



Memo

Re: Response to queries from OECD on regulatory reform in Japan

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Casey Sedgman,

Policy Director,

European Business Community in Japan (EBC) ^{1[1]}

sedgman@ebc-jp.com

1. To what extent do domestic commercial interests consider that the current programme of regulatory reform has enhanced competition in the domestic market? What evidence is there that the current programme of reform has enhanced foreign competition within the Japanese market?

Mixed results. In areas such as retailing (revisions to the big store law), telecommunications (revisions throughout the 1990s to the Telecommunications Law), and insurance (revisions in the mid-1990s to the Insurance Business Law) regulatory reform (coupled with changing market dynamics) has resulted in an increase in new foreign entrants to the market (e.g. Retail: Carrefour, Toys R Us, Walmart, IKEA; Telecoms: Vodafone, C&W; Insurance: ING Life, PCA Life, AXA Life, Hartford Life, Manulife). In a number of other areas such as medical services, companies are still prevented by law from engaging in commercial activity.

In general, however, the EBC feels that the regulatory reform programme in Japan has not gone far enough to create an open environment for trade and investment.

^{1[1]} The European Business Community is the trade policy arm of the combined European national Chambers of Commerce in Japan.

2. What major problems persist?

At a broad structural level, the main problem with Japanese regulatory policy is the general attitude of the government officials, an attitude which still favours micro-regulation over macro-supervision. This point was noted in the OECD report on regulatory reform in Japan published in 1999, and remains valid five years on.

Another issue of long standing structural concern is the lack of transparency of the regulatory process. It is difficult to receive binding, written clarification from authorities in Japan regarding issues of regulatory concern. A lack of transparency creates uncertainty, and this makes business planning difficult. This is one of the factors most frequently cited by European businesses as inhibiting the development of a truly open environment for trade and investment in Japan.

The GOJ implicitly acknowledged this problem with the introduction of the Japanese “No-Action Letter” system in March 2001. The “No-Action Letter” system was a welcome development, but has suffered from the following constraints: a) replies are not considered legally binding, b) oral replies are in some cases still allowed, c) the ministries have not actively encouraged its use, and d) as a result very few no-action letters have actually been issued in areas that need it the most.

More disturbing, however, is the general attitude of the regulatory authorities towards transparency and clarity in their respective regulatory jurisdictions. Regulators should be proactively seeking out areas that need clarification, and this is still not happening. Many firms continue to report receiving replies from regulators (especially concerning financial services and taxation) to the effect of “just try it and see what happens”. This is unacceptable.

As a matter of standard practice, regulators should reply in writing to all requests for clarification from private firms, be it within the framework of the Japanese no-action letter system, or not. Despite numerous policy initiatives designed to eliminate the practice, oral replies remain the norm in Japan.

This has created somewhat of a double standard, especially in the financial services sector: on the one hand, the regulator requires firms to maintain a clear written relationship with their clients (in the interest of consumer protection), while on the other, they do not afford this same courtesy to the firms that they regulate.

At a sectoral level, the EBC would like to see the regulatory reform program strengthened to eliminate the numerous barriers on trade and investment that persist in Japan.

Examples include:

- Firewalls on wholesale banking operations at a time when such firewalls are being eliminated on the retail side;
- Plant quarantine regulations that do not make a practical distinction between harmful and non-harmful organisms;
- Pricing and distribution regulations on international airfares that inhibit the development of direct (transparent) sales to consumers, contrary to practice in nearly all countries worldwide;
- Continued requirement for national assays for animal-use vaccines and diagnostics, despite the elimination of such requirements for human-use products; and
- Food additive regulations that are out of step with the rest of the industrialized world.

(For a more detailed analysis of specific sectors, please refer to the EBC publication “Promoting Foreign Investment Through Decisive Reform: The EBC Report on the Japanese Business Environment 2003”)

3. How does the Japanese business community view current efforts by the government to double FDI into Japan?

The EBC appreciates the apparent new-found enthusiasm by the Japanese Government to promote foreign investment, but is wary of Japan's ability to attract significant amounts of foreign investment given the poor investment fundamentals of the Japanese market. The creation of the “one-stop shop” for investors and other promotion activities are definitely a step in the right direction (Japan never really had a comprehensive investment strategy in the past), but Japan's high cost structure and relatively saturated market makes Japan a difficult sell when compared to its more dynamic neighbours.

The EBC has been arguing that it will take more than fancy brochures to lure foreign investors to Japan. Recommendations include:

1. Continued efforts to promote Japan to the foreign business community, not only through PR activities, but also through decisive action on the part of the government to show that it is serious about attracting foreign investment. Recent decisions to allow Japan Post's insurance business to expand its operations, decisions to reform the Corporate Enterprise Tax placing more tax burden on new entities, and decisions to reduce reimbursement prices for medical products is not sending the right sort of message to the rest of the world.
2. Display strong leadership to dispel the myths of FDI, such as the fallacy that all foreigners want to do is take over Japanese companies and sell off the pieces (truth: foreign firms, even so called "vulture funds", are more interested in making a go of it than destroying something that already exists. In fact, FDI leads to the opposite: more jobs, more inflows of capital, more productivity) and that FDI has no benefits for the rural areas of Japan (truth: Foreign firms employ most of their workers outside of the major centres) (Note: The ACCJ has produced an excellent report about the "myths" of FDI)
3. Continue to promote deregulation, especially in areas such as health service provision where there is the potential for substantial investment from the private sector.
4. Make more of an effort to privatise public enterprises and outsource to the public sector - not just posts and hiways, but also water service provision, sewage, waste management, and welfare facilities. PPP/PFI has yet to catch on on Japan.
5. Make it easier to do cross border M&A: The vast majority of FDI is in the form of M&A, which is just as productive as greenfield investment. The Ministry of Finance must be convinced to give the same tax treatment to cross border mergers as for wholly Japanese mergers, and the commercial code and other company laws should be amended to facilitate corporate restructuring.
6. More decentralization to give local governments more tools to attract investment, be it through tax incentives, regulatory incentives, etc.

It should be noted that these are more or less the same sort of recommendations made by the Government's own Japan Investment Council.

4. How does the Japanese business community view the efficiency of the Office of the Trade Ombudsman (OTO)? Has its effectiveness changed since it has moved into the Cabinet Office?

It is difficult for the EBC to make an authoritative comment on this, as our experience

with the OTO is limited. The EBC has been involved in only two cases before the OTO. However, both ended in positive outcomes.

5. How do the views of the Japanese business community enter into the regulatory reform process? Could any examples of ways in which Japanese business community participation has significantly contributed to the regulatory reform process be shared? How can consultation be improved?

There are many ways in which businesses, including foreign-affiliates, are able to participate in the regulatory reform process. Important venues include:

- The Council on Regulatory Reform, which produces an annual set of regulatory reform recommendations that provide the basis for the Government of Japan's regulatory reform program. Companies are encouraged to provide input into the Council's deliberations. The EBC usually provides input into this process through the EU's bilateral regulatory reform dialogue with Japan.
- Bilateral business dialogues, such as the EU-Japan Business Dialogue Roundtable, which has a significant regulatory component.
- The new "special deregulation" zone system, where companies are free to make suggestions on specific deregulation measures in a specific locale.
- The Office of the Trade Ombudsman.
- Directly to politicians and regulators. In the experience of the EBC, both groups are usually willing to meet and discuss issues of regulatory concern (... not that this always translates into action!)
- Through the media.

The EBC, for example, was, through the OTO process, able to force a change in Government policy vis-à-vis the regulation of product approvals for in-vitro diagnostics in Japan. Another recent success, achieved in cooperation with various foreign governments and business organizations, has been the recent decision to allow for full partnerships between Japanese and foreign lawyers.

Unfortunately, while on the face of things the process appears transparent and open to debate, the reality is that most regulation is still developed behind closed doors on an ad hoc basis by the ministries involved in consultation with the main players in the market. The much-vaunted "public comments" process is not much of a public comments process

at all: the public is rarely given any meaningful opportunity to provide input into new legislative proposals. The “no-action letter” system suffers from similar criticisms.

The EBC recommends a much more “proactive” as compared to the current “reactive” approach towards regulatory policy in Japan. Consultation on regulation (in fact, on economic policy in general) needs to start much earlier in the process. The EBC recommends that:

- a) Each ministry and/or regulatory body publish an annual management plan that gives consumer groups and the industry advance notice of consultation on issues that may affect them;
- b) Issue a consultation document setting out preliminary proposals on particular issues to draw in the views of the industry and the public. Consultation should take the form of an initial period for comments followed by a second stage of comments on the views expressed in the first round. All responses, other than those restricted on the grounds of commercial confidentiality, should be made available on the Internet;
- c) Allow sufficient time for responding – current timeframes are too short in Japan (particularly for foreign companies given the need for translation). A minimum of 6 weeks should be allowed, although most developed countries typically allow longer; and
- d) Issue a statement setting out the results of the consultation process, responding to points made in the consultation process, and giving full details reasons for decisions.

6. What are the views of the Japanese business on the process of regulatory reform in the area of standards and conformity assessment? With regard to progress in the area of Suppliers Declaration of Conformity (SDoC)?

As mentioned above, the EBC feels that Japan still has a long ways to go with regards to moving away from a micro-management “ex-ante” regulatory structure to a macro-supervisory “ex-post” system. The application of GMP is not as advanced in Japan in some sectors as it is in North America or in Europe.

By way of example, the EBC has for many years been asking the Japanese Government

to remove regulations that require a national assay for animal-use vaccines and diagnostics, a requirement that does not exist for similar products intended for human-use in Japan. The ministry involved, however, is wary about ceding authority over conformity assessment to the manufacturers themselves, a situation complicated by the fact that government approval institutions are run by ex-ministry officials.

With regards to SDoC in particular, SDoC for telecommunications equipment has been introduced into Japan as of January 1, 2004. The EBC supports the general principles of this system, which is similar in outlook to the one that exists in Europe.

However, SDoC as has been adopted in Japan differs in substance from the one that has been adopted in Europe.

Japanese SDoC only allows for 8 type of Radio Equipment:

1. Cordless Telephone
2. TDMA Terminal
3. CDMA Terminal
4. DS-CDMA Terminal
5. MC-TDMA Terminal
6. T-CDMA Terminal
7. Digital Cordless Telephone
8. PHS Terminal

In addition, the Japanese SDoC system requires that companies apply to the Japanese Government (MPHPT) for a Certification Number, which needs to be printed on the label marked on the radio equipment. This defeats the original purpose of the reform. European SDoC does not require this.

7. Is there any evidence of reciprocity in the treatment of regulations by Japan vis-à-vis European countries, in the form of parallel relaxations or parallel tightening?

Depends on the issue area. In areas where the EU has taken a very activist regulatory stance (e.g. chemicals, feed additives), Japan generally has not followed. In other areas, such as in the regulatory environment governing the approval of new human-use pharmaceuticals, a certain amount of convergence has occurred.

The EBC welcomed the introduction of the Mutual Recognition Agreement between the EU and Japan with regards to GLP for chemicals, GMP for pharmaceuticals, telecommunications terminal equipment and electrical equipment, signed in April 2001. Implementation, however, has not been smooth.