The WTO Dispute Settlement Process and the De-Regulation of Japan's Retail Sector

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I: Introduction

Since the first Westerner set foot upon its shores, Japan has grappled with the conundrum of deciding the extent to which it should open itself up to international trade. For over 250 years under the Tokugawa Shogunate (1600-1867) Japan was effectively closed off from the rest of the world. When Commodore Perry of the United States Navy arrived off the coast of Japan in his "black ships" in July 1853, his mission was to seek trade terms with one of the world's few remaining closed markets, not to wrest political control from the government of the day.[1] The very real concern among Japan's leaders at the time was that opening up to foreign commerce would lead, as it had in many other nations, to a dilution of political power and control by colonial masters. Perry's mission was to signify a rejoining of the battle for access to the Japanese domestic market that Western powers, and the United States in particular, have actively pursued ever since.[2]

Japan's barriers to foreign trade fall into five basic categories: formal, regulatory, strategic, business and cultural.[3] Often condemned over the years as the "bad boy of the Japanese economy", the Japanese distribution sector has been protected by barriers in all five categories. The sector has been described as the largest difference between the way Japan and the United States do business,[4] and one regime in particular, the Large-scale Retail Store Law ("LSRSL"), has come in for constant criticism as a clear-cut example of all that was "bad" with the Japanese model. The effect of the law, the domestic and foreign pressure that caused it to be abolished, and the regime that replaced it is the focus of this article.

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1 Schweitzer, "Flash of the Titans: A Picture of Section 301 in the Dispute between Kodak and Fuji and a View of Toward Dismantling Anticompetitive Practice in the Japanese Distribution System" (1996) 11 Am U J Int'l L & Pol'y 847, 856-857.

2 Excluding the period immediately prior to and during World War II.

3 Thatcher, "Section 301 of the Trade Act 1974: Its Utility Against Alleged Unfair Trade Practice by the Japanese Government" (1987) 81 NW J Int'l L & Bus 492, 495.

4 Zimmerman, "How to Do Business with the Japanese: A Strategy for Success" (1985) 134-140, in Yanagida et al (eds), Law and Investment in Japan: Cases and materials (1994) 104.

II: Japanese Distribution Sector Regulation

1. Overview

In stark contrast to the common view of a sharp and innovative Japanese manufacturing sector, the distribution sector is viewed as an obsolete profit devourer.

Empirical analysis of the Japanese distribution sector over the past 40 years shows that there has been only a gradual evolution from post-war manufacturer-dominated distribution to a retailer-controlled system. By contrast, data suggests that the United States has had a retailer-controlled distribution system for the best part of a century.[5] In the early 1980s, the average number of retail stores per capita in Japan was about three times that of other industrialised countries[6] while the value-added per employee also remained comparatively low. All these facts led to the general view, from a United States perspective, that the Japanese system was "woefully inefficient".[7]

Critics have focused most of their blame for this inefficiency on the existence of the "keiretsu".[8] These sometimes informal networks appeared to exclude competitor products from their distribution systems by controlling manufactured products from the parts production stage through to retail. While the Japanese economic culture is one that encourages stability through affiliation, it would be wrong to consider the *keiretsu* as accounting for all distribution in Japan. It must also be recognized that distribution systems in Japan, as in other countries, will depend on the individual product being distributed. In some cases, even within a single industry, the distribution channels may be completely dissimilar from firm to firm.[9]

One way to solve some of Japan's distribution inefficiency woes, analysts argued, was to remove the regulatory legislative regimes that restricted competition and were a fetter on the free market. To many, both domestically and internationally, the epitome of such legislation was the LSRSL, which imposed heavy burdens on prospective large scale retailers and protected the smaller, less efficient, owner-operator stores.

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5 Nishimura, Tachibana and Tsubouchi "Evolution of Japanese Distribution", in Miwa, Nishimura & Ramseyer (eds), Distribution in Japan (2002) 33.

6 1987/88 OECD Economic Surveys: Japan, OECD, (1989), 80.

7 Upham, "Privatizing Regulation: The Implementation of the Large-scale Retail Stores Law" in Allinson & Sone (eds), Political Dynamics in Contemporary Japan (1993) 265.

8 Post-war Japan developed and expanded on a manufacturer-oriented distribution system. Most of the retail market had been destroyed by the war, and the rapidly rebuilding manufacturing industry was stretched to find retail outlets equipped to handle and service the goods being produced. The upshot of this was that, by necessity, larger manufacturers had to form distribution channels where they supported the wholesalers and retailers with training, expansion costs and marketing. In return, manufacturers gained loyal committed distributors. The resulting distribution channel is known commonly as "keiretsu".

9 In the automobile industry, for example, Toyota sells through multi-outlet dealerships; Honda generally has one outlet per dealer. In the cosmetics industry, some firms sell direct door-to-door; others sell through retail outlets.

2. The Large-Scale Retail Store Law

Enacted in 1974, the LSRSL was the fourth reincarnation of the Department Stores Law ("DSL") of 1937. The initial Act was introduced originally out of consideration for small owner-operator stores. Small stores were struggling to compete with larger stores that had diversified their product base during the Depression in order to stay viable. The Law regulated the construction of new stores and limited the effect of the newly formed Association of Department Store Owners.

Domestic criticism of the legislation has revolved around the concern that competition was being stifled, and that the regime was effectively encouraging the creation of voluntary cartels and supporting the *keiretsu* structure.

From a foreign retailer's standpoint, there were two arguments behind a desire to have the LSRSL removed. First, as large stores are more likely to sell imported products, the sustaining of *keiretsu*-like cartels by the LSRSL regime was preventing foreign products from gaining a foothold in the market because a new entrant could not take advantage of the majority of medium to large-scale retail outlets already open.

Detractors of this theory argue that it ignores the fact that domestically-owned large-scale retail stores have been opened throughout Japan, and that foreign firms were just as able to follow the same method that any number of Japanese entrants to the market have, and build a network of their own stores. Furthermore, some analysts argue, any claim that the distribution sector in Japan is a cause of exclusion of foreign firms and products can be negated by the fact that there is no one exclusive distribution technique.[10] Rather, there are a wide variety of techniques that can be utilised by any company wishing to distribute their products in the Japanese market.

The second argument that foreign retailers have given was that there was a lack of transparency surrounding the application of the Law. As will be seen in the section detailing the regulations and guidance that supported the LSRSL regime, a positive relationship with both local government and the Ministry of Economy, Trade and Industry ("METI")[11] was essential to advance one's application for opening a new store. A hypothetical foreign company that lacked an understanding of the Japanese business culture, or worse yet, tried to introduce their own business cultures to the market was likely to be conceived of as "disturbing calm waters". Under such conceptions, building the necessary relationship with Japanese officials was likely to be almost impossible. Even if a foreign firm spent the considerable amount of time and money that was needed to actually build such a relationship, once they had opened their store, the offsetting of such set-up costs would necessarily have to be shifted to shelf prices. The

10 Nishimura, Tachibana and Tsubouchi, supra note 5, 6.

11 Prior to 1999, the Ministry of Economy, Trade and Industry (METI) was known as the Ministry of International Trade and Industry (MITI).

obvious result of this being that the company would lose any comparative price advantage it may have had over inefficient domestic rivals. The barriers to entry were hence weighted more heavily against foreign retailers than domestic firms.

3. History of the Large-Scale Retail Store Law

After the war, the Allied Occupation Command had the Department Store Law repealed, but it was reinstated in 1956 after the Japanese government regained autonomy and the economy was on the way to recovery.

Despite the Department Stores Act, the 1960s was a period of substantial growth for the Japanese economy. The retail sector as a whole, and large-scale stores in particular, were able to expand by adopting ingenious plans to circumvent the legislation. The major player in this period was the "super-store", a kind of pseudo-department store, selling grocery items on one floor and other merchandise on another. The business was organized so that each floor was a separate legal entity with a floor space under 1500 square metres. By doing this the stores fell outside the ambit of the Department Stores Act, which applied only to stores which sold a variety of merchandise on floor space of over 1500 square metres.

The extraordinary success of the "super-stores" caused them to become the focus of not only small retailer, but also traditional department store, opposition. Eventually, their success, coupled with the moves internationally for more trade liberalization, caused enough political pressure to force the Government to convince METI of the need for a more controlled distribution system. In 1973, METI proposed major changes to the legislation, based around the introduction of a notification process for new store openings.[12] When the DSL was replaced by the LSRSL in 1974, the new legislation faced opposition almost immediately from small retailers, concerned that the removal of the licensing process, requiring local retailer approval under the Department Stores Act, might make them worse off. METI managed to console this opposition by introducing a compromise. During the consultation stage previous to the law being passed, METI added the requirement of prior inspection by the Ministry which took into account the "advice" of interested parties.

Contrary to the expectations of the Government, METI, and the small-store retailers, rather than slow the number of large-scale retail store openings, the pace of construction increased quite dramatically under the LSRSL. The number of large-scale stores nationally doubled within six years of the law passing.[13]

Reaction to this state of affairs came in two forms. First, local governments at both prefectural and municipal level began to introduce regulations covering medium-scale stores not covered by the LSRSL. Second, at national level, intense

12 METI Report (1972), 82-4.
13 Nishimura, Tachibana and Tsubouchi, supra note 5, 122.

political pressure on the ruling Liberal Democratic Party ("LDP") led to the Diet instructing METI to investigate amending the law so as to integrate local and national regulation.[14]

After only five years the law was amended. The main provisions of the amended law, which came into force in 1979, are set out below.

(a) Purpose

To protect the interest of the consumer and secure the business opportunities of nearby smaller retailers by controlling the business activities of large-scale retail stores.

(b) Size of Stores Controlled

Stores were divided into two types. Type One stores were those with a retail floor space of 1,500 square metres (or 3,000 square metres in larger metropolitan areas). Type Two stores were those over 500 square metres. Type Two stores were made subject to the Act in 1979 but, in contrast to Type One stores, only had to report opening or expansion to the Prefectural Governor, whereas Type One stores had to report directly to the Ministry of International Trade and Industry ("MITI").

(c) Notification

A person wishing to construct a large-scale retail building had to send a report to METI (Type One) or the Governor (Type Two), who then contacted the local retailers and issued a public notice. A minimum of seven months was required between the issuing of the public notice and the store opening.

Any entity planning to operate within the proposed new store was required to report to METI (Type One) or the Governor (Type Two) details of the type of store it was to be and the history of company operating it. This report was required at least five months prior to opening.

(d) Inspection of Plans

After an inspection by the Large-scale Retail Store Council ("LSRSC"), a body set up by the METI to determine whether a large-scale store proposal would have adverse affects on local retailers, the METI or the Governor could advise the company planning the store to postpone its opening until recognized problems

14 A survey in the Nikkei Marketing Journal (1977) showed 33 municipalities had devised their own regulations.

were cleared up, or to reduce the floor space.[15] Advice had to take place within four months of the notification.

(e) The Large-scale Retail Store Council

The Council was made up mainly of academics, and it was obliged to take into account opinions from the local Chamber of Commerce and Industry ("CCI") and any other interested parties. The local CCI was in turn required to establish a Commercial Activity Adjustment Council ("CAAC") of local retailers, consumers and scholars to come up with recommendations regarding issues such as opening dates and times and store size. The deliberation period for this council was set at three weeks. The position of the CAAC, in effect, determined the position of the local CCI, which then stated its position to the LSRSC.

Theoretically, on the face of these provisions, it was possible for a large-scale retail store to open its doors seven months after the notice of construction. Actual periods for store openings, according to some companies, could take several years.[16]

III: Criticism of Distribution Sector Regulation

1. Domestic Criticism of the Large Scale Retail Store Law

Domestic criticism of the LSRSL focussed on six significant concerns. The first major problem arising from the law could be found in the introduction to the Act. The Law had three stated, and ostensibly contradictory, aims. The legislation sought to achieve consumer protection while securing business opportunities for small retailers, and balance the interests of *all* retailers. While these may be admirable aspirations, together they are patently unattainable.

Second, the make up of the CAAC meant that political and social pressures could easily affect the Council's recommendations. Indeed, in some cases, local businesses with vested interests were often directly involved in decisions that curbed the ambitions of large-scale store planners.[17]

Third, as the CAAC was set up by the local CCI, new store openings were regulated by parties representing very small areas such as towns or city suburbs, adding to the danger that private interests were getting in the way of larger public and consumer interests.

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15 Should the advice be ignored, METI was able to order compliance, but this condition was never tested. It seems the existence of the provision alone was sufficient to induce acquiescence.

16 According to one survey done by The Daily Yomiuri Newspaper, the longest application to be completed was one by Nichii Co which took 12 years and 8 months. The Daily Yomiuri, April 6, 1990.

17 Nishimura, Tachibana and Tsubouchi, supra note 5, 130.

Fourth, METI had succumbed to political pressure and introduced a further informal institution, known as the Prior Commercial Activity Adjustment Council ("PCAAC") to the process. The role of the PCAAC was to make inspections after notification, and before application, to ascertain any possible problems that may be faced by advancing to the application phase.

Fifth, "administrative guidance" by METI over who could build what type and size of store in which place continued right through the 1980s, causing the system to increasingly lack transparency.[18] Over the four year period immediately after the introduction of the 1979 amendment, the number of store openings decreased dramatically. While some of this may be put down to a slow-down in the Japanese economy and a shift to more conservative growth plans by retail companies, one can speculate that METI's administrative guidance control over new openings was also a large factor.

Finally, the various forms of guidance METI exercised in the control of LSRSL regulation were invariably complex and unclear. Specifying certain municipalities as requiring more regulation than others, without actually publishing which areas had been so designated, was just one of the rules to which third parties wishing to obtain consent were not privy. This lack of transparency not only acted as a barrier to companies wishing to enter the market, but also served to deny any consumer interests that may have existed, and unequivocally aided the interests of large-scale stores already in the area. As one Japanese analyst states, the rules discernibly lessened competition and "violated the basic principles of a free market economy".[19]

The concerns of some supporters of the status quo were in many respects far less noble than the many small store retailers who were, after all, dependant on the law to maintain their livelihoods. The cartel effect of the LSRSL meant that many large retailers were quite content with the barriers to entry that surrounded their fiefdoms. Some of the comments from Japan's retail barons highlight the hypocrisy that surrounded their support. Isao Nakauchi, President of Japan's largest super store chain '*Daiei*' was quoted as saying:[20]

> I approve [of retail liberalization] in both general theory and in the particulars. It is, however, not necessary to repeal the Large-scale Retail Store Law. That would be unacceptable – before you knew it, there would be a Sears opening next door! It would be fine if the Commercial Activities Adjustment Council would just discuss matters correctly. Not even getting a foot in the door is inappropriate, but if it was done according to the language of the statute, it would be fine.

18 Ibid 126-127.
19 Ibid 139.
20 Upham, supra note 7, 282.

2. Preferential Taxation

Any review of the regime would be incomplete without acknowledging the fact that the LSRSL was not the only factor affecting the continued existence of small-scale owner-operator retail stores. The Japanese tax system provides several loopholes that advantage small stores. Ambiguity between household consumption and business capital expenses, in addition to the possibility of under-reporting sales revenues, allow small store owners to avoid tax by declaring less business income. When added up, a number of tax provisions have produced fairly substantial exit barriers for owner-operators wishing to leave the market. While inherited land used for retail stores has allowed a taxpayer a deduction twice that allowed for residential land, capital gains realized by selling land in Japan have consistently been heavily taxed.

3. Domestic Pressure for Change

Four important shifts in the domestic perspective during the 1980s added to the political pressure for change to the distribution sector. First, more and more Japanese had experienced overseas travel, and were realizing that there was a huge discrepancy between the prices they were paying overseas and at home for fundamentally the same goods. Second, new modes of direct importing were developed that competed with the traditional "*sogo-shosha*" trading companies, creating large differences in the price being paid for essentially the same item at different stores. Third, many major Japanese manufacturers began to produce their products overseas and then import them back into Japan for sale at significantly decreased prices. Finally, retailers were beginning to use their customer preference information advantage to develop their own products and designs, squeezing out the wholesaler margins.[21]

In early 1989, Japan's Fair Trade Commission ("JFTC") came out with a report on the distribution sector that centred on the effects of the LSRSL.[22] The report distinguished six areas of the regime that were a hindrance to fair trade:

1. The law encouraged large retailers and local shop owners to engage in bargaining sessions, and the concerns of other interested parties such as consumer groups and scholars of city planning were basically ignored.
2. The law did not stipulate a *maximum* period of time for extracting consent from local merchants.
3. Some local communities actually solicited large donations from retailers in order to finance local projects.

21 Ibid 267.
22 Editorial, Nihon Keizai Shinbun (Japan Economic Journal), March 25, 1989.

4. Even minor operational changes to a large-scale store that may have been necessary for marketing efficiency were extremely difficult and expensive to make after opening. Each proposed change was required to be put through the same notification process as for new store openings.
5. Local bodies were regulating the opening of stores much smaller in size than the floor space regulated by the Act.
6. METI had had discussions with the major retailing firms,[23] "asking" them to restrict the number of stores they opened in certain municipalities.

The JFTC found that the law had not only undeniably led to higher than necessary consumer prices, but that it had also provided a safe haven for established retail companies, and that those companies, having being denied the opportunity to expand domestically, had expanded extensively off-shore, especially in Hong Kong, Singapore, Hawaii and Malaysia.

4. Foreign Pressure for Change – "GAI-ATSU"

During the same period, what had been an essentially domestic issue was fast becoming one of importance internationally too. The LSRSL issue was raised for the first time by the United States in the annual United States – Japan Trade Committee Meeting in 1985,[24] and was added to the list of barriers posited by the United States in the USTR National Trade Estimate Report on Trade Barriers in 1986 – a position it was to keep until 1999.[25]

Soon after the JFTC report was issued, the United States signalled a shift in their foreign policy agenda with Japan, putting the de-regulation of the distribution sector as their chief priority. In an interview with the Japan Economic Journal, the Deputy United States Trade Representative Lynn Williams explained the need for the talks as not only being a response to the huge trade deficit that was building between the two countries, but also to advance the desire of the United States to push ahead with the trade liberalization agenda.[26] The United States in particular expressed a wish to reach a mutual understanding about what they considered to be impediments to manufactured goods and capital goods, where the United States believed they had a competitive advantage that was not being realized.

On 25 May 1989, the Structural Impediments Initiative ("SII") round of bi-lateral negotiations were announced, attracting a great deal of media attention. The primary focus of the negotiations from Day One was the LSRSL. The contention of the United States was that "since larger retailers are usually more

23 In particular, the six major super-store owners - Daiei, Seiyu, Ito-Yokado, Jusco, Nichii, and Uny.
24 Schoppa, Bargaining with Japan: What American Pressure Can and Cannot Do (1997) 160.
25 USTR, National Estimate Report of Foreign Trade Barriers (1986), 161-62.
26 United States Section, Nihon Keizai Shinbun (Japan Economic Journal), August 12, 1989.

willing to risk introducing new products or aggressively promoting imported product lines, limits on retail expansion effectively hindered the import of U.S. goods".[27] Soon afterwards, when one of America's largest toy retailers, Toys 'R' Us, sought government support for its entry into the Japanese market, the United States was able to point to a direct example of a United States company being prevented from entry into the Japanese marketplace.[28]

IV: Deregulation

1. Stage I – 1990

In addition to this explicit foreign pressure, in the midst of the SII negotiations, Japan's two major business organisations, the *Keidanren* (Federation of Economic Organisations), and the *Nikkeiren* (Japan Federation of Employer's Associations) came out with an announcement giving their support for pressure to revise the LSRSL. Both organisations have significant pull within the LDP. The Keidanren, in particular, is an especially powerful lobby, as it is the procurer of political contributions by big businesses to the LDP.

So, despite having made opposition to liberalization of the rice market and the LSRSL a mainstay of their electoral campaign,[29] the LDP were now motivated to push ahead with their re-evaluation of policy surrounding the retail industry. The task of placating the small store and shopping arcade lobby had been made easier now that the Ministry had a foreign "menace" to add to the domestic pressure on which to blame their apparent about-face.

On 24 March 1990, the Japanese Government issued an interim report of the progress of the SII negotiations. Within the report were initial proposals to ease the restrictions imposed by the LSRSL. This was followed six days later by an announcement by Prime Minister Kaifu indicating his intention to abolish the LSRSL within three years. In accordance with the interim report, by May 1990, METI had undertaken a substantial review of the semi-formal and informal rules related to the Law. In the final SII report, issued in June 1990, METI finally acceded to the United States requests for liberalization, announcing a three-phase plan that was to "enhance the vitality of the distribution industry and to ensure smooth procedures for opening new stores".[30]

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27 USTR, National Estimate Report of Foreign Trade Barriers (1989), 113-14.

28 Upham, supra note 7, 267.

29 Political parties in Japan are involved in both national and local government. For the past 40 years, except for a few years in the early 1990s, the Liberal Democratic Party has monopolised control of Japan's Diet and local government.

30 Joint Report of the United States – Japan Working Group on Structural Impediments Initiative 2 (Tokyo, Japan) (28 June 1990).

The ordinance METI issued contained the following major advances:

1. The outright ban in some municipalities of large-scale store openings was abolished.
2. There was a call for a streamlining of the consultation procedures.
3. The period from the notification of intent to the handing down of "advice" from the CAAC was set at no more than one and a half years.
4. Local rules such as the pre-prior consent process and the regulation of medium-sized stores were abolished.
5. Regulations on store closing times and holidays, as well as limits on import item floor space were eased.

To appease the United States negotiators, METI had explained that these changes were the maximum extent of change to the regime that was legally possible within the provisions of the LSRSL. To deregulate further, they argued, would require completely new legislation.[31] Closer inspection of the law reveals that this is not entirely true, as the law itself provided for a maximum period of consultation of around seven to nine months, half of the time proposed in the METI ordinance. Furthermore, the CAAC was still in the control of local parties, making transparency all but impossible. As one academic argues, METI had only in effect taken a few steps closer to the formal processes that the law already provided, but was far from following them literally.[32]

Regardless of these inconsistencies, the results of this ordinance had a dramatic affect on the openings of large-scale stores. The rate of new stores being announced was up 200 per cent on the previous year, and nine times the rate of the 1982-1985 period.[33] The first evidence that the relaxation was also going to benefit foreign firms came with the opening of the first Toys 'R' Us store in December 1991. Toys 'R' Us had been interested in establishing itself in the Japanese retail toy market for years, and, even before the first store had opened, had plans to open 100 stores nationwide within ten years.[34] As evidence of the symbolism with which the entry of the foreign toy chain was to be seen, the opening of the company's second store was attended by President George Bush during his trade talks visit in January 1991.

2. Stage II – 1992

The next key step the Ministry took was to revise the LSRSL itself. In January 1992, the role of the CAAC was removed and placed entirely within the scope

31 Upham, supra note 7, 285.
32 Ibid 287.
33 Yomiuri Shinbun, (The Daily Yomiuri, NY ed.), 6 December 1990.
34 Toys 'R' Us was a Joint Venture between the US parent company and McDonalds Japan. By May 2003, the company had opened 139 stores throughout Japan – a rate of 10 new stores per year.

of LSRSC. The intention was to bring responsibility for proposal inspections back from local to national level. In contrast to the CAAC, the LSRSC was made up primarily of academics, whose task was to evaluate the opinions of local governors, CCI and interested parties, then obtain an order from METI. The academics involved in the LSRSC had quasi-public servant status, which, given that public servants in Japan are subject to criminal liability for bribery and corruption, supposedly made them more readily accountable. The maximum period allowed for the consultation process was set at 12 months. As a sweetener perhaps to continued pressure by the United States, at the time of these revisions METI also reiterated the intention to repeal the law entirely by 1994.

When the system was revised, the local organizations lost very little real control. While the new LSRSC was ostensibly free from the local administrative constraints, the truth was that it remained reliant on the local Chambers of Commerce and Industry for putting together local consents. Moreover, to appease the small-store owner lobby, immediately after the LSRSL revision METI also announced a proposal for how they intended to protect smaller retailers on the road ahead. The essence of the plan was to integrate small store interests into a city planning regime. Each municipality was to put together a proposal for the city centre, to be approved by the Ministry and local governments. All retailers were encouraged to participate in the scheme through a range of financial subsidies and tax relief entitlements. The net effect of the City Planning Law was that the revitalization of facilities and parking for the shopping arcades that most small stores inhabited was to be funded essentially by the large-scale stores in the area.

3. Stage III – 1994

The third and final step made towards de-regulation of the system before its abolition was in May 1994. Again, the change was stimulated by both domestic and foreign provocation.

After nearly 40 years in government, the LDP was swept from power in the 1993 general election by a coalition of breakaway ex-LDP politicians under Morihiro Hosokawa. Hosokawa's administration advocated massive changes and de-regulation as the only way Japan was going to be able to kick start its stalling economy. One of the focal points of the Hosokawa coalition's campaign was the retail sector and the need to bring Japan's retail prices somewhat closer to the rest of the industrialized world. The LSRSL was again brought to the centre of domestic political attention. As it turned out, internal politics and back- room negotiations saw the LDP regain its position as governing party only 11 months after the Hosokawa administration came to office.

In the United States, the new Clinton Administration was also focusing on the law as a target for discussion. In 1993, trade representatives entered a new round of bi-lateral negotiations under the 'United States – Japan Framework for a New Economic Partnership'. Though not going so far as to fulfil their 1992 promise

to repeal the law entirely, METI issued new ordinances revising certain minor aspects of the law. The crux of the revision, which came into effect in 1994, was to remove almost all regulation of stores between 500 and 1000 square metres, and to relax and extend the limits on the amount of hours and days a large-scale store was allowed to stay open.

In addition to these pressures, Japan's Economic Planning Agency ("EPA") had reported empirical evidence that added weight to the argument that de-regulation was working. First, and allaying the fears of Japanese government that relaxation of restrictions on large-scale stores would lead to extensive unemployment, de-regulation of the retail industry had led to a net gain of 300,000 jobs despite a loss of 600,000 jobs due to small retail store closures over the period 1990 to 1995. Furthermore, data from the EPA also showed that in spite of the poor overall economic outlook, the retail industry had grown by 4.5 trillion yen over the same period.[35]

By the time of the establishment of the World Trade Organisation ("WTO") in 1995, the issue had reached its crescendo. The United States was demanding the law be phased out by the end of 2000.[36] Domestic organizations saw the continued existence of the LSRSL as hindering any hope of a revitalization of the now flailing Japanese economy.[37] Even METI itself was announcing it was working on a new statutory regime that would replace the present law with a system based on City Planning Laws much like those in Europe.[38]

V: The Fuji – Kodak Dispute

The complaint made by the United States to the WTO identifying Japan's failure to fulfil its obligations and commitments under the GATS agreement was to prove to be the definitive act in bringing about the end of the LSRSL regime. The complaint was one of three dispute settlement proceedings laid by the United States in June 1996 using the WTO mechanism related to a dispute by Eastman Kodak Company ("Kodak") over access to the Japanese photographic materials market.

1. Overview

Kodak and Fuji Photo Film Ltd ("Fuji") together control 70 per cent of the world market in photographic materials. The inherent nature of the industry

35 Editorial, Nihon Keizai Shinbun (The Nikkei Weekly), 12 May 1997.

36 Submission by the Government of the United States to the Government of Japan Regarding De-regulation, Administrative Reform and Competition Policy in Japan (15 November 1996).

37 Report of Japan Fair Trade Commission, as reported in Nihon Keizai Shinbun (The Nikkei Weekly), 26 June 1995.

38 Schoppa, supra note 24, 148.

means that the four existing manufacturers have a virtual oligopoly.[39] Attempts at participation in the market have failed because of the huge economies of scale being realized by the established firms.[40] The rivalry between the firms is also extremely intense.

The dispute that ended in the GATT/GATS complaint by the United States began with an anti-dumping petition by Kodak in 1993. The United States International Trade Commission, and later the Commerce Department determinations in late 1993 led Fuji to make an agreement with the Commerce Department to increase their export prices to the United States in return for a suspension of the anti-dumping investigations.[41] Soon after the agreements were settled, in an effort to maintain their market position in the United States, Fuji pushed ahead with a plan to develop a manufacturing facility in the United States, the construction of which finished in March 1996.

Following this development, Kodak then filed a petition with the United States Trade Representative ("USTR") requesting that the United States government take action under section 301 of the Trade Act 1974. Kodak claimed that the Japanese government was imposing barriers to imports of Kodak's products which were unreasonable, unfair, and discriminatory. The claim was not specifically directed at Fuji, but was aimed rather at making Japan a "fair and competitive market".[42]

2. The USTR Section 301 Investigation

Much has been said about the validity of section 301. Many condemn it as the "nuclear weapon"[43] of international trade, and see it as evidence of a United States policy of "aggressive unilateralism".[44] On the other hand, the section can be conceived of as an astute and practical policy that protects United States firms under the legitimacy of state sovereignty. The comment by one Japanese government official that "the United States uses its own criteria to determine unfairness, prosecutes the case itself, and hands down the sentence"[45] is probably a fair reflection of the way section 301 is generally viewed in Japan.

A section 301 investigation that finds against a foreign government's practices can lead to mandatory or discretionary retaliatory action. Where an act by a foreign government is in direct violation of the WTO or other trade agreement, or a denial of any rights of the United States under any trade agreement then

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39 As with the automobile industry, the photographic industry requires continuous technology innovations and research, and huge capital outlays on mass production in order to remain profitable.

40 Komuro, "Fuji-Kodak Film Dispute and WTO Panel Ruling" (1998) 32(5) J of World Trade 161, 164.

41 US Department of Commerce News, Press Statement, August 19, 1994.

42 Komuro, supra note 40, 168.

43 "US Launches Broad WTO case under GATT, GATS against Japan on Film" Inside US Trade (14 June 1996) 22.

44 Schweitzer, supra note 1, 850.

45 Kuroda, "We've Had Enough of John Wayne" (Nov-Dec 1988) International Economics 67. It should be noted that Japan has on its own statute books the equivalent of Section 301 – Article VII of the Customs and Tariff Law.

retaliatory action is mandatory, whereas retaliation for "unreasonable" policies by foreign governments is discretionary. Kodak placed particular reliance on the new section 301(d)(3)(B), introduced to the Trade Act after the establishment of the WTO, which defines "unreasonable" and includes tolerance by foreign governments of cartel-like behaviour.

The USTR investigation began in June 1995, but no bilateral talks between the USTR and the Japanese government took place. In taking the complaint directly to the USTR, Kodak had bypassed the Japanese antitrust authority, the JFTC, which would ordinarily be the first port of call to hear any dispute about market competition in Japan. Insulted, and not wishing to set a precedent that such a course of action was acceptable to the Japanese government, Japan refused to talk to the USTR on the matter.

The results of the investigation were published by the USTR on 13 June 1996. Japan was deemed to have "unreasonably refused to consult on the substance of the matters under investigation", and it was concluded that the Japanese government was pursuing policies and practices that were unreasonable and burdensome to a fair and competitive market in which United States companies were involved. As a result of these findings it would have been legitimate under United States law for the USTR to take retaliatory action against Japan.

For the United States to have pursued this course of action, however, would have been a direct affront to the newly formed WTO Dispute Settlement Understanding ("DSU"), which prohibits the use of unilateral retaliation.[46] The alternative route, and the route chosen by the United States, was to seek redress under the new international dispute regime, and put their case to a WTO panel.[47]

On the same day as the section 301 decision was reported, the United States instigated two dispute settlement proceedings under the WTO (one GATS and one GATT based),[48] and another under the 1960 Arrangement of the GATT.[49]

3. The GATS Dispute

On 13 June 1996, the Permanent Mission of the United States to the WTO sent the Permanent Mission of Japan a "Request for Consultations". The request claimed that through "measures affecting distribution services, applied by the Government of Japan pursuant to or in connection with the Law Pertaining to Adjustment of Business Activities of the Retail Industry for Large Scale Retail Stores", the Japanese Government was failing to carry out its obligations and commitments under Article III (Transparency) and Article XVI (Market Access) of the GATS. As a result, the United States considered that benefits accruing to

46 Article 3: Understanding of Rules and Procedures Governing the Settlement of Disputes.

47 Komuro, supra note 40, 170.

48 GATT Dispute (WT/DS44/1), GATS Dispute (WT/DS45/1): Search available at <http://docsonline.wto.org/> (at 20 September 2004).

49 The 1960 GATT Arrangement dispute was not followed up after the GATT/WTO discussions went ahead.

it under the GATS were being nullified or impaired within the meaning of Article XXIII:3 of the Agreement.

(a) Settlement Process

After an initial round of consultations, the United States sent a renewed and increased set of concerns on 20 September 1996, adding a number of different laws and regulations related to the LSRSL, and notifying Japan that it now considered that it was failing to carry out its obligations and commitments under Article VI (Domestic Regulation) and Article XVII (National Treatment) as well as Articles III and XVI.

After a second round of consultations in November 1996 the United States appeared to decide that they would refrain from taking the issue any further. No panel was ever requested, and hence the dispute was never given a full and thorough airing in the public arena. The dispute was not, however, withdrawn from the WTO.

The events of the following year, as described below, lead one to assume that the reason for this retreat was a promise by the Japanese negotiators to replace the LSRSL as soon as practicable. However, the reason why the Japanese had come to the conclusion that the GATS dispute was not one with which they wished to proceed requires some consideration.

(i) Article III – Transparency

Article III of the GATS is a general commitment, from which a state cannot opt out. It seems apparent from the obligations listed in the Article that there would be a strong case for the argument that Japan was not divulging all the relevant measures pertaining to or affecting its retail sector. As had been pointed out by the JFTC in its 1989 report on the LSRSL, METI had not only been engaging in discussions with the major domestic players in the market, it had also specified certain municipalities that were to be subjected to "more regulation" than others, yet did not disclose exactly which municipalities those were. In addition, as was alleged in the GATT/WTO dispute, the various "administrative guidance" notices that had been issued appear to contain implicit or vague regulatory devices that may be in conflict with the principle of the Article.

(ii) Articles VI, XVI, and XVII

Articles VI, XVI, and XVII relate to the specific commitments a state has made in its Schedule to the GATS. In the 1994 Schedule of Specific Commitments, Japan had indicated that it was undertaking to impose no limitations on the relevant "Commercial Presence" mode of supply in the Distribution Services

– Retail Services sector.[50] Hence, it was possible that any limitation imposed on distribution services by the government may be considered a violation of the principles of the GATS.

On the Article XVI (Market Access) issue, it is readily apparent from the application of the LSRSL that the regime was in effect a limitation on the number of retail service providers. Even given the various amendments and steps made towards de-regulation throughout the whole LSRSL dispute, the legislation was always inherently based on restricting the incursion of large-scale retail stores, be they domestically owned or foreign, on the market of local small store merchants. As discussed later in the paper, it was this obligation in particular that METI focused on when re-constructing a GATS-proof legislative regime for the retail store sector.

The National Treatment requirement in Article XVI necessitates that the treatment of foreign companies be "no less favourable" than that for domestic suppliers. In this regard, the United States would have had a decidedly plausible argument that the system as it was set up was weighted against foreign service suppliers. Time delays, knowledge of the area and local concerns, and the ability to negotiate settlements with local small store retailers were all necessary factors that would possibly have put a foreign company at a distinct disadvantage to a domestic retailer.

(b) Conclusion

A WTO panel is limited to considering and ruling on whether or not a particular domestic law or regulation violates a principle or rule of the WTO agreements. It is not the concern of the panel whether a ruling invalidating a country's laws has any major consequences for a government either politically or socially.[51] From a government's perspective, however, the result of a negative decision by a WTO panel can have a significant impact on its authority, both internationally and domestically.

In the case of the Japanese distribution sector, a sector which is inherently linked to the whole way business is executed in Japan, the reverberations of a finding for the United States by a WTO panel in this dispute would have been tremendous.

Domestically, in the politically-unstable climate of the 1990s, support for abolition of the LSRSL amongst politicians in Japan was next to nil, especially among LDP members who were rapidly losing electoral support in the cities. The small store lobby's support had always been an essential part of the LDP being

50 The Schedule states "NONE except for as indicated in Horizontal Commitments". The horizontal commitments are not relevant to the present case. See <http://www.wto.org/english/tratop_e/serv_e/serv_commitments_e.htm> (at 20 September 2004).

51 Dillon, "Fuji-Kodak, the WTO, and the Death of Domestic Political Constituencies" (1999) 8 Minn J Global Trade 197, 235.

able to maintain its hold on political power. To have any legislation ruled to be in violation of WTO rules would probably have confirmed many constituents' suspicions that the LDP had pursued policies that were restricting the nation's growth in order to win favour amongst political lobbyists. Such a finding would have almost certainly damaged the already tarnished reputation of METI, whose meddling in the marketplace many ordinary Japanese were beginning to blame for Japan's regression into an ever-deepening recession.

A ruling against the LSRSL would have had incalculable repercussions internationally, too. Not only would it have given the United States the ability to enforce retaliatory sanctions against Japan, impacting immensely on Japan's exporters, but it may also have reaffirmed the apparent belief that the United States held that all distribution sectors in other markets should be modelled on the United States model.[52]

4. The GATT Dispute

The GATT request for consultations by the United States was made pursuant to Article XXIII:1 of the GATT 1994 and Article 4.4 of the DSU on the same day as the GATS request and the USTR ruling. The contents of this dispute were distinct from the GATS dispute in that they concentrated specifically on the trade in photographic film and paper. Consultations were held on both disputes a month later in Geneva, but a satisfactory conclusion was not agreed upon for either. In November, as described above, events or promises by the Japanese Government caused the United States to decide to discontinue the GATS dispute. At the same time, it would seem, the decision was made to push ahead with the GATT claim. In accordance with Articles 4 and 6 of the DSU, the United States requested that a WTO panel be set up to consider the dispute, the composition of which was decided by the Director-General of the WTO on 17 December 1996.[53] The Final Panel Report was issued on 30 January 1998, and adopted by the DSB in April of that year.

The United States' claim to the Panel was based around the point that the Japanese government had restricted the distribution and sale of foreign photographic material. The measures that the Japanese government was accused of pursuing can be summarized as follows:

1. The regulatory measures surrounding the domestic distribution system aided Japanese manufacturers to exclude foreign competition.

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52 Evidence of this belief can be found in the GATT dispute discussion. As the Japanese government countered, the United States arguments failed to take into account the cultural aspects behind the Japanese distribution system.

53 The members of the Panel were Mr W Rossier (Switzerland), Mr A Macey (New Zealand), and Mr V Luiz do Prado (Brazil).

2. The restrictions on Large-scale Retail Stores inhibited the growth of a major potential distribution network for imported film.
3. Regulation of sales promotions disadvantaged importers to the market.

Under Article XXIII:1, where a benefit to a member under the WTO is nullified or impaired by an infringement of GATT obligations by another member, then the aggrieved member may make a "violation complaint".[54] On the other hand, where a benefit of a member is nullified or impaired by a measure that does not conflict with a provision of the GATT, a member may still make a "non-violation complaint".[55] In the Fuji-Kodak dispute, the United States made both kinds of complaint about the measures the Japanese government was accused of taking.

(a) Non-Violation Complaints

The United States non-violation nullification and impairment complaints were only the eighth time in the 50-year history of the GATT that the provision had been invoked, and as such was treated cautiously by the Panel.[56] The Panel considered that "the United States case against distribution measures may best be understood in the context of the general theme advanced by the United States to the effect there exists in Japan a unique relationship between government and industry".[57]

(i) Distribution System Regulation

The United States proposed eight separate distribution measures that they considered nullified or impaired benefits due to them. The concept of whether "administrative guidance" (as discussed earlier in this article) could be considered "measures" was resolved by the Panel by appropriating statements in the Japan-Semiconductor case calling the question one of form versus substance. Lacking any substantial proof, the United States essentially asked the Panel to read between the lines and declare the Japanese method of governance unlawful under the WTO. The Japanese responded to this by maintaining that the United States were trying to substitute pre-conceived ideas about the Japanese culture for substantial evidence, and that the behaviour of a government will depend on many things not the least of which is the very culture it protects.

However, having examined each of the measures put forward by the United States, the Panel was unable to find any legal link between the "measures" taken by Japan and the loss of benefit the United States claimed.

54 GATT 1994, Article XXIII:1(a).
55 GATT 1994, Article XXIII:1(b).
56 WTO Panel Report, Japan – Measures Affecting Consumer Photographic Film and Paper, WT/DS44/R (3 April 1998), s 10.
57 Ibid.

(ii) The Large-scale Retail Store Law

The United States' second claim was that the LSRSL "restricted the growth of an alternative distribution channel for imported film". Not surprisingly, the Panel rejected this claim entirely. Japan had a long history of protecting its small owner-operator retailers, which was a factor in determining whether the United States could reasonably have anticipated that Japan would continue to do so. Moreover, the measures regulating the distribution sector were not only "neutral as to products and the origins of products", but the Panel also noted the significant liberalization of the retail sector since the early 1990s and the relative ease with which a large store was now able to open in the market.

(iii) Promotion Measures

The essence of this claim was that the Premiums Law that regulated the way in which firms can promote their products disadvantaged foreign manufacturers by constraining their ability to give discounts, gifts and use other innovative advertising campaigns. Again, the Panel considered these measures to be origin-neutral, and thus, while the restrictions may have an effect on competition, the United States was unable to point to substantial proof of discrimination.

The United States also attempted to argue that the combined effects of the above three measures collectively nullified and impaired benefits accruing to the United States. The Panel found that the United States had failed to justify this submission, and stated that it was not the function of the Panel to engage in its own investigation into effects of this theory.

(b) Violation Complaints

The next complaints dealt with by the Panel were two violation complaints under the GATT principles. The first was based on the National Treatment principle in Article III:4, the second being one of Publication and Administration of Trade Regulations under Article X:1.

On the National Treatment issue, the Panel reaffirmed its decision for the non-violation complaint, dismissing the claim that the measures were discriminatory on the grounds that the United States had failed to provide substantive proof. Furthermore, the United States was unable to prove a violation of the publication principle as it could provide no demonstrable evidence of any unpublished administrative rulings. Both violation complaints therefore failed.

(c) Conclusion

When the Panel's Final Report came out, the United States was quick to state its whole-hearted disagreement with the decision, but the fact that it is the only Panel decision not to have been taken on appeal to the DSB perhaps gives some indication of the true perception of the findings in the case. It was dealt with by the Panel in a lengthy, thorough and objective manner. Furthermore, the proceedings sent a clear message to member states that substantive facts and conclusive evidence, rather than conjecture and theory, are necessary elements of the WTO dispute resolution process. The Fuji-Kodak GATT dispute has since been criticised as being "a weak and premature attempt by the United States to bring competition law within the scope of the WTO".[58]

VI: Towards Abolition of the Large–scale Retail Store Law

Even while the GATT/WTO panel was considering the LSRSL impact on the photographic film industry, the United States continued to pursue the repeal of the law at a bi-lateral level. The topic was made a priority under the United States – Japan Enhanced Initiative on De-regulation and Competition Policy which began in early 1997.

As both these talks continued, in June 1997 METI held a meeting of the Joint Distribution Council to deliberate on the future of the LSRSL and surrounding issues. It seems clear that METI was keen to exercise control over the agenda and outcome of the meeting, as most government ministries do in Japan.[59] However, as it was still dominated by pro-small retailer members that until now had been supported by METI officials, the position of the Council had not changed. The Council voted firmly against further de-regulation.[60]

METI's reaction to this position, however, would seem to suggest that continued international pressure had altered METI's stance on the issue. By the time METI recalled the Council in October 1997, the Ministry had organized representatives from four groups advocating abolition of the law to make submissions to the Council. In addition to the Japan Chain Stores Association ("JCSA") and the Keidanren, METI took the unprecedented step of inviting the United States and European Union to state their arguments on the issue. All requested that the Council recommend the replacement of the law. Within a couple of months the Council issued a report recommending the LSRSL be scrapped.

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58 Dillon, supra note 51, 219.

59 Oya, "The Failings of the Government's Advisory Councils" Japan Echo (Autumn 1996) 15, 17.

60 Grier, "Japan's Regulation of Large Retail Stores: Political Demands versus Economic Interests" (2001) 22 U Pa J Int'l Econ Law 1, 29.

1. The New Legislative Regime

Despite the request by the United States at the Joint Council meeting that the formulation of the new legislation be made a public process, METI went ahead and drafted a new framework that would appeal to all parties. The package introduced to the Diet in February 1998 was a three-pronged regime that moved the central focus of control away from protection of small scale retailers towards an environmental approach. The three laws included in the package were the Large-Scale Retail Store Location Law ("SLL"), an amended City Planning Law, and the Town Revitalization Law.

The latter two laws can be considered as a compensatory package for the small owner-operator store lobby.[61] Under the City Planning Law amendment, local governments were given the authority to create special zones within their jurisdictions that could be dedicated to small to medium retailers only, or conversely set up so that large-scale stores would congregate in a designated area. Application of the City Planning Law comes under the guidance of the Ministry of Construction. The Town Revitalization Law is basically a funding scheme, the distribution of which is determined by proposals submitted by local governments. The scheme is designed so that zones such as the traditional shopping arcades in the vicinity of major train stations are given funds to modernize and "revitalize".

2. The Large-Scale Retail Store Location Law

In spite of the similarity in names between the new law and the old, the SLL is a completely different scheme of regulation to the LSRSL. Enacted by the Diet on 27 May 1998, and coming into effect June 2000, the focus of the SLL is not to control the number of large-scale stores, but rather to govern their impact on the surrounding environment.[62]

The main provisions of the SLL are the guidelines by which an application can be evaluated. After receiving notice of a planned development, local governments can make recommendations about the concerns they have with traffic congestion, parking, and noise, but such recommendations are not binding, nor can METI assert any influence over the application.

The United States, under the "Enhanced Initiative" negotiations, pushed for a "notice and comment" process to be adopted in the development of these guidelines, to which the Japanese government eventually agreed. Doubtless, this was an advance on the complete lack of public comment procedures pervading Japanese government. However, the extent to which the submissions by the United States[63] and others were taken on board is dubious, given that the

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61 Ibid 37.

62 Dillon, supra note 51, 242.

63 USTR, Submission of Comments by the Government of the United States on the Government of Japan's Guideline Established under the Large-scale Retail Store Location Law, 20 May 1999.

guidelines were finalized some ten days after the comments were due. One may speculate that the Japanese government had undertaken to perform the exercise of the process to the letter, but not the spirit.[64]

(a) The United States Response to the Large-scale Retail Store Location Law

The United States comments on the new legislation's guidelines indicate lingering concerns that the United States has regarding the future for foreign retailers in Japan, and would appear to be the reason that the United States has not taken the final step in removing its GATS complaint entirely from the WTO settlement process. The United States submission raises the following concerns:

1. The Guideline requires prospective retailers to conduct extensive research to "prove" that they will meet the standards in the Guideline. As such the SLL is merely a shift from a notification system to an approval system.
2. The SLL incorporates procedural requirements based on standards from other regulations that prima facie are not applicable to large-scale stores. These regulations are not mandatory, and appear to place unjust burdens on large-scale retailers.
3. The terms and contents of the SLL lack sufficient precision, which may lead to application by local governments that is not uniform. Lack of uniformity may lead to unnecessary inefficiencies for prospective retailers.[65]

(b) Implications of the Large-Scale Retail Store Location Law for Foreign Companies

It would appear from the way in which METI has designed the regime that METI officials held the belief that a business that wants to achieve anything in Japan would never contemplate going against a recommendation issued by a local government, and traditionally that would certainly be the case. For years, the mountains of required paperwork and exhausting consent periods meant that good relations with local government were essential. The result of this is that, amongst most business people, even in modern Japan, there is still a belief that any firm wishing to survive and grow steadily would have to maintain a degree of harmony with local officials.

As Professor Dillon points out though, all this means nothing to large international retailers of the likes of Toys 'R' Us and Wal-Mart.[66] Clearly it is not in the best interests of a retailer wishing to gain custom in a neighbourhood

64 Grier, supra note 60, 47.
65 USTR Submission, supra note 62, 5-7.
66 Dillon, supra note 51, 243.

to abuse the goodwill of local authorities, but it is also extremely unlikely that a multinational company that has undertaken a feasibility study giving promising results is going to be put off entry to a profitable market merely because a municipal government issues a negative "recommendation". To some extent therefore, METI's new legislation may even have gone as far as to give foreign retailers an advantage over domestic players, in that social and cultural barriers that may influence a domestic company are not apparent to a foreign firm.

VI: Conclusion

At this point it is worth considering why Japan did not go ahead with the abolition of the LSRSL as Prime Minister Kaifu had promised at the time of the SII. The two possible explanations that Schoppa gives go some way to answering this, and are indicative of the culture of governance that pervades Japanese politics in general. Schoppa claimed that "to do away with the law [at that stage] would mean [METI] would lose all of its influence over the retail sector. It would also have no way of stopping local governments from passing even stricter regulations ...".[67]

Despite the overwhelming need for de-regulation in the Japanese economy, Ministry officials seem loathe to give up control over their particular spheres of influence. In the case of the LSRSL, METI effectively had the ability to control the entire retail sector. In practice, they were able maintain control, to some extent, over which cities were to change and how; which retailers were to expand and how; and how, where, and on what consumers were going to be able to spend their money. METI was never likely to give all of that away easily, and with the possibility of withdrawal of electoral support by powerful small store retailers' lobby working in its favour, METI was able to prevent any sudden moves by the LDP to strip the Ministry of this influence. Furthermore, the thought of allowing that power to be handed over to their lesser cousins at local government level was probably an even more vexing proposition. After all, local governments were more likely to impose greater regulatory controls in order to protect local business (and almost certainly political) interests. It would also be METI that would have to deal with the international implications should local government regulations be criticised as being barriers to local markets.

Undoubtedly the United States demands during the SII, when added to the domestic pressure, helped to change METI's stance on the need for LSRSL-like regulation of the retail sector. With the benefit of hindsight however, one might be tempted to consider the Japanese government's announcement of the forthcoming repeal of the law during the SII negotiations, some nine years before the law was actually changed, to be a prime example of METI stalling the opposition. It

67 Schoppa, supra note 24, 165.

now seems highly likely that the period was used by METI to work out a new regime that was less likely to be considered in violation of Japan's international commitments and more likely to promote economic growth while all the while protecting METI's position of influence over the retail sector.

It is also clear that the GATS complaint was the turning point in METI becoming serious about the law change. According to a USTR Trade Compliance Center report on the progress of the implementation of Japan's stated commitments to the WTO panel, "Senior Japanese Government officials have acknowledged that [the act of repealing the LSRSL] was taken because of concern that a WTO panel would very likely find the Large Stores Law in violation of the General Agreement on Trade in Services (GATS)".[68]

That the Government of Japan was induced to reform legislation in such an important area of the economy by the threat of a WTO challenge has been acclaimed by some academics as a highly significant episode in the evolution of the WTO. The more rules-based and legalistic approach to international trade disputes that the WTO assures, in comparison to the more arbitrary rulings under the GATT, and which Japan had vigorously supported,[69] was showing itself to be a double-edged sword.

As Professor Dillon remarks, whatever relief the Japanese bureaucracy felt with the establishment of the WTO and the diminished need for constant bilateral negotiations such as the SII, Japan's pre-WTO socio-economic structure, selective internationalization, and controlled industrial expansion is likely to come under more and more pressure to succumb to the "absolutist dispute settlement system" that WTO membership entails.[70]

68 Assessment of Japan's Implementation of Specific Representations It Made to the WTO (August 19, 1998) United States Trade Representative, Trade Compliance Center, available at <http://170.110.214.18/TCC/DATA/commerce_html/assoc_docs/film1998.html (at 20 September 2004).

69 Ikeda, "GATTO kara WTO e: Boeki Masatsu no Gendaishi [From GATT to WTO: A History of Trade Friction]" (1996).

70 Dillon, supra note 51, 236.