respective enforcement actions and "prior explanation" practices have created an opaque enforcement system pursuant to the Premiums Law and have made it impossible for foreign firms and their governments to "become acquainted" with relevant procedures under the Large Stores Law. Consequently, the United States claims that Japan's Premiums Law enforcement system and continuing application of the Large Stores Law's "prior explanation" requirement are inconsistent with Japan's obligations under Article X:1.

7.128 **Japan** continues to maintain that the JFTC and MITI have published all laws, regulations and administrative rulings of general application in an appropriate form<sup>1164</sup> and Japan believes to be in full compliance with the requirement of Article X:1.

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<sup>1164</sup>Japan notes that important enforcement actions are reported in leading legal periodicals, but claims that they fall outside the scope of Article X.

## VIII. ARGUMENTS OF THIRD PARTIES

### A. THE EUROPEAN COMMUNITIES

8.1 The European Communities (EC) attaches great economic and political importance to maintaining conditions of fair and transparent market access conditions around the world. The EC is a major player in the photographic film and paper business and EC-origin products constitute from 5 percent (film) to 8 percent (photographic paper) of the Japanese market and over 20 percent of the rest of the world film market. EC companies face difficulties of access to distribution channels for imported film and paper products in Japan, whereas Japanese companies do not face any of these problems when importing Japanese origin products into Europe. The EC alleges that some measures adopted by Japan could affect the balance in the competitive opportunities between imported film and paper products and domestic film and paper products and therefore be in breach of WTO rules and in particular of Article III:4 of GATT.

8.2 The EC emphasizes that this case raises important issues including the scope and applicability of several key WTO and GATT 1994 provisions. It requires the Panel to achieve "a proper balance between rights and obligations of Members" in accordance with Article 3.3 of the DSU. In the view of the EC, the following aspects should be carefully considered:

- i. The notion of "treatment no less favourable than that accorded to domestic products", on the one hand, and the notion of "upsetting the competitive position" or of "restrictive business practices", on the other hand, cannot operate simultaneously.
- ii. The first has been consistently interpreted by different panels in the past as concerning "competitive opportunities between imported products and domestic products". The second suggests the possible violation of internal rules concerning competition between undertakings or of general domestic policies as implemented by a WTO Member.
- iii. Article III is not directed against any "impediment" or "narrowing of trade opportunities" which might affect imports of any kind but only against internal measures affecting the internal sale of imported goods "so as to afford protection to domestic production"<sup>1165</sup>. A Member's internal measure is relevant in the context of Article III only in so far as it accords treatment that is less favourable to imported than to domestic goods. In the EC's view, the Panel should be concerned with the protection of domestic production which infringes GATT and WTO rules, and not with any other general governmental measure which is aimed at limiting or regulating, at the same time and in the same way, the marketing of both domestic and imported products.<sup>1166</sup>
- iv. Some aspects of this dispute such as the effects of anti-competitive behaviour and practices, confirm the need for an international framework of competition rules within the WTO system.
- v. The dispute settlement procedures have been conceived and structured to provide "security and predictability to the multilateral trading system"<sup>1167</sup> and not to compare or harmonise different legal or economic systems applied by WTO Members. Therefore, it is

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<sup>1165</sup>Article III:1 of GATT.

<sup>1166</sup>The EC relies on panel reports on *Italian Discrimination Against Imported Agricultural Machinery*, adopted on 23 October 1958, BISD 7S/60, 65, para. 18 and on *United States - Section 337 of the Tariff Act of 1930*, adopted on 7 November 1989, BISD 36S/345, 387, para. 5.13.

<sup>1167</sup>Article 3.2 of the DSU.

paramount for a consistent analysis by the Panel that a clear and direct relation between the products whose importation is hindered and the contested governmental measures be established before any finding of an infringement of GATT rules by a Member is made.

## **1. FACTUAL ASPECTS**

8.3 The EC submits that access to the Japanese market for imported film and paper has proven to be difficult for European producers. European film and paper has not been accepted for distribution by the four leading Japanese wholesalers (*tokuyakuten*), which, due to the distribution structure of the Japanese film and paper market is a key element in market access. This has contributed to the difficulties, despite intensive efforts, for European film and photographic products to acquire a market share in Japan which corresponds to their actual overall world market share.

8.4 According to the EC, the impressive volume of information provided by the United States demonstrates that Japan, during the period from 1960 to 1975 and up to the present day, worked on strengthening the economic and financial ties between the Japanese photographic wholesalers and the Japanese producers of film and paper to the detriment of imported film and paper.

8.5 The EC can confirm that it is impossible to have adequate access to retailers in Japan if the main wholesalers (*tokuyakuten*) are out of reach. While access to small retailers and small shops is not completely barred by Japan's measures, the commercial position of the products not sold through the *tokuyakuten* is particularly weak, notably because of the lack of brand awareness of the Japanese public. In order to overcome this important commercial weakness, only strong media advertising and costly store promotions could help. However, these costs inevitably raise the already high distribution costs of overseas products, affecting therefore either the capability of attaining a reasonable profitability or to compete in price with the major competing film and paper products on that market, or both. These additional burdens do not affect domestically produced film and paper.

8.6 Against this background, the EC notes that since 1970 the Japanese Government implemented a series of actions to guide the distribution sector of Japan, and in particular the *tokuyakuten*, to strengthen the links between the domestic film and paper producers and the *tokuyakuten*. The result of this policy has been the exclusion of all imported film and paper products from the major wholesale distribution channels.

8.7 The EC notes that Japan objects to the existence of any relation between the 1970 Guidelines and the actual so-called "verticalisation" of the distribution system. According to Japan, the restructuring of the Japanese *tokuyakuten* and their reverting to the single-brand distribution mode was already on-going before that date. In Japan's view, therefore, there cannot be a causal link between the governmental action and the restructuring of the *tokuyakuten* that led to the exclusion from that distribution channel of the imported film and paper products because the effect was supposedly happening before the alleged cause.

8.8 The EC is not convinced by the Japanese rebuttal for two main reasons: *First*, for the EC it is apparent that there was, and to a certain extent there still is, an expressed worry on the side of the Japanese Government concerning the state of its internal distribution system, in particular in the film sector. Allegedly in order to streamline the internal distribution system, Japan established the Distribution Systemization Promotion Council (1970), which published its Basic Plan for the Systemization of Distribution (1971). The MITI Distribution Systemization Development Centre (1972), in executing the Basic Plan, issued the Manual for Systemization of Distribution by Industry - Camera and Film (1975). The MITI-sponsored creation of a "Natural Colour Photography Promotion Council" (1963) and the "Photosensitive Materials Committee of the Distribution Systemization Promotion Council" (1975) also responded directly to the need of representing joint government/private sector co-operation in order to formulate standardised transaction terms and narrow lines of distribution. The "Business

Reform Law" (1995) established a broad legal framework for MITI to continue its intervention to strengthen and protect domestic industry, including film and paper materials.

8.9 The EC further notes that MITI's "Guidelines for Standardisation of Transaction Terms for Photographic Film" of 1970 were substantially maintained in force in 1990. The implementation of those guidelines was monitored by the Japanese Government. Japan also provided funding through the Japan Development Bank (JDB) to domestic producers in order to support the implementation of MITI's industrial policy. The EC concludes that, against this background, it is not credible that the Japanese Government was intervening only at a time when the whole restructuring of the distribution system around the relation between the domestic producers (Fuji and Konica) and the four major *tokuyakuten* had already taken place.

8.10 *Second*, the EC argues that beyond the objective of restructuring the Japanese film and paper, and camera distribution chain towards an improved efficiency, a link was created between the four major wholesalers and the domestic film and paper producers, in particular Fuji. The result of that action, according to the EC, is clearly perceivable by the interconnection between Fuji and all four *tokuyakuten*:

- i. Fuji has a substantial equity participation in Misuzu and Kashimura (15 percent and 17.8 percent according to the latest figures). This is not a limited investment in an otherwise profitable business by a flourishing company but represents a very substantial participation in those companies. In both cases, Fuji is the largest outside owner;
- ii. Fuji is part of the Mitsui Keiretsu: this implies that a cross-shareholding is in place between the two major banks of Mitsui Group (Mitsui Trust and Sakura Bank) and Fuji. The banks are the largest Fuji shareholders and Fuji has its largest equity holding in the two Mitsui banks;
- iii. The two Mitsui financial institutions are the main banks and largest creditors of three of the four *tokuyakuten* (Misuzu and Kashimura plus Asanuma). Omiya, the fourth major distributor, is linked strongly to Fuji through both Sakura bank and Sumitomo bank, the other major shareholders of Fuji.

8.11 The EC contends that Fuji's links with the *tokuyakuten* amount to considerably more than an arms-length business relationship. The *tokuyakuten* are in a state of financial dependency from Fuji. In intervening legally, financially and by control through MITI, the Japanese Government must have been aware that the result of its action would be to upset the competitive opportunities in favour of the film and paper domestic production by preventing the imported film and paper products to have access to the most important distribution channel, the four main wholesalers.

8.12 According to the EC, it is standard practice all over the world, including in Europe, that photographic producers have one subsidiary per country representing their interests in selling their products to wholesalers, retailers, dealers or end users in dependence of the products and situation. The extraordinary situation in Japan, however, is the existence of four *tokuyakuten* distributing exclusively or close to exclusively the same products of only one company, the major domestic producer. A subsidiary of a European company in Japan is in the same situation as the Japanese producers themselves. It has to find means to enter into the market which includes the four *tokuyakuten* already serving the large majority of retailers, wholesalers etc. As long as the four major wholesalers refuse to purchase any film other than the one domestically produced by Fuji, the market access for imported film will continue to be impaired.

8.13 In the EC's view, within the framework of the potentially legitimate goal to support the restructuring of the Japanese internal distribution system while the liberalisation under the auspices

of the GATT and the WTO was under way, a less legitimate action was in fact implemented, allowing the creation of a complex structure around the main domestic film and paper producer that tied up completely the most important and profitable distribution channels in the country, which, in view of the particular distribution structure in the Japanese film and paper market, is essential. The EC concludes that the result of that action is the exclusion of imported film and paper from the best way to reach the Japanese customers and, more important, the consolidation of the domestic production which is now virtually impossible to overcome in terms of market share.

## 2. *LEGAL ASPECTS*

8.14 The EC focuses on the part that it considers to be at the heart of the present case, namely whether the Japanese Government has taken measures that afford less favourable treatment to imported products than to like domestic products in violation of Article III:4 of GATT 1994.

8.15 The EC notes that in past GATT practice the examination of violation cases has always preceded the non-violation cases. The latter are in fact used to remedy to nullification and impairment of benefits caused by the adoption of a GATT-legal measure as opposed to the violation cases where the issue is the nullification and impairment caused by a GATT-illegal measure.

8.16 Moreover, in view of the fact that film and paper are bulk products, there is no need to enter into an analysis whether or not domestic and imported film and paper are "like", since this would be the case under any of the generally accepted possible interpretations of the word "like" under Article III.

8.17 The EC has analyzed the situation in Japan concerning film and paper on the assumption that certain Japanese Government actions are measures having *de facto* a binding effect. The EC recalls the findings of the panel on *Japan - Trade in Semiconductors*:

"All these factors led the Panel to conclude that an administrative structure had been created by the Government of Japan which operated to exert the maximum pressure on the private sector to cease exporting at prices below company-specific costs. This was exercised through such measures as repeated direct requests by MITI, combined with the statutory requirement for exporters to submit information on export prices, the systematic monitoring of company and product-specific costs and export prices and the institution of the supply and demand forecasts mechanism and its utilisation in a manner to directly influence the behaviour of private companies. These measures operated furthermore strong peer pressure to comply with requests by MITI and at the same time to foster a climate of uncertainty as to the circumstances under which the exports could take place. The Panel considered that the complex of measures exhibited the rationale as well as the essential elements of a formal system of export control. The only distinction in this case was the absence of formal legally binding obligations in respect of exportation or sale for export of semi-conductors. However, the Panel concluded that this amounted to a difference in form rather than substance because the measures were operated in a manner equivalent to mandatory requirements. The Panel concluded that the complex of measures constituted a coherent system restricting the sale for export of monitored semi-conductors at prices below company-specific costs to markets other than the United States, inconsistent with Article XI.1".<sup>1168</sup>

8.18 The EC notes that Japan, based on an analysis of the different language used in Article XI and Article III, refutes the applicability of the *Semiconductors* precedent to this case. In particular,

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<sup>1168</sup> Adopted on 4 May 1988, BISD 35S/116, 157-158, para. 117.

Japan draws on the fact that Article XI:1 refers to "other measures", while Article III:4 contains the words "laws, regulations and requirements". In Japan's view, the comparison of the two texts makes it clear that the language in Article XI:1 is broader than that contained in Article III:4 and therefore the same reasoning that is found in *Semiconductors* cannot be extended *per se* to the present procedure where the complaining party should demonstrate the existence of at least "requirements" and not only "other measures".

8.19 While the EC does not disagree with the basis of the Japanese legal analysis, it cannot agree with the conclusions drawn. According to the EC, the above quotation shows that *Semiconductors* was considering not only the formality but the reality of a very peculiar system, the Japanese interconnection between government and industry. This particular situation is characterised by a significant capability of the Government to directly influence the behaviour of private companies through the traditional peer structure of the society and the strong pressure that it can produce without the need of adopting legally binding instruments. For the EC, it is striking to note the perfect parallelism, *mutatis mutandis*, between the description of Government intervention in the *Semiconductors* case quoted above and the one that occurred in the present case. The EC concludes that the actions are very similar, the monitoring activities are similar, the governmental means used are even identical (i.e., MITI structure), and the results are strikingly close.

8.20 For the EC, it is not surprising that the *Semiconductors* panel report when referring to the Japanese Government's practices instead of using the definition of "measures" reverted more specifically to the notion of "requirements". The EC is of the view that in this specific case, the reality shows that the Japanese Government's action amount to a "requirement" as defined under Article III:4 of GATT.

8.21 The EC further notes that Japan also contests the existence of these measures at present. The EC agrees that a violation claim can only be based on measures that are operating, *de facto* or *de jure*, at the time of the establishment of the Panel or are entering into effect shortly afterwards. In that regard, the EC recalls that the 1970 Guidelines for the restructuring of the distribution system have allegedly been replaced by the 1990 Guidelines and the other governmental interventions have apparently never been officially repealed. However, the EC considers that the 1990 Guidelines and their application have not had the effect to eliminate the measures concerned by this case. On the contrary, the impression is given that those measures have been confirmed and are still in place.

8.22 The EC suggests to read the terms "no less favourable treatment" in Article III as referring to the competitive opportunities but not to the actual economic impact of the measure. This implies in turn that Article III is applicable whether imports from other contracting parties were substantial, small or non-existent.<sup>1169</sup>

8.23 The EC also emphasizes that Article III:4 should not be read as affecting the distinction between trade policies and general domestic policies (e.g., competition policy, labour policy, environmental policy, monetary policy, immigration policy, consumers' protection policy, etc.), given that the former are subject to WTO rules and scrutiny while the latter are not. Nevertheless, WTO rules should be deemed to cover Member's trade laws and regulations (even when they are taken in the form of general internal measures) in cases like the present one where evidence has been provided showing that the Japanese internal policies concerning film and paper products were in fact designed to afford protection to domestic products on top and independently from their facial objective of pursuing general internal policies under their jurisdiction and thereby violate Article III:1, read in conjunction with Article III:4.

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<sup>1169</sup>Panel Report on *United States - Section 337 of the Tariff Act of 1930*, BISD 36S/345.

8.24 The EC refers to the Appellate Body Report on *Japan - Taxes on Alcoholic Beverages*<sup>1170</sup>, which addresses this issue by affirming that the "issue is how the measure in question is applied" in order to determine the existence of "protective taxation" "in the light of the particular circumstances of each case". In the EC's view, the Panel should examine whether:

- i. In the particular circumstances of this case there is a less favourable treatment of imported products when compared to domestic products;
- ii. there is a governmental requirement (measure) creating such less favourable treatment;
- iii. the measure is applied in such a way as to create distortions in the conditions of competition between domestic and imported like products;
- iv. there is a direct causal link between the application of that measure to those specific products under those specific circumstances and the distortion in the conditions of competition between domestic and imported products. By contrast, a simple side-effect resulting from the implementation of a general measure pursuing a general internal policy, and which affects the conditions of competition, should not be considered to infringe Article III:4 unless a clear evidence is provided that this general policy measure was designed to afford protection to domestic products.

8.25 The EC, therefore, argues that, based on the relevant facts, it appears that the "objective intent" of Japan's action was to afford protection to domestic film and paper through the creation of a complex structure that is the result of the systemization aimed at preventing imported film and paper from benefitting from the major and most profitable distribution channels in the country. The Japanese Government could not ignore that by acting in that particular way it would objectively create a system which apparently is still in place due to the persistent pressure exerted by the Government through MITI.

8.26 However, the EC does not agree to any interpretation of the "protectionist intent" purely on the basis of an assessment of the political views expressed in a particular country to achieve a political result ("subjective intent"). Apart from the almost impossible task of determining the real intentions of the legislator in countries where the legislative power is constitutionally not submitted to any obligation of explicit motivation, a legislative measure can be implemented for many years and be applied in a manner which has only a remote link with the initial intent of the legislator.

8.27 The EC concludes that the evidence before the Panel demonstrates that a number of Japanese Government measures were adopted with the objective intent to afford protection to domestically produced film and paper and, therefore, that a violation of Article III:4 has been committed. The EC believes that a *prima facie* case has been objectively demonstrated by the United States and, therefore, that under the current Panel practice in the WTO, the burden of proof to show the contrary has shifted to Japan. The EC is not convinced by arguments put forward by Japan that the alleged violation does not exist. A violation of a WTO provision amounts *per se* to a presumption of a nullification and impairment of rights and benefits accruing under those agreements<sup>1171</sup>. Therefore, the EC sees no reason to enter into any development of the non-violation claims case raised by the United States.

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<sup>1170</sup> Adopted on 1 November 1996, WT/DS8/AB/R, WT/DS10/AB/R and WT/DS11/AB/R.

<sup>1171</sup> Article 8 of the DSU.



### 3. ARGUMENTS IN REPLY BY JAPAN

8.28 In response to the EC third party submission, Japan contests that the alleged connection between Fuji and its primary wholesalers amounts to "considerably more than an arms-length business relationship" and that this amounts to an Article III violation. Japan argues that even if one were to assume that the primary wholesalers were subsidiaries of Fuji, the fact remains that imported film is not prohibited from using the same type and the same level of distribution channels. All other film manufacturers - both foreign and domestic - sell through their own single-brand primary wholesalers.

8.29 Japan claims that of all the major film manufacturers selling in the Japanese market, the link between Fuji and its primary wholesalers is the weakest. Kodak and Konica each sell through their wholly-owned subsidiaries. Fuji's primary wholesalers are independent companies and are not even under contractual obligation to deal exclusively with Fuji.<sup>1172</sup> In Japan, foreign manufacturers are at least free to make an offer to Fuji's primary wholesalers, or even to acquire one or more of the wholesalers. However, for Japan it is inconceivable that in the United States any Japanese manufacturer could utilize Kodak's internal sales staff that handle the direct-to-retailer sales, the functional counterpart to the primary wholesalers that sell to retail customers. Japan also points out that a major part of Kodak's "distribution channel" is based on exclusive relationships between Kodak and retailers.<sup>1173</sup>

8.30 According to Japan, the EC acknowledges that single-brand distribution is the "standard practice all over the world, including in Europe". Nevertheless, the EC notes that in most countries manufacturers sell through a single subsidiary but that in Japan Fuji sells through four primary wholesalers. While Japan accepts this distinction is factually true, it considers it as logically irrelevant because selling through four wholesalers simply preserves the benefits of intra-brand competition.<sup>1174</sup> Japan argues that other manufacturers made a business decision to merge the wholesalers they acquired into single entities, whereas Fuji made a different business decision.

8.31 In Japan's view, the EC appears to argue that four independent primary wholesalers should not be allowed to maintain single-brand relationships with Fuji, and that the government measures are somehow responsible for this. Japan points out, however, that the EC provides no evidence of any government measures that either created the relationship between Fuji and its primary wholesalers or which prevent other manufacturers from developing a relationship with one or more of those primary wholesalers.

8.32 According to Japan, the EC overlooks a public statement made by Agfa emphasizing the difficulty it faces in both the United States and Japanese markets, due to its position as a new entrant facing well-established rivals: "It cannot be disputed that the photomarkets in the United States, as well as Japan, are dominated by their respective domestic companies. This means considerable barriers for outsiders such as ourselves". Japan underscores that there is nothing unusual about the Japanese market and that new entrants always face obstacles becoming established in a market.<sup>1175</sup>

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<sup>1172</sup>Japan indicates that some of Fuji's primary wholesalers handle Kodak's products other than film.

<sup>1173</sup>Japan notes that Kodak also uses a variety of techniques, including cash payments, to ensure retail exclusivity.

<sup>1174</sup>Japan emphasizes that intra-brand competition may actually reduce Fujifilm's effectiveness as an interbrand competitor. As a result, Fujifilm's use of multiple wholesalers could actually benefit competing manufacturers like Kodak. W. Kip Viscusi, John M. Vernon, Joseph E. Harrington, Jr., *Economics of Regulation and Antitrust*, 1992, p. 237, noting that reduced *intra-brand* competition could make a manufacturer a more effective *interbrand* competitor, Japan Ex. F-8; see generally, E. Thomas Sullivan, Jeffrey L. Harrison, *Understanding Antitrust and its Economic Implications*, 1988, pp. 147-177, Japan Ex. F-9, discussing the free rider problems caused by intra-brand competition.

<sup>1175</sup>A public statement made by Agfa, Film Dispute Before the WTO, October 17, 1996, Japan Ex. F-10.

**B. MEXICO**

8.33 Mexico states that this particular case deals with the relationship between the measures introduced by the Japanese Government and access to its market for imports of photographic paper and film.

8.34 According to Mexico, three types of measures which the Japanese Government has implemented since the 1960's have affected access of imports to Japan:

- (a) measures that impede the distribution of imported photographic film and paper;
- (b) measures that limit the establishment of large retail stores, which constitute an alternative system for the distribution of such imports;
- (c) measures involving the imposition of restrictions on sales-price and advertising campaigns for such products.

8.35 With regard to the *distribution* of imported photographic paper and film, the Japanese Government adopted a number of measures through MITI's fostering the integration of manufacturers and distributors at the end of the 1960's and beginning of the 1970's. Japan promoted the adoption of common transaction terms between all manufacturers and distributors, which encourage their integration. These terms relate to discounts, rebates and payment terms applicable to distributors, for imported goods as well.

8.36 At the same time steps were taken to promote the use by manufacturers and distributors of shared infrastructure, e.g. warehouses and distribution routes, thereby strengthening their ties. This was achieved, inter alia, through subsidized financing of photographic laboratories, from which those laboratories in which there was foreign participation were excluded.

8.37 Moreover, efforts were made to strengthen information links between domestic manufacturers and distributors through government agencies. This integration has affected the access of imports of such goods to the Japanese market.

8.38 With respect to *large retail stores*, Mexico notes that a law was enacted in 1973 permitting MITI to limit the establishment, operation and expansion of such stores in order to protect small business. Notwithstanding its general character, this law has affected access of imports by restricting an alternative channel for the distribution of photographic paper and film.

8.39 Finally, as regards measures relating to *promotions*, Mexico notes that, on the basis of the Anti-Monopoly Law of 1947 and the Premiums Law of 1962, the Japanese authorities, starting at the end of 1960's, imposed limitations on discounts and advertising by large- and small-scale distributors of photographic paper and film. These limitations affected the access of imported goods.

8.40 Mexico emphasizes that tariff reduction, national treatment and non-discrimination are fundamental to the achievement of the WTO's objectives. Accordingly, the continued consistency of any measures adopted by WTO Members has to be ensured, in particular with:

- (a) Article III which stipulates that products imported from a Member country shall be accorded treatment no less favourable than that accorded to domestic products;
- (b) Article XXIII which establishes the legal safety that must be a feature of any advantage enjoyed by a Member as a direct or indirect result of GATT 1994;

(c) Article X which provides that all provisions of general application shall be brought to the knowledge of both governments and traders.

8.41 Finally, Mexico requests the Panel to:

- (i) conduct its examination in keeping with the terms of reference established by the DSB;
- (ii) base its findings and recommendations on such relevant provisions of the covered Agreement as have been invoked by the parties to the dispute;
- (iii) avoid the creation of new disciplines through interpretations that could go further than what was agreed by the Members of the WTO; and
- (iv) ensure full implementation of the concessions under the terms and conditions in which they were agreed and in conformity with the relevant provisions of the WTO.