

## 2. Japan

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### 1. GENERAL HISTORICAL BACKGROUND

Japan entered the modern age in 1868, the year of the Meiji revolution in which alliances of regional samurai domains defeated Tokugawa (Edo) shogunate (hereditary commander). Tokugawa had engaged in 200 years of national isolation, in which the shogunate prohibited all trade and communications with foreign countries, with the exception of limited trade with Dutch and Chinese merchants.

The Meiji revolution ushered in a new government which modernized Japan based on the political, economic and educational system of Europe and the US. For its legal system, the Japanese government adopted the continental (civil law) legal system developed by Germany and France.

After defeating Russia in the Russo-Japanese war (1904–5), Japan established itself as one of the most powerful nations in the world. Since 1926, after a worldwide depression, the military steadily gained power and eventually took over from the democratic government. This militarized Japan, then went into the disastrous Second Sino-Japanese War, resulting in Japan's alliance with Nazi Germany in World War II.

After their subsequent defeat in World War II, under US occupation, Japan transformed itself to a peaceful democratic country. Since the 1950s, Japan enjoyed rapid economic growth, ultimately becoming the second largest economic power after the US. However, since 1989 when the property and stock bubble burst, Japan has suffered more than two decades of economic stagnation. Japan is currently the third largest economy in the world by gross domestic product (GDP). By comparison, the population of Japan is 128 million (2010), the tenth largest in the world.

### 2. POLITICAL SYSTEM OF JAPAN

The Japanese government is based on the parliamentary system, in which a political party which prevails in the general election becomes the ruling

party in the legislative Parliament (Diet) and produces the prime minister, head of the executive branch.

## **2.1 Relationship between the Executive Branch, Political Parties and Bureaucrats**

The Japanese parliamentary system is constitutionally similar to that of the UK, but, in actual operation very different: the Japanese system makes it difficult for the prime minister to exercise leadership, and many government officials (bureaucrats) exercise autonomous power which can frustrate government policy.

Many of the characteristics of the Japanese parliamentary and the concomitant governmental system stem from the almost continuous rule of the Liberal Democratic Party (LDP) from 1955 to 2009. In order to allocate positions between factions inside the LDP, ministerial positions are rotated almost every year, so that ministers rarely master their policy brief, thus making them dependent on government officials for policy creation and application. Ministers, therefore, become captured by each ministry's sectional interests, at the expense of the minister's role as a member of the executive branch under the leadership of prime minister.<sup>1</sup> The bureaucracy is the permanent government of Japan, with ministers acting as little more than democratic camouflage.

## **2.2 Relationship between Bureaucrats and Businesses**

The weakness of ministerial direction in the executive branch has allowed bureaucrats to exert a predominant influence on policy making. Bureaucrats at each ministry have enjoyed autonomy in personnel appointments, including the heads of directorates, escaping intervention by the ministers.<sup>2</sup> Corruption by bureaucrats has been infrequent, but has occasionally occurred, mainly in the form of receiving bribes in exchange for giving benefits to companies under their administration.<sup>3</sup> Companies under heavy economic or social regulation (i.e. financial, energy and

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<sup>1</sup> See Iio, Jun (2007), *Nihon-no Tohchi Kozo* [Governmental system of Japan], Tokyo: Chuo-Koron Co., pp. 19–25. Moreover, LDP politicians, most of whom come from hereditary local magnates, are preoccupied with getting budget money to satisfy local special interests in their voting districts.

<sup>2</sup> Promotion of bureaucrats has been determined predominantly by seniority, resulting in a lack of either a merit system or high professional standards.

<sup>3</sup> Yet the Public Prosecutors' Office has effectively prosecuted corrupt bureaucrats, thus suppressing corruption at a low level.

utilities companies) have nurtured collusive relationship with bureaucrats, typically through accepting former top bureaucrats as company executives upon their retirement from public service (known as *Amakudari*: ‘descent from heaven’). Such collusive relationships have endangered or contributed to putting at risk citizens’ lives, i.e. HIV contaminated drugs and the nuclear disaster at Fukushima Daiichi in 2011.<sup>4</sup>

However the establishment of regulatory agencies such as the Financial Service Agency, separated from industry policy ministries, has proved effective in eliminating business–bureaucrat collusion.<sup>5</sup> The Corruption Perceptions Index (CPI)<sup>6</sup> indicates that Japan is ranked 17th (for cleanliness) out of 185 countries in 2010.<sup>7</sup>

### 2.3 The Role of the Courts

The Supreme Court is equipped with the power to annul legislation which violates the Constitution (Constitution Article 81), but has rarely exercised this power.<sup>8</sup> Courts are, as stated in the Constitution (Article 76, 77, 78), independent from the government. The government’s administrative decisions or orders have occasionally been challenged in the courts. The courts have, in the great majority of cases, upheld administrators’ actions, but in some cases – cases on the environment, employment relations, etc. – have found them illegal, thus effectively checking the administrative agencies.<sup>9</sup>

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<sup>4</sup> Virtually for the first time after World War II, the LDP lost the general election in 2009, ushering in a new era of ruling for the Democratic Party. The Democratic Party, in spite of repeated political troubles due to its lack of experience, hoped to change Japanese politics and government for the better, thanks mainly to its politicians being mostly untainted by Japanese political tradition. Yet labor unions, major supporting institutions for the Democratic Party, constitute a big special interest group that objects to social and economic reform. Moreover, the farmers’ associations maintain disproportionate political power against reforms.

<sup>5</sup> The Fair Trade Commission of Japan, an independent regulatory commission, has remained immune from close relationships with businesses.

<sup>6</sup> The Corruption Perceptions Index (CPI) was developed by Transparency International (TI), a non-governmental organization that monitors and publicizes corporate and political corruption.

<sup>7</sup> Transparency International’s Corruption Perceptions Index 2010 (2010). Retrieved 14 December 2011 from [http://www.transparency.org/policy\\_research/surveys\\_indices/cpi/2010/results](http://www.transparency.org/policy_research/surveys_indices/cpi/2010/results) (last accessed 2 February 2013).

<sup>8</sup> Yet the Supreme Court, in 2011, judged the general election system, in which voters are treated conspicuously unequally, as unconstitutional.

<sup>9</sup> See Mabuchi, Masaru (2009), *Gyoseigaku* (Public Administration), Tokyo: Yuhikaku Co., p. 274.

Judges have generally remained uncorrupt and there are no cases of judges involved in corrupt activities.

### 3. ECONOMIC SYSTEM OF JAPAN

#### 3.1 Structure and Nature of the Japanese Economy

The gross domestic product (GDP) of Japan in 2010 was US\$4330 billion (current PPT),<sup>10</sup> which currently is the third largest in the world after the US and China. GDP per capita at current prices is US\$39,738 in 2009,<sup>11</sup> ranking 24th in the world; a conspicuous decline from ranking third in 2000.

The Gini coefficient regarding income (for households consisting of two or more persons) for the year 2009 was 0.311,<sup>12</sup> which is considerably lower (more equal) than that of the US (0.45, year 2007) and about the same level as that of Canada (0.32, year 2005).

#### 3.2 Transition from Rapid Growth to Maturity and Stagnation

Japan achieved rapid economic growth (around 10 percent annually) until the end of the 1970s, thanks to the virtuous cycle of high saving ratio, high investment ratio and movement of labor from low productivity sectors (agriculture) to high productivity sectors (manufacturing). This cycle ended when Japan caught up with the advanced economies.<sup>13</sup>

During the 1980s, Japan became a mature economy with moderate economic growth. After the stock and property bubbles burst in 1989, the Japanese economy has been stagnant with a growth rate of around 1.2 percent.

In the last decade, Japan has experienced significant population decline as well as an aging population, which is expected to lead to deteriorating economic conditions. In order to overcome unfavorable economic

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<sup>10</sup> Data source: OECD, *Key Tables from OECD* (last updated: 9 May 2011). Retrieved from [http://www.oecd-ilibrary.org/economics/gross-domestic-product-in-us-dollars\\_2074384x-table3](http://www.oecd-ilibrary.org/economics/gross-domestic-product-in-us-dollars_2074384x-table3) (last accessed 27 May 2011).

<sup>11</sup> Data source: World Bank, *World Development Indicators* (last updated 2 April 2011).

<sup>12</sup> Source: Japan Statistics Bureau (2009). Retrieved from <http://www.stat.go.jp/data/zensho/2009/hutari/yoyaku.htm> (Japanese version only) (last accessed 13 December 2011).

<sup>13</sup> See Ohkita, Yoichi (2010), *Sengo-Nippon Keizairon* (Post-war Japanese Economy), Tokyo: Toyo-Keizai Co. pp. 165–95.

conditions, Japan needs to increase productivity in the agriculture and service sectors, as well as to raise innovation in the manufacturing sector through regulatory reforms and increased competition.

The Japanese economy is characterized by a ‘dual structure’: a highly productive manufacturing sector on the one hand and less productive agriculture and service sectors on the other.<sup>14</sup>

### 3.2.1 Agriculture

The importance of the agricultural sector has steadily declined and now occupies less than 1 percent of Japan’s GDP (farmers comprise 5.5 percent of the total population).<sup>15</sup> Agriculture is the least efficient sector in Japan, with the average farm’s scale being minuscule compared to other developed countries. The minuscule scale does not indicate the poverty of Japanese farmers: the average farmer’s income surpasses that of the average wage earner. This gap is partly explained by the fact that large majority of farmers are part-time, with their main income coming from non-farm activities, but the agricultural sector also benefits from very substantial subsidies and high trade barriers.<sup>16</sup>

### 3.2.2 Manufacturing sector

‘Secondary industry’ (mining, manufacturing and construction sectors) occupies a little less than 30 percent of GDP (2008).<sup>17</sup> Nevertheless, 90 percent of exports come from the manufacturing sector. Since 2000, the growth of Japan’s GDP has predominantly come from a small number of internationally competitive manufacturing industries – electrical appliances, steel, machinery and automobiles in particular.<sup>18</sup>

The labor productivity of these internationally competitive industries

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<sup>14</sup> Yashiro, Naohiro (2010), ‘Case Study 1 – Japan’, *Regulatory Reform for Recovery: Lessons from Implementation during Crises*. Paris: OECD, p. 77.

<sup>15</sup> This decline is the result of the natural evolution of a nation’s industry structure – Petty-Clark’s Law.

<sup>16</sup> Farmers and farmers’ associations have a disproportionately strong influence on politics partly due to inequality in voting districts. Agriculture is the most protected industry in Japan, with a high degree of import barriers and subsidies, as well as partial exemptions from Japanese competition law.

<sup>17</sup> Data source: The Statistics Bureau, Ministry of Internal Affairs and Communications, *Statistical Handbook of Japan, Chapter 3 Economy*, available at [http://www.stat.go.jp/english/data/handbook/c03cont.htm#cha3\\_3](http://www.stat.go.jp/english/data/handbook/c03cont.htm#cha3_3) (last accessed 27 May 2011).

<sup>18</sup> Ministry of Economy, Trade and Industry (the METI) (2010), *Sangyo-Kozo Vision 2010 (Industry Structure Vision 2010)*, p.12. Retrieved from <http://www.meti.go.jp/committee/summary/0004660/index.html> (last accessed 27 May 2011).

has constantly improved, while that of domestic manufacturing industries has, since 1990, stagnated, resulting in a marked disparity in productivity between the two industrial groups.<sup>19</sup>

### **3.2.3 Services sector**

The service sector accounts for a dominant share of economic activity in Japan: around 70 percent of both GDP and employment. The labor productivity of the service sector is low, which is responsible for low aggregate productivity in the Japanese economy.<sup>20</sup>

The low productivity of the service sector in Japan compared to the US has been attributed to the small scale of operation and lack of innovation. Compared to manufacturing, the service sector has natural barriers to international competition due to the impossibility of exporting or importing a large portion of services. Moreover, World Trade Organization (WTO) rules apply only partially to the service sector and thus service industries have less incentive to improve their efficiency.<sup>21</sup>

## **3.3 Economy-wide Competitiveness**

The IMD World Competitiveness Yearbook (2011) reports that Japan is ranked 26th among 58 countries.<sup>22</sup> This is a steep decline from 17th place in 2009, and a conspicuous decline from its top tier ranking in the 1990s.

Japanese manufacturers' worldwide ranking has also experienced a constant decline after the 1980s: electrical appliances and information technology companies have lost their top tier rankings. Only the auto manufacturers have maintained strong international competitiveness.

## **3.4 International Economic Relations**

Pressure from different international institutions and the US to open up the Japanese economy has played a vital role in deregulating industries and reforming regulations to increase competition. Pressure from outside

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<sup>19</sup> *Id.*, p.13.

<sup>20</sup> 'The growth of labour productivity per hour worked in services decelerated from an annual rate of 3.5% between 1976 and 1989 to 0.9% between 1999 and 2004' (OECD 2008).

<sup>21</sup> Nevertheless, not a few service companies in Japan have attained innovative and efficient operation: convenience store chains and courier service companies, for example. An accurate measurement of labor productivity in the service sector is difficult; the statistical data may have failed to take into account the generally high quality of service in Japan.

<sup>22</sup> IMD (2011).

is important for Japan because Japanese politics make it difficult to break the status quo, and special interest groups exert disproportionately strong political influence. The government is only able to defeat status quo interests on the pretext of obeying international obligations.

### 3.4.1 Membership in WTO and FTAs

Japan's membership in the General Agreement on Tariffs and Trade (the GATT, the forerunner of the WTO, 1955) has greatly contributed to Japan's post-war rapid economic growth through reductions of tariff rates for Japan's manufactured goods. On the other hand, agriculture remained largely exempt from the trade discipline of GATT. However, following the conclusion of the Uruguay Round in 1993, through the extension of trade discipline to agriculture, Japan was forced to eliminate import prohibitions and substantially decreased tariff rates for agricultural products. Nevertheless, tariff rates for agricultural products have remained very high, and domestic competition is very restricted due to the political power held by farmers and farmers' associations.

The Japanese government, since the end of the 1990s, has shifted its emphasis from the WTO to Free Trade Agreements (FTAs), having entered into a total of 11 FTAs, mainly with Asian countries. In comparison to the WTO, FTAs have grave deficiencies in that equal treatment among WTO member countries is neglected. Nevertheless, now that the Doha Round of the WTO faces failure, Japan's entry into FTAs with major global players has opened the possibility that now perhaps the necessary pressure may be exerted to stimulate reforms and enhance competition in Japan's low productivity sectors: agriculture, services as well as purely domestic industries.

In line with this scenario, the Japanese government has started to negotiate an FTA with the US and is at the pre-negotiation stage with the EU.<sup>23</sup> The former is within the framework of the Trans-Pacific Partnership (TPP)<sup>24</sup> – a new FTA whose predominant member is the US.

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<sup>23</sup> Gou Fujita (16 December 2011), 'Minister of Economy and Industry Discussed with the EU Counterpart on Japan/EU FTA', *Nikkei* (reporting that the METI Minister (Mr Edano) discussed with the EU Commissioner for Trade (Mr Deft), agreeing that the preliminary negotiation on a Japan/EU FTA be precipitated); Shigeru Seno (21 February 2012), 'Japan/EU FTA Negotiation to be Initiated before Summer', *Nikkei* (reporting that the heads of 12 EU member countries, including Premier Cameron, sent a joint letter to the President of the European Council (Mr Van Rompuy) urging the start of negotiations with Japan on the FTA prior to the coming summer).

<sup>24</sup> Former Prime Minister Naoto Kan, on October 2010, and new Prime Minister Noda, on November 2011, expressed the government's intent to apply

### 3.5 Openness to External Trade

Japan, in the 1980s, consistently achieved large trade surpluses with the US. American governments claimed that this was proof of Japanese domestic markets being closed to foreign companies. This perception triggered a Japan–US trade conflict.<sup>25</sup> Regardless of the cause of the trade surplus, the Japanese government, since the mid-1980s, has been engaged in projects to reform Japan’s economic structure, with the goal of increasing competition and opening up domestic markets to foreign companies.<sup>26</sup>

#### 3.5.1 Level of foreign direct investment

Foreign direct investment (FDI) for Japan is characterized by the low level of inward FDI: the inward flow of FDI into Japan, in 2009, was US\$ 11.8 (a 52 percent decline from 2008).<sup>27</sup> By contrast, Japan’s outward FDI, in 2009, was US\$ 74.7 billion (a 43 percent decline from 2008).<sup>28</sup> The low level of inward FDI indicates the unattractive nature of Japanese domestic markets for foreign companies.<sup>29</sup>

#### 3.5.2 Structure and ownership of the industrial sector

In the pre-World War II era, major Japanese industries were owned by a small number of financial/industrial conglomerates – known as ‘Zaibatsu’. But, after Japan’s defeat in World War II, the US occupation and government forcibly dissolved the Zaibatsu, thus making Japanese industries much more competitive. This greatly contributed to the rapid growth of the Japanese economy in the 1950s and 1960s. The occupation forces also imposed a competition law – the Antimonopoly Act – through which the Fair Trade Commission (the JFTC) was given power to prevent mergers and stock acquisitions, thus checking the concentration of industrial ownership.

The level of direct or indirect state ownership of industrial sectors is extremely low and the electricity supply and telecommunications sectors

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for membership in the TPP. Nevertheless, farmers’ associations have been fiercely opposed to this project.

<sup>25</sup> However, notable economists have pointed out that Japan’s trade surplus was caused by macroeconomic conditions, i.e. insufficient domestic demand.

<sup>26</sup> This endeavor has resulted in the deregulation of several industries, as well as the strengthening of the competition law.

<sup>27</sup> Data source: JETRO, *Japanese Trade and Investment Statistics*, available at <http://www.jetro.go.jp/en/reports/statistics/> (accessed 27 May 2011).

<sup>28</sup> Id.

<sup>29</sup> Many commentators have interpreted the low level of inward FDI as reflecting entry barriers to foreign businesses in Japan.

are operated by private companies. Japan Post was state owned until 2007, and engaged in postal, banking and insurance services, but it was privatized in 2007.

## 4. COMPETITION LAW AND POLICY

### 4.1 Nature of Competition Policy

Competition policy in Japan has been implemented predominantly through the enforcement of its competition law – the Antimonopoly Act (hereinafter ‘the AMA’) – by its enforcement agency – the JFTC.

Competition-oriented policies have been implemented by several economic ministries. The Ministry of Economy, Trade and Industry (METI, formerly MITI) has since the mid-1990s advocated pro-competitive industrial policies, with the goal of increasing companies’ competitiveness. Since 2004 METI has published reports on improving the AMA and its enforcement by the JFTC, although the METI has no legal authority to intervene in JFTC’s application of the AMA. Despite this pro-competition stance METI has maintained a marked tendency to implement industrial policies by attempting to pick industrial champions.<sup>30</sup>

The Ministry of Internal Affairs and Communications (MIC), in its regulation of the telecommunications sector, has advocated a pro-competition policy. Nevertheless, the ‘competition policy’ espoused by MIC is more interventionist than that of main-stream competition laws. For example, in its telecommunications regulation, MIC has adopted ‘dominant regulation’, in which designated telecommunications carriers are obliged to give other carriers access to their telecommunications facilities.<sup>31</sup> This is similar to monopolization (or abuse of dominance) regulation in competition laws. However, the dominant companies (‘designated telecommunications carriers’) are designated by reason of their market share being more than 50 percent. This standard is conspicuously more interventionist than that of the mainstream competition laws, which

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<sup>30</sup> See the following publication where the government advocates reshuffling industries through selecting promising industries. eg, Ministry of Economy, Trade, and Industry (the METI) (2010), *Sangyo-Kozo Vision 2010 (Industry Structure Vision 2010)*.

<sup>31</sup> Telecommunications Business Act (Act No. 86 of 25 December 1984, latest revision 2007), art. 33, translation available at [http://www.soumu.go.jp/main\\_sosiki/joho\\_tsusin/eng/Resources/laws/pdf/090204\\_2.pdf](http://www.soumu.go.jp/main_sosiki/joho_tsusin/eng/Resources/laws/pdf/090204_2.pdf) (last accessed 27 May 2011).

require that dominant companies' facilities at least attain 'essential facility' status before mandating dominant companies to give access to rival companies.

#### **4.2 State Action and Competition Law**

The AMA is broadly applicable to the actions of national and local governments, when these acts are in competition with business entities.

Enactments adopted by national and local governments may not be condemned as violations of the AMA. Nevertheless, conduct by national and local governments is not, of itself, exempt from the application of the AMA. The AMA is applicable to conduct by 'entrepreneurs' (a better translation would be 'business entities') which are defined as persons engaging in 'commercial, industrial, financial or any other businesses' (AMA Article 2 (1)). Court decisions have shown that governmental agencies are treated as 'entrepreneurs' when they operate in competition with private companies.

The Supreme Court in its *Tokyo Municipal Slaughter House* decision<sup>32</sup> opined that 'entrepreneurs' are identified, without regard to their legal status, whenever they engage in economic activities which consist of repeatedly and consistently supplying economic goods in exchange for revenue.

Not only local governments but also the national government may be found in violation of the AMA. The Supreme Court in its *New Year's Greeting Post Card* decision<sup>33</sup> stated that the AMA is applicable to the Post Ministry when the Ministry sells value-added postal cards (such as anniversary cards) in competition with private companies.

#### **4.3 Industrial Policy and Competition Law**

Industrial policy used to play a conspicuous role in the Japanese economy, but its role has greatly diminished. One form of industrial policy was the protection of infant industries. For instance, foreign automobile manufacturers were initially severely restricted as regards exports or investments in Japan until the mid-1970s. However, much industrial policy was exercised not to bolster new industries, but rather to protect mature or declining industries.

Mainstream economists today deny that industry policy played a

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<sup>32</sup> Supreme Court decision, 43 (12) Minshu 2078 (14 December 1999).

<sup>33</sup> Supreme Court decision, 45 Shinketsushu 467 (18 December 1998).

positive role in Japan's post-war economic growth. Rapid economic growth was attained, in spite of industrial policies, thanks to favorable macroeconomic conditions, as well as intense domestic and export competition.<sup>34</sup>

After Japan became a member of the GATT (1955) and then the Organisation for Economic Co-operation and Development (OECD) (1964), obligations to adhere to international trade and investment rules hindered Japanese ministries' ability to engage in blatantly protectionist industrial policies since the Japanese government realized that competition was vital to strengthen Japanese firms.

Industrial policies conducted by the METI (or any other economic ministry) had no authority to block enforcement of the AMA by the JFTC, except in instances where such policies emanated from legislation which specifically exempted business entities or conduct from application of the AMA. Such special legislations have gradually been curtailed. The last such legislation was the Industrial Restructuring Law (Sanko-Ho) (1983–7).<sup>35</sup>

#### 4.4 Regulated Industries and Exemptions from the AMA

The AMA is applicable to regulated industries unless the industries are specifically exempted from the AMA by law (including the AMA itself). Such exemptions are rare, for example: the telecommunications and electricity sectors are not exempt from the AMA.

In the JFTC *NTT East* decision,<sup>36</sup> the defendant's argument that a telecommunications company regulated by telecommunications legislation may not be found in violation of the AMA was rejected. The JFTC based its conclusion on the fact that conduct in conformity with the telecom legislation is not necessarily in conformity with the AMA.<sup>37</sup>

In limited instances, clauses in the AMA or other laws exempt certain conduct from the application of the AMA. Such exemptions used to be numerous and previously robbed the AMA of much of its effectiveness. However, in the 1990s the Japanese government drastically curtailed

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<sup>34</sup> See e.g. Ohkita (2010), pp. 199–249.

<sup>35</sup> The Industrial Restructuring Law designated several industries (e.g., the petrochemical industry) for industrial policies aiming at supply reduction. The Law also provided companies with limited exemptions from the AMA. Nevertheless, the exemptions required the approval of the JFTC, preceded by the JFTC's consultation with MITI.

<sup>36</sup> The JFTC hearing decision, 53 Shinketsushu 776 (26 March 2007), supported by Supreme Court decision, 1339 Hanrei Times 55 (17 December 2010).

<sup>37</sup> Id. at 812.

AMA exemptions. Repealed exemptions include those related to natural monopolies (rail, electricity etc.), as well as an exemption for depression cartels (cartels to reduce production quantities or production facilities in depressed industries where prices do not cover costs).

Currently exemptions from the AMA apply to 21 activities authorized by 15 laws (Sea Transport Act, Air Transport Act, etc.). This is a marked decline from 89 activities authorized by 30 laws in 1995.<sup>38</sup> Most exemptions are on price (or rate) cartels in such industries as insurance, sea transport and aviation. These exempted cartels have shielded these industries from competition, and have thus lowered efficiency.

The JFTC has advocated repealing many of these exemptions. The JFTC has also advocated, through its study group, the implementation of regulatory reform by introducing competition to regulated industries. Nevertheless, the JFTC's power in regulatory reform is limited to an advocacy role.

Conduct compelled by governmental regulations may not be found in violation of the AMA. The JFTC decision in *Osaka Bus Operators' Association*<sup>39</sup> showed that the JFTC severely limits the circumstances under which legal compulsion can be used to justify breaches of the AMA. In this case, the Osaka Bus Operators' Association reached an agreement not to operate chartered buses at rates lower than the approved rates. The JFTC's decision recognized that 'substantial restraint of competition' was not realized because low prices were prohibited by the Road Transportation Act. Nevertheless, the decision noted that the JFTC may issue remedy orders against price collusion when transactions at prices prohibited by laws (other than the AMA) are openly conducted.<sup>40</sup>

Administrative guidance by ministries directed at companies may not exonerate violations of the AMA because guidance intrinsically lacks penalties against non-observance. This standpoint was confirmed in the JFTC Guidelines on Administrative Guidance.<sup>41</sup>

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<sup>38</sup> The JFTC (2009), *2009 NendoNenji-Hokoku (Annual Report, Fiscal year 2009)*, abbreviated translation available at [http://www.jftc.go.jp/en/about\\_jftc/annual\\_reports/pdf/101008\\_Annual\\_Report\\_FY2009.pdf](http://www.jftc.go.jp/en/about_jftc/annual_reports/pdf/101008_Annual_Report_FY2009.pdf) (last accessed 27 May 2011).

<sup>39</sup> The JFTC hearing decision, 42 Shinketsushu 5 (10 July 1995).

<sup>40</sup> *Id.* at 61.

<sup>41</sup> The JFTC, Guidelines Concerning Administrative Guidance under the Antimonopoly Act (30 June 1994), at §1 (1) ('Without exemption clauses, private conduct induced by administrative guidance is subject to the AMA application, when the conduct fulfills the conditions for illegality under the AMA.'), translation available at [http://www.jftc.go.jp/en/legislation\\_guidelines/antimonopoly\\_guidelines.html](http://www.jftc.go.jp/en/legislation_guidelines/antimonopoly_guidelines.html) (last accessed 27 May 2011).

## 4.5 Enforcement of the AMA

The AMA amendments in 2005 and 2009 considerably strengthened the enforcement powers of the JFTC. First, a leniency system was adopted. Second, the fine rate against violations increased from 5 percent to 10 percent. Third, the types of conduct subject to fines were widened. On the other hand, the AMA revision envisioned in 2011 (extended to 2013) will repeal the JFTC administrative hearing system, and so allow defendant companies to appeal the JFTC's remedy orders directly to the courts.

### 4.5.1 Fair Trade Commission of Japan

The AMA is enforced by the Fair Trade Commission (the JFTC). Private actions (private suits) may also be filed in the courts without the involvement of the JFTC. Their number has increased, but they still represent only a small proportion of AMA cases.

The JFTC is composed of Commissioners and the Secretariat. Five Commissioners (Chairman and four Commissioners) are authorized to act independently of the government, although the JFTC, as a governmental organization, is accountable to the Cabinet Office (AMA Article 27, 28).

Commissioners (including the Chairman) are appointed by the Prime Minister. The Chairman is a political appointee and has usually been selected from former senior civil servants from influential government ministries, predominantly the Ministry of Finance.

The Secretariat is composed of a Director-General, three general divisions (15 sections) and five local offices. Staff members are mostly recruited from among university graduates with an undergraduate degree in law or economics. A few of them have had experience as attorneys, or have PhDs in economics. The JFTC has pledged to increase the number of such professionals among its recruits. Indeed, the number of attorneys recruited from the Prosecutor's Office and private law firms has increased, particularly for posts dealing with decisions, suits and criminal investigations.

### 4.5.2 Remedy orders, hearings, decisions and sanctions

The JFTC orders have quasi-judicial status. The envisioned revision of the AMA in 2011 (now extended to 2013) will repeal the decision system. The JFTC will lose its quasi-judicial nature and instead become a purely administrative agency. After the proposed revision, the JFTC will issue remedy orders as administrative orders. The remedies usually consist of cease-and-desist provisions, but they may also include behavioral orders or structural remedies. Cited companies may bring nullification suits directly to court in the new post-2013 system.

Penalties against companies or individuals found to be in violation of the AMA consist of (1) administrative fines and (2) criminal penalties. Fines are levied only on companies (not on individuals).

Fines were originally levied only on companies engaging in price cartels or similar serious violations affecting prices. But the 2009 AMA amendment greatly expanded the coverage of these fines. Types of violations now covered by fines include (1) monopolization cases, as well as (2) unfair trade practices, consisting of (i) unduly low pricing and discriminatory pricing, (ii) concerted refusal to deal, (iii) resale price maintenance, (iv) abuse of superior bargaining position, (v) misrepresentations in violation of the Act against Unjustifiable Premiums and Misleading Representations.

Fines are automatically levied, without any discretion on the part of the JFTC, being set at 10 percent for manufacturers (4 percent for small and medium enterprises) of firms' sales of the affected product for up to three years for the targeted violations.<sup>42</sup>

Political considerations, rather than legal logic, induced the Diet (legislature) to amend the AMA to enlarge the coverage of fines. Small and medium enterprises (SMEs) exert disproportionate influence on policy making due to their importance as loyal voters and as a source of political funding. The coverage of fining was expanded to cover violations of the AMA clauses which were considered to be important for the protection of small and medium enterprises. As a result, unduly low or discriminatory pricing was included as a finable offence. However, punishing low pricing often softens price competition, to the detriment of consumer interests, and so protects competitors rather than competition in many instances.

The 2009 enlargement of the coverage of fines extended the types of business conduct that are not clearly anti-competitive. Thus, the current fining system risks discouraging aggressive competition. In order to rectify this, the fine system should be amended to give the JFTC discretion as regards the amount of the fine, as well as whether or not to impose a fine at all. Criminal penalties may be levied only on violators (companies and individuals) in relation to breaches of 'unreasonable restraints of trade' (most commonly horizontal cartels), as well as monopolization, though the JFTC has never applied a criminal penalty to a monopolization offense.

#### **4.5.3 Judicial enforcement and remedies**

Courts are involved in AMA cases via two routes: (1) suits that seek nullification of JFTC decisions and (2) private actions. The first route is available when companies are found to be engaged in illegal activities as a

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<sup>42</sup> The fine rate can be raised to 15% for repeat offenders.

result of a JFTC decision; aggrieved defendants may then bring a suit to court seeking nullification of the JFTC decision.

In private actions (private suits), citizens or companies may file an action based on the AMA violations and directly proceed to regional courts without the involvement of the JFTC. In contrast to the US, the number of private actions (either injunction suits or damages actions) in Japan has remained very small. This is due to lack of an effective class action system in Japan. However, the number of private actions has been increasing in recent years, and court decisions with noteworthy opinions have resulted.

## 5. STRUCTURE OF COMPETITION LAW

### 5.1 Structure of the AMA

The AMA was imposed on Japan in 1947 in the wake of World War II, under the auspices of the US occupation government. The AMA was therefore modeled broadly along the lines of US antitrust laws. However, some unique Japanese characteristics – especially the concept of unfair trade practices – were added to the AMA, making the AMA provisions more complicated (and confusing) than the US Sherman Act.

The AMA has four pillars: (1) unreasonable restraint of trade, (2) unfair trade practices, (3) mergers and stock acquisitions and (4) monopolization. These pillars, apart from (3) mergers, are overlapping: application of (2), the unfair trade practices clause, overlaps with that of either (1) unreasonable restraint of trade or (4) monopolization.

In addition, the unfair trade practices clause deals with business practices usually not considered as the domain of competition law: in particular, the abuse of a superior bargaining position and unfair inducement of consumers to enter into contracts.

The common classification of anti-competitive conduct, developed mainly through US and EU competition laws, generally consists of: (1) horizontal restraints (agreements), (2) vertical restraints, (3) mergers and (4) unitary conduct by dominant entities. In relation to this common classification, the four pillars of the AMA are constituted as shown in Table 2.1.

### 5.2 Horizontal Restraints

Horizontal restraints – agreements among competitors – are prohibited by the AMA, only when they constitute the exercise of market power.

*Table 2.1 Classification of anti-competitive conduct and corresponding AMA clauses*

| Classification of anti-competitive conduct | Applicable AMA provisions   |
|--|---|
| Horizontal restraints                      | Unreasonable restraint of trade<br>'Control' part of monopolization<br>Unfair trade practices |
| Vertical restraints                        | Unfair trade practices  |
| Mergers and stock acquisitions             | Clauses on mergers and stock acquisitions   |
| Unitary conduct                            | Monopolization<br>Unfair trade practices  |
| Other unfair conduct                       | Unfair trade practices  |

Nevertheless, price cartels and bid rigging have been prohibited as virtually per se illegal.

### 5.2.1 Market power standard

Horizontal agreements are predominantly regulated by AMA Article 3 and 2 (6). Article 3 (the latter half) prohibits 'unreasonable restraint of trade', which is defined by Article 2 (6) as 'business activities, by which any entrepreneur, by contract, agreement . . . in concert with other entrepreneurs . . . fix, maintain, or increase prices, or to limit production . . . thereby causing . . . substantial restraint of competition in any particular field of trade'.

'Substantial restraint of competition' is the most important criterion for identifying illegality under the AMA. The AMA clauses for monopolization (Article 2 (5)), and mergers (Article 10, 15) also use this criterion. 'Substantial restraint of competition' was interpreted by the Supreme Court as 'the formation, maintenance, or strengthening of market power', which is paraphrased as 'a situation where existing rivals do not amply restrain the power of the incumbent'.<sup>43</sup>

### 5.3 The 'Illegal in Principle' Standard for Price Cartels and Bid Rigging

The requirement that market power be identified for finding horizontal restraints (including 'hardcore' cartels) illegal is at odds with the global standard of condemning hardcore cartels as per se illegal (or illegal in

<sup>43</sup> Supreme Court *NTT East* decision, 1339 Hanrei Times 55 (17 December 2010).

principle). The lack of the per se illegal treatment has burdened the JFTC with determining the relevant markets for calculating the combined market share of cartel participants. In order to lighten this burden, the JFTC has routinely identified a relevant market for a price agreement (price cartel) as the product for which cartel participants aim to raise the price.

Moreover, the JFTC published its Distribution Guidelines,<sup>44</sup> which express an ‘illegal in principle’ position against price cartels and similar hardcore cartels or restraints – ‘agreements not to compete for customers, group boycotts, and resale price maintenance’.<sup>45</sup>

Nevertheless, the courts have never explicitly accepted this position; therefore the JFTC has been obliged to present a rough delineation of the relevant markets and market power even in price cartels and bid-rigging cases.

#### 5.4 Finding an Agreement

As a condition for identifying an illegal cartel (collusion), the JFTC is required to prove that an agreement was reached between conspirators. This is a universal requirement for identifying an illegal cartel. A unique issue arising from the AMA is the need to identify mutuality in relation to the restriction between participants.

The phrase ‘mutual restriction’ (AMA Article 2 (6)) engendered two requirements for identifying an illegal ‘unreasonable restraint of trade’, which were set out by the Tokyo High Court in the *Newspaper Distribution Agreement* decision<sup>46</sup> (as well as the subsequent JFTC decisions). First, ‘mutual restrictions’ may be found only in agreements between horizontally competing companies; agreements between companies in a vertical relationship (typically, a manufacturer and its distributors) are not considered as ‘mutual restriction’. Vertical agreements, then, are regulated only as unfair trade practices. (See below at 5.7)

Second, transactions between companies, in which one party is deemed to have unilaterally imposed a restriction on another party, is not considered to be a mutual restriction and, thus, may not be condemned as an unreasonable restraint of trade. This situation typically has arisen in bid-rigging cases in which one party obtains a contract while the other

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<sup>44</sup> The JFTC, Guidelines Concerning Distribution Systems and Business Practices under the Antimonopoly Act (11 July 1991) (hereinafter ‘Distribution Guidelines’), translation available at [http://www.jftc.go.jp/en/legislation\\_guidelines/antimonopoly\\_guidelines.html](http://www.jftc.go.jp/en/legislation_guidelines/antimonopoly_guidelines.html) (last accessed 27 May 2011).

<sup>45</sup> *Id.* at Introduction 3.

<sup>46</sup> Tokyo High Court decision, 2 Hanrijihō 8 (9 March 1953).

parties are constrained to make higher bids, so that mutual restraints are not found. The JFTC, then, has had to identify a source agreement which resulted in subsequent bid-rigging behavior.

An agreement may not be identified from the mere existence of parallel price rises, but a parallel price rise together with circumstantial evidence may lead to finding of an agreement. This has become a common standard in competition jurisdictions worldwide, including Japan.

Since the 1990s, JFTC has identified agreements from circumstantial evidence. This stance by the JFTC was supported by Tokyo High Court in the *Toshiba Chemical* decision,<sup>47</sup> in which explicit proof of an agreement was not found, but the participants were found to have held meetings and exchanged information on price prior to the parallel price rises. The decision held that ‘mutual communications of intent’ may be found from ‘implicit mutual understanding between companies about their price rises’.

### **5.5 The Role of Leniency in Discovering Price Cartels and Bid Rigging**

The AMA revision in 2005 ushered in a leniency system, which grants immunity from (or a reduction of) penalties in exchange for informing the JFTC of illegal horizontal restraints.

The first company to provide the relevant information is granted full leniency, the second company a 50 percent reduction, and the third a 30 percent reduction (AMA Article 7-2).

Although leniency is not formally applicable to criminal penalties, the JFTC pledged not to appeal for criminal penalties against the first informant company, its executives and employees.

The leniency system has proved to be remarkably effective in disclosing hidden cartels, contrary to the widespread perception that leniency would not succeed in the Japanese business circle, which traditionally honored harmony and collusion. Leniency has generated as many as 349 applications since its introduction in January 2006 (up to the end of March 2010).<sup>48</sup> This number amounts to approximately seven instances a month.

### **5.6 Assessment of Effectiveness and Areas for Improvement in Horizontal Restraints Regulation**

The leniency system has proved to be quite effective in uncovering cartels. Nevertheless, the outmoded AMA clause on horizontal restraints should

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<sup>47</sup> Tokyo High Court decision, 1493 Hanreijihō 54 (25 September 1995).

<sup>48</sup> The JFTC Annual Report (*Neiji-Hokoku*) for fiscal year 2009, *supra* note 38.

be modernized, and the JFTC needs to establish an administrative guideline on horizontal restraints.

The AMA clause on horizontal restraint (Article 2 (6)), which prescribes that cartels are illegal only when participants have market power, has inflicted an unnecessary burden on the JFTC in identifying illegal hardcore cartels. The AMA Article 2 (6) should be amended to stipulate that hardcore cartels may be found illegal without proof of market power (namely, ‘substantial restraint of competition’). Such an amendment might take the form of prohibiting an agreement whose objective is to restrain competition, in line with EU competition law (Treaty on the Functioning of the European Union Article 101).

The requirement to identify ‘mutual restraint’ instead of proving the existence of a restraint should be repealed through amendment of AMA Article 2 (6), since strict mutuality of restraints is not logically necessary to operate a cartel.

As regards the criteria for identifying an ‘agreement’, the established criterion of ‘implicit mutual understanding’ being sufficient (e.g. *Toshiba Chemical*) is so broad that legitimate ‘conscious parallelism’ risks being found to be illegal. The JFTC and courts need to refine the criteria identifying agreements, learning from the antitrust jurisprudence in the US and the EU.

The JFTC’s enforcement in respect of horizontal restraints has been exclusively applied to hardcore cartels. Treatment of other horizontal restraints (for example, joint venture agreements) is opaque. The JFTC should publish a guideline on horizontal restraints, taking as models the EU’s Horizontal Restraint Guidelines and the US’s Collaboration Guidelines.

## 5.7 Vertical Restraints

Vertical transactions are those between a seller and a buyer (or a supplier and a customer). Vertical transactions often involve restraints that manufacturers impose on distributors. Such restraints may also be imposed through agreements between suppliers and customers. Vertical restraints that foreclose against rivals (exclusive dealing, tying etc.) are treated as unilateral conduct by the AMA (see 5.11.2). Vertical restraints here concern those restricting intra-brand competition – competition in relation to one manufacturer’s products.

### 5.7.1 Illegality of vertical price restraints

JFTC and the courts have distinguished vertical price restraints, namely, resale price maintenance (RPM) from non-price vertical restraints,

treating RPM as per se illegal. Per se illegality, however, is not mandated by the AMA provision dealing with RPM; AMA Article 2 (9) (iv) stipulates that RPM is illegal when it is exercised ‘without legitimate reasons’. Nevertheless, the JFTC and courts have never elaborated on what constitutes ‘legitimate reasons’ in RPM cases.

Copyrighted published goods (books and music CDs) are specifically exempted from the prohibition on RPM by AMA Article 23 (4). JFTC had endeavored to repeal this exemption clause, but political pressures have supported publishers who opposed the abolition of the exemption. This exemption has resulted in prohibition of bargain prices, and thus has hampered online sales of books and musical CDs and electronic versions of music files and books in Japan.

### **5.8 Vertical Non-Price Intra-Brand Restraints – Rule of Reason Type Scrutiny**

In contrast to price restraints, the AMA condemns non-price vertical restraints only when they are performed ‘unjustly’.<sup>49</sup> Non-price vertical restraints – those causing intra-brand restraints – are scrutinized on their reasonableness. Nevertheless, the JFTC has not adopted the rule of reason as practiced in the US, but has adopted a more rigid regulation similar to the EU system.

The JFTC, in its Distribution Guidelines,<sup>50</sup> classified non-price vertical restraints into three groups and, for each, provides detailed standards to judge their reasonableness. These three groups are: (A) restraints that are always treated as legal (non-rigid territorial arrangements, etc.), (B) restraints found to be illegal when they are conducted by manufacturers with a ‘significant position in the market’ (rigid territorial restraints, namely those forbidding sales outside territories), (C) restraints found to be almost per se illegal, namely, a mere finding of a ‘danger to raise or maintain price’ is enough for the JFTC to identify illegality (an absolute territorial restriction forbidding acceptance of offers from outside the territory granted, a ban on sales to discounters, etc.).

However, courts have not always followed the Distribution Guidelines. The Supreme Court in *Fujiki v. Shiseido* held that restraints on sales methods imposed by a manufacturer on distributors may not be found to

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<sup>49</sup> The AMA art. 2 (9) and the JFTC Notification No. 15 of 1982, Designation of Unfair Trade Practices (18 June 1982) (hereinafter ‘General Designation’), Section 13 and others, translation available at [http://www.jftc.go.jp/en/legislation\\_guidelines/ama/unfairtradepractices/index.html](http://www.jftc.go.jp/en/legislation_guidelines/ama/unfairtradepractices/index.html) (last accessed 27 May 2011).

<sup>50</sup> *Supra* note 44, at §II.

be an unjust restriction in so far as the restraints are ‘based on a certain degree of reasonableness for the product’s sales, and at the same time, other distributors are subject to the same restraints’.<sup>51</sup>

Moreover, the Tokyo regional court, in the *Sankomaru* decision,<sup>52</sup> enunciated a rule of reason type approach, which was more flexible than the rigid JFTC Distribution Guidelines. This decision concerned a rigid territorial restraint imposed by a pharmaceutical manufacturer. The Regional Court required three conditions to be fulfilled for a rigid territorial restraint to be found illegal: (1) the manufacturer should occupy a ‘significant position in the market’; (2) the restraint should form an unreasonable restraint on the distributor’s business; and (3) the restraint should exert price-restraining effects.<sup>53</sup>

With the parallel existence of different criteria in relation to vertical non-price restraints, their regulation is confusing. JFTC needs to modernize their approach and establish new ‘Vertical Restraint Guidelines’, in which regulatory criteria need to be based on sound economic thinking. Then, market power needs to be required in order to condemn non-price restraints because consumers are not worse off without the existence of market power.

### 5.9 Assessment of Effectiveness and Areas for Improvement in Vertical Restraints Regulation

The JFTC’s Distribution Guidelines have become outmoded as they are preoccupied with rigid form-based classification of restraints. Moreover, courts have expressed differing standards in respect of vertical restraints. The JFTC, therefore, needs to replace its existing guidelines. The envisioned new guidelines might adopt presumptively illegal standards on vertical price restraints (RPM), under which manufacturers would be allowed to rebut the presumption by showing the efficiency effects of RPM.

The AMA Article 23 (4) (which authorizes RPM on books and musical CDs) needs to be repealed because this legal authorization has become the major obstacle to online sales of physical books, e-books and music.

With regard to non-price vertical restraints, the JFTC might adopt a rule of reason modeled after current US practice, in which non-price restraints would be found illegal only where market power exists. The current rigid standard based on the form-based classification unduly

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<sup>51</sup> *Fujiki v. Shiseido*, 45 Shinketsushu, at 458.

<sup>52</sup> Tokyo Regional Court decision, 51 Shinketsushu 877 (15 April 2004).

<sup>53</sup> *Id.* at 913–16.

restricts manufacturers' freedom to design their own distribution methods. In contrast to the EU, Japan does not need to be preoccupied with market integration.

## **5.10 Unilateral Conduct (Dominance/Monopolization)**

Exclusion (or foreclosure) of rivals is conducted either unilaterally or in collaboration (by multiple companies). Collaborative exclusion may be regulated as a horizontal agreement between competitors. This section, therefore, deals with unitary exclusion.

### **5.10.1 Lack of market power requirement**

Under the AMA, exclusionary (unitary) conduct may be attached under either the monopolization clause (the AMA Article 2 (5)) or the unfair trade practice (UTP) clause (Article 2 (9)). The monopolization clause, modeled after the US Sherman Act Section 2, has a market power requirement, while the UTP clause lacks a market power requirement. The JFTC, therefore, has found it much easier to make use of the UTP clause rather than the monopolization provision regulating exclusionary conduct.

The UTP clause, as applied to exclusionary (unitary) conduct, increases the risk of false positives (the risk of too much intervention), because the UTP clause allows the JFTC to eschew the task of identifying market power through delineation of a relevant market. However, in order to narrow the range of illegal unitary conduct, some limiting principles, similar to the market power requirement, are indispensable. The JFTC is aware of this necessity; thus, in its Distribution Guidelines, the JFTC established an 'influential position in a market' requirement for the majority of sections in General Designation<sup>54</sup> (GD) on UTPs, with regard to exclusionary conduct. This requirement, although weaker than the market power requirement, limits the range of circumstances that can be condemned as illegal exclusions.

Nevertheless, two of the GD Sections (Section 10 on tying and Section 15 on obstruction of competitors' business) do not have the 'influential position in a market' requirement. The reason for this omission lies in the JFTC's view that these practices fall into the second category of UTPs ('unfairness of competition methods'); UTPs belonging to the second category (tying and obstruction) are deemed inherently unfair or unreasonable.

Moreover, the regulation against 'abuse of a superior bargaining

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<sup>54</sup> *Supra* note 49.

position' (Article 2 (9) (v) as well as GD 14) is broadly applicable to exclusionary conduct. The JFTC considers this regulation to fall into a third category of UTPs ('disruption of fundamental free market order') and, therefore, 'the influential position in a market' requirement is not required.

## 5.11 Distinction between Legitimate and Illegitimate Exclusions

Exclusionary conduct, even when it creates or maintains market power ('substantial restraint of competition') is not automatically found illegal under either the monopolization or UTP clauses. Unreasonableness (or injustice) needs to be identified in the exclusionary conduct for it to be found illegal.

### 5.11.1 Identification of unreasonableness in exclusions

The JFTC decisions on monopolization have been few, which makes it hard to understand how to distinguish legitimate from illegal exclusions. The JFTC decision (hearing decision) in *NTT East*<sup>55</sup> is the only one in which the JFTC and the defendant expressed arguments on the reasonableness of an exclusionary practice in a monopolization case.

The *NTT East* case concerned a price squeeze in a regulated industry. The defendant (NTT East) operated in both the upstream market (local loop of optical-fiber cable) and the downstream market (optical-fiber based internet access service), holding dominant shares in both. NTT East sets its access fee at a level below its retail price, thus rendering it impossible for competitors in the downstream market to make a profit. Nevertheless, NTT East argued that the competitors could reduce the access fee by making more efficient use of the rented optical-fiber line by splitting it for multiple users, in the same way as NTT itself intended to do. NTT East, thus, contended that its conduct was not unreasonable from the viewpoint of 'equality of competitive conditions'. However, the JFTC found that NTT itself did not adopt the splitting method because of the small number of customers. Therefore, the JFTC found that the conduct of NTT East was unreasonable from the viewpoint of 'equality of competitive conditions'.

The 'equality of competitive conditions' argument is, in essence, equivalent to the 'equally efficient competitor test' developed in the

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<sup>55</sup> The JFTC hearing decision, 53 Shinketsushu 776 (26 March 2007), supported by Tokyo High Court decision, 56 (2) Shinketsushu 262 (29 May 2009), and Supreme Court decision, 1339 Hanrei Times 55 (17 December 2010).

US.<sup>56</sup> In two UTP (private action) cases on exclusionary conduct, the Tokyo High Court adopted this ‘equally efficient competitor test’.<sup>57</sup> The JFTC also, in its Exclusionary Monopolization Guidelines,<sup>58</sup> adopted the test in a predatory pricing case. Concomitantly, the JFTC adopted avoidable costs as the benchmark for unduly low price.

The special circumstance of the *NTT East* case – the issue of the ‘splitting method’ – makes it controversial to consider this case a precedent in ‘margin squeeze’ cases. Nevertheless, the Supreme Court, in its appeal decision,<sup>59</sup> basically regarded this case as margin squeeze, as the Court identified the essence of the case as ‘the aspect of unilateral refusal to deal or predatory pricing’. The Court, then, supported the JFTC’s finding of undue exclusion in the NTT East’s conduct. Nevertheless, the Court did not give a detailed explanation of why NTT East was judged to be engaged in either an illegal refusal to deal or predatory pricing.

### 5.11.2 Exclusive dealings and rebates

The JFTC has begun to apply the monopolization provision to exclusive dealings, although it usually utilizes the UTP prohibition.

US and EU competition law show that exclusive dealing (and similar market foreclosing conduct) should be scrutinized in relation to (1) the degree of market foreclosure in respect of rivals, and (2) an efficiency defense. In Japan, in monopolization cases, the first point (degree of market foreclosure) has never been considered by the JFTC. The JFTC may have taken the view that exclusive dealing by a dominant company invariably exerts enough of a foreclosure effect to be identified as monopolization.

Likewise the second point (efficiency defense) has also not been considered in monopolization cases, as a result of dominant companies’ mere acceptance of the JFTC’s recommendation without raising efficiency defenses.

The JFTC *Intel* decision<sup>60</sup> concerned a rebating tactic adopted by Intel.

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<sup>56</sup> See Posner, Richard A. (2001), *Antitrust Law* (2nd edn), Chicago: University of Chicago Press, p. 194.

<sup>57</sup> *LP Gas Discriminatory Price* case, Tokyo High Court decision, 52 Shinketsushu 818, 826 (31 May 2005); *Yamato Transport v. Japan Post* case, Tokyo High Court decision, 54 Shinketsushu 699 (28 November 2007).

<sup>58</sup> The JFTC, The Guidelines for Exclusionary Private Monopolization under the Antimonopoly Act (2009), available at [http://www.jftc.go.jp/en/legislation\\_guidelines/antimonopoly\\_guidelines.html](http://www.jftc.go.jp/en/legislation_guidelines/antimonopoly_guidelines.html) (accessed 27 May 2011).

<sup>59</sup> Supreme Court decision, 1339 Hanrei Times 55 (17 December 2010).

<sup>60</sup> The JFTC recommendation decision, 52 Shinketsushu 341 (13 April 2005).

Intel Japan had close to a 90 percent share of the Japanese microprocessor market. Its main rival, AMD, had been increasing its market presence. Intel Japan, to preserve its dominant position, adopted a rebating scheme in which rebates were given only to those customers (PC manufacturers) who purchased at least 90 percent of their microprocessors from Intel. In response to this rebating scheme, the PC manufacturers acquired at least 90 percent of their purchases from Intel. Some manufacturers shifted their purchases from AMD to Intel as a result of incentives affected by the rebate scheme. The JFTC found this rebating system was in violation of the monopolization prohibition. Whether the rebating system affects efficiency was never discussed because Intel simply accepted the JFTC determination.

### **5.11.3 Predatory pricing (unjustly low price sales)**

Where a dominant company engages in a policy of unreasonably low pricing to exclude rivals, the policy is commonly known as ‘predatory pricing’. Under US and EU competition laws, predatory pricing has been considered in relation to: (1) the selection of the benchmark cost for identifying presumptively illegal low prices: average variable cost, avoidable cost, or average total cost; and (2) the identification of market power (or dominant position) for the company engaging in the predatory pricing.

Under the AMA, predatory pricing may be attached either by the monopolization provision or the UTP. In practice, the JFTC has always applied the UTP to predatory pricing. AMA Article 2 (9) (iii), together with the General Designation (GD) on UTP, explains that two types of low prices constitute illegal ‘Unjust Low Price Sales’: (1) non-temporary sales of products at prices greatly below the cost of supplying them and (2) other sales at unduly low prices. The definition of the second type of low prices is vague, potentially covering prices above cost. These two types of low prices are both illegal when they are found to ‘have the danger to cause difficulties to the business of competitors’, without ‘proper justification’ for them (AMA Article 2 (9) (iii) and GD Section 6).

In relation to the first universal issue regarding predatory pricing – the selection of the benchmark cost – AMA Article 2 (9) (iii) clearly takes it as the average total cost. Nevertheless, the low price should be greatly below cost (for a type 1 low price) or an unreasonably low price (a type 2 low price).

The JFTC does not opt for the Areeda-Turner test adopted by the US courts that never finds prices above incremental cost (measured by average variable cost) as illegal. The current position of the JFTC is similar to that of the European Commission, which may find a price below the average

total cost (but above the average variable cost) illegal, when intent to harm competitors is found.

The JFTC, in its recently revised Unjust Low Price Guidelines,<sup>61</sup> adopted the same standard as that of its Exclusionary Monopolization Guidelines,<sup>62</sup> namely ‘the equally efficient competitor test’, and consequently the JFTC adopted the avoidable cost as the unduly low price benchmark.

#### **5.11.4 Discriminatory pricing**

The JFTC may find price differentiation illegal, even when it does not amount to illegal low pricing. This is derived from AMA Article 2 (9) (ii), which defines illegal discriminatory practices as: ‘Unjustly supplying goods or services continuously for a consideration which discriminates between regions or between parties, thereby tending to cause difficulties to the business activities of other entrepreneurs’.

Article 2 (9) (ii) considers price discrimination to be an exclusionary practice,<sup>63</sup> but treats it as distinct from unjust low pricing. Therefore, the JFTC has found price discrimination illegal even when the price is not below cost. The newly revised Unjust Low Price Guidelines<sup>64</sup> explain that the ‘[Illegality of differential treatment] is determined on a case-by-case basis, by comprehensively taking into consideration the intention of the person who committed the act or the purpose of the act, the extent of difference in the transaction price . . .’. The Guidelines do not apply to price differentiation the ‘equally efficient competitor test’ which is applied to undue low pricing.

The most recent JFTC decision on price discrimination is the *Yusen Broad Networks* decision.<sup>65</sup> In this case, Yusen Broad Networks Co., the largest operator in the market for ‘cable radio broadcasting for businesses’, selectively reduced its price to customers of its largest competitor, and thus induced a large number of such customers to switch from the

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<sup>61</sup> The JFTC, Guidelines Concerning Unjust Low Price Sales under the Antimonopoly Act (revised 18 December 2009). Retrieved from [http://www.jftc.go.jp/en/legislation\\_guidelines/ama/pdf/unjustlowprice.pdf](http://www.jftc.go.jp/en/legislation_guidelines/ama/pdf/unjustlowprice.pdf) (last accessed 27 May 2011).

<sup>62</sup> *Supra* note 58.

<sup>63</sup> General Designation (GD) Section 3 covers price discrimination (and other discriminatory treatment) which is not covered by the AMA 2 (9) (ii). According to GD Section 3, the JFTC may find price discrimination illegal even when it is not exclusionary.

<sup>64</sup> *Supra* note 61.

<sup>65</sup> The JFTC Recommendation decision, 51 Shinketsushu 518 (13 October 2004).

competitor to Yusen. The JFTC condemned the selective price reduction as illegal monopolization under Article 2 (5).

In contrast with this JFTC decision, the Tokyo Regional Court *LP Gas Discriminatory Price* decision<sup>66</sup> opined that price discrimination needs to amount to illegal predatory pricing (unreasonably low pricing) for it to be found illegal. The court held that price differentiation is judged unjust when the seller's pricing tactics are such that equally or more efficient competitors are not able to survive in the market. This viewpoint is equivalent to the 'equally efficient competitor test'<sup>67</sup> in the US. The court then denied the plaintiff's argument that price differentiation targeted at a specific competitor should be found illegal. The decision opined that it is natural for a company to pay heed to the competitiveness of its specific competitor, in order to take customers from the rival.

### **5.12 Assessment of Effectiveness and Areas for Improvement in Unilateral Conduct Regulation**

The JFTC has significantly improved its unilateral conduct regulation through the recent issuance of the Exclusionary Monopolization Guidelines as well as the amendment of the Undue Low Price Guidelines, resulting in considerable convergence with the EU standard.

Nevertheless, overlapping applicability of the monopolization prohibition and the UTP rule has caused unnecessary complications. Following the trend exhibited in the recent JFTC Guidelines, the JFTC needs to further streamline the applications of the monopolization and UTP rules, prioritizing monopolization clause.

The most troublesome application of the UTP provision results from the second and third types of UTPs ('unfairness of competition methods' and 'disruption of fundamentals of the free market order', namely abuse of a superior bargaining position). These types of UTPs, due to their lack of limiting principles, lead to arbitrary findings of illegality.

Types II and III UTPs have been predominantly regulated from the objective of either direct protection of consumers or the protection of SMEs. These provisions have come about due to social needs in Japan. First, consumers need to be protected from misleading advertisements as well as from unfair marketing methods. Second, SMEs are protected, in Japanese society, through various governmental measures,

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<sup>66</sup> *LP Gas Discriminatory Price* case, Tokyo Regional Court decision, 1855 Hanreijiho 88 (31 March 2004).

<sup>67</sup> Posner (2001).

partly due to general political support for SMEs by the population and partly due to SMEs' disproportionate political power. However, implementing these protections via AMA enforcement has compromised the AMA's primary objective – namely maximization of consumer welfare through the competitive process. Therefore, regulation of types II and III UTPs should be decoupled from the AMA and should be achieved through other policy instruments, such as consumer protection policy or SME promotion policy within clearly defined boundaries. Such examples already exist in the form of the Act against Unjustifiable Premiums and Misleading Representations, as well as the Act against Delay in Payment of Subcontract Proceeds, etc.

As to the substantive rules on unitary exclusionary conduct, the 'equally efficient competitor test' has come to be highlighted as the most important criterion for judging the unreasonableness of unitary (exclusionary) conduct. This is a welcome improvement as this criterion is much more objective than the ambiguous unreasonableness test.

However, the 'equally efficient competitor test' should not be applied to unilateral refusal to deal, as enterprises need to be given the freedom to refuse to deal. Otherwise, investment and innovation incentives may be lost. The JFTC and courts need to clarify, in future cases, how to identify exceptional circumstances in which unilateral refusal to deal (as well as 'margin squeeze') should be considered illegal.

The JFTC's condemnation of discriminatory pricing is prone to false positives (over regulation) since the JFTC does not apply the 'equally efficient competitor test'. Discriminatory pricing needs to be regulated as predatory pricing, to which the 'equally efficient competitor test' should be applied.

## **5.13 Mergers**

### **5.13.1 Pre-merger notification and merger review procedure**

Companies engaging in mergers (including stock acquisitions) of a substantial scale (those where the assets of one of the parties exceed 20 billion yen and of the other 5 billion yen) are obliged, under the threat of punishment, to pre-notify the JFTC (prior to consummation of merger).<sup>68</sup> The JFTC is mandated to complete the merger assessment within 30 days, which may be extended by an additional 90 days.<sup>69</sup>

However, merging companies and the JFTC have de facto established

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<sup>68</sup> AMA Article 10 (2), 15 (2).

<sup>69</sup> AMA Article 10 (9), 15 (3).

a system in which merging companies seek consultations with JFTC officials before filing mandatory pre-notifications. Through informal consultation, companies can obtain an opinion regarding the legality of the merger, thereby, if necessary, taking measures to rectify any possible areas of concern arising from a proposed merger. This custom has become so well established that the JFTC had, before changing to a new system in June 2011, issued only one formal merger decision since the inception of the AMA.<sup>70</sup>

This informal pre-notification consultation does not accord with the practice in the US and EU, which have established formal phase I and phase II procedures. Japanese companies previously welcomed the informal consultation process, but recently business circles have begun to criticize the informal consultation as being too lengthy since, under the informal consultation procedure, the JFTC faces no time constraint. In response to this criticism, the JFTC, in June 2011, abolished the pre-consultation process and adopted the formal procedure mandated by the AMA: a phase I period of 30 days and a phase II of 90 days.

### 5.13.2 Market power test

The JFTC, in its merger guidelines ('Business Combination Guidelines'<sup>71</sup>) adopted the same market power test as is used in the US and the EU. The AMA itself provides that mergers (including business combinations through stock acquisitions) are unlawful when 'the effect of the merger may be substantially to restrain competition in a particular field of trade' (AMA Article 10, 15). 'Substantial restraint of competition' has been interpreted by the JFTC and the courts as the power to substantially influence price and other market conditions.<sup>72</sup> The recent Supreme Court decision interpreted it as the 'formation, maintenance, or strengthening of market power'.<sup>73</sup>

This is, in essence, the same as the market power test that is applied in the US Horizontal Merger Guidelines. Merger regulation in Japan is an area which most closely follows the emerging global standard initiated by

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<sup>70</sup> *Yawata/Fuji (Nippon Steel)* case, the JFTC hearing decision, 16 Shinketsushu 46 (30 January 1969).

<sup>71</sup> The JFTC, Guidelines to Application of the Antimonopoly Act Concerning Review of Business Combination (2004, revised 2007 and 2009), Retrieved from [http://www.jftc.go.jp/en/legislation\\_guidelines/ama/pdf/Revised\\_MergerGuidelines.pdf](http://www.jftc.go.jp/en/legislation_guidelines/ama/pdf/Revised_MergerGuidelines.pdf) (last accessed 28 May 2011).

<sup>72</sup> *Id.* at §III. 1 (1), which follows the Tokyo High Court's *Toho/Shintoho* decision (7 December 1953).

<sup>73</sup> *Supra* note 43.

the US and EU and promoted by the International Competition Network (ICN) and the OECD.

### **5.13.3 Unilateral market power**

Instead of the former outmoded standard, the JFTC, in its 2004 Business Combination Guidelines, adopted an economics-oriented explanation for unilateral market power: when competitors, other than the dominant merged company, have only limited sales or production capacities, those competitors do not have production capacity to fully meet the increased demand for their merchandise caused by a merged company's price rise without increasing their prices; therefore, the merged company obtains power to unilaterally affect the price of the product.<sup>74</sup>

Within the concept of unilateral market power, following the concept contained in the US Horizontal Merger Guidelines, the 2007 Guidelines additionally adopted the notion of unilateral market power regarding differentiated products.<sup>75</sup>

### **5.13.4 Coordinated market power**

In recent consultation cases, the JFTC has increasingly resorted to oligopolistic coordination as a reason to block mergers. The JFTC Business Combination Guidelines incorporate the idea of market power caused by coordination: when a horizontal merger reduces the number of competitors in a market, the concentrated market, together with the characteristics of the product and transaction practices, enables companies to predict each other's reactions with a high degree of precision; therefore, such companies are able to profitably engage in coordinated activities.<sup>76</sup>

The best example of oligopolistic coordination as a reason for preventing a merger is that of *JAL (Japan Airline)/JAS (Japan Air System)*.<sup>77</sup> This case concerned the merger of the second and third largest firms in the Japanese air transport market. The largest company, outside the merger, was ANA (All Nippon Airways). In addition, the most profitable route (Tokyo to Fukuoka) included a new entrant (Skymark) with a small market share, operating alongside the three leading airlines. This merger, then, would have reduced the number of major competitors from three to two (with one fringe company). The JFTC noted in a published statement

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<sup>74</sup> The JFTC Business Combination Guidelines, at §IV. 4 (1).

<sup>75</sup> Id. at §IV. 1 (1) b.

<sup>76</sup> Id. at §IV. 1 (2).

<sup>77</sup> *JAL (Japan Airline)/JAS (Japan Air System)*, the JFTC consultation case (26 April 2002).

that airfares were already being coordinated, and a reduction in number of major competitors from three to two would make price coordination easier.

In response to the JFTC opinion, the merging parties suggested remedial measures: a pledge to assist new entrants by the transfer of landing slots and assistance with aircraft maintenance. In addition, the merging companies would reduce their fares with major air routes. Accepting these measures, the JFTC allowed the merger to proceed.

However, it is doubtful whether the remedial measures were sufficient to counteract the merger's anti-competitive nature. In particular, a reduction in airfares exerted no positive effect on competition. JFTC might have considered the price reduction as a kind of efficiency defense, but it did not give any explanation of its reasoning.

### 5.13.5 Market delineation

To identify market power ('substantial restraint of competition' in the AMA terminology) resulting from a merger, JFTC has relied heavily on the market shares of the merging companies, or on the market concentration ratio of the relevant market. Delineation of a relevant market, therefore, greatly affects whether or not a merger is considered to create or enhance market power, resulting in the merger being blocked.

Delineation of the relevant market is a common crucial factor in the application of the AMA provisions, in which market power (substantial restraint of competition) is a crucial element in the determination of violations: horizontal agreements (unreasonable restraint of trade), monopolization and mergers.

The JFTC, in the same way as the US and EU authorities, delineates a relevant market from the viewpoint of a product's substitutability for consumers.<sup>78</sup> The supply-side response is also considered.<sup>79</sup>

In line with the emerging global standard initiated by the US and the EU, the JFTC Business Combination Guidelines adopt the hypothetical monopolist test (or SSNIP test) to delineate both product and geographical markets. Nevertheless, the test cohabits with the traditional method of delineating markets: examination of the similarities in utility and usage of the product. In published merger consultation cases, the JFTC has mostly utilized the traditional method.

For geographical market delineation, JFTC had limited the market to the domestic market. Actual imports have been included in the calculation

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<sup>78</sup> Business Combination Guidelines, §II. 1.

<sup>79</sup> Id. at II. 1.

of merging companies' market share, but foreign companies' supply capacities have not been taken into account in the delineation of a geographical market. Therefore, the worldwide (or global) geographical market had never been admitted as relevant by the JFTC. However, the denial of a global market is inconsistent with the concept of hypothetical monopolist test. The JFTC in its 2007 Business Combination Guidelines changed this stance and admitted the possibility of world market delineation.<sup>80</sup>

### **5.13.6 Safe harbors on concentration ratios**

The JFTC Business Combination Guidelines do not provide a specific numeric for concentration ratios (or market shares) beyond which the JFTC is likely to identify market power. Nevertheless, the Guidelines provide safe harbors: a combination of post-merger HHIs<sup>81</sup> and incremental HHIs. For horizontal mergers, the safe harbor numbers are respectively: (a) post-merger HHIs of not more than 1500, (b) post-merger HHIs of between 1500 and 2500, and at the same time, the increment of HHIs are 250 or less, or (c) post-merger HHIs are above 2500, but the increment of HHIs are 150 or less.<sup>82</sup>

### **5.13.7 Entries, failing companies and other factors mitigating market power**

The JFTC explains in its Business Combination Guidelines that it takes into consideration the possibility of market entrants in the assessment of market power. Entry conditions are considered together with other factors mitigating market power: i.e. the impact on imports' increase, and purchasers' bargaining power.<sup>83</sup>

A failing company defense is considered as one of the elements alleviating market power. The Business Combination Guidelines explain: in a case where one of the merging partners is highly likely to go into liquidation and, at the same time, a less anti-competitive measure than the merger cannot be found, the merger generally will be considered *not* to substantially restrict competition.<sup>84</sup> This explanation on the failing company defense is qualitatively narrower than the generally accepted meaning of

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<sup>80</sup> Id. at §II. 3.

<sup>81</sup> Herfindahl–Hirschman Index (HHI) measures the concentration ratio of the industry as the sum of the squares of the market shares of the firms in the industry.

<sup>82</sup> Id. at §IV. 1 (3).

<sup>83</sup> Id. at § IV. 2, 3.

<sup>84</sup> Id. at §IV. 2 (8).

the defense, in which an otherwise illegal merger would be tolerated to save a failing company.

### 5.13.8 Efficiency consideration

The JFTC had maintained that merger regulation should exclusively aim to prevent the creation of market power. This position is based on the AMA provision on mergers (AMA Article 10, 15), which prohibits mergers that achieve market power ('substantial restraint of competition'). These provisions make no reference to efficiencies or public interest defenses.

Changing this traditional stance, the JFTC, in its 2004 Business Combination Guidelines, adopted an efficiency consideration for the first time, subsequently expanding this in the revised 2007 Guidelines. These guidelines allowed efficiencies as one of the many elements (including market entry and imports) relevant in the analyses of market power.<sup>85</sup>

The guidelines suggest that the JFTC's consideration of efficiency is equivalent to an 'efficiency defense'.<sup>86</sup> Nevertheless, the JFTC guidelines' treatment of efficiency is narrower than that of the US Horizontal Merger Guidelines, and is more akin to the EU standard in two respects: (1) accounted efficiencies are limited to those increasing consumer welfare (not producer surplus), and (2) an efficiency consideration would rarely justify a merger realizing a near monopoly.

### 5.13.9 Regulation of economy-wide concentration

As a unique feature of Japanese competition law, the AMA is equipped with a prohibition against economy-wide concentrations, distinct from merger regulation in each market. This rule had an historical importance because it was established at the inception of the AMA, with the goal of preventing the revival of the concentrated economic power held by owners of the giant holding companies (the *Zaibatsu*) in the era before Japan's defeat in World War II.

However, over the course of the post-war economic growth, this rule has gradually lost its relevance, because the uniquely Japanese characteristics of the economy – interlocking stockholdings etc. – have gradually diminished.

The Diet and the JFTC, through legislation and practice, have gradually reduced the scope of this rule. Most notably, the prohibition on pure

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<sup>85</sup> Id. at §IV. 2 (7).

<sup>86</sup> Business Combination Guidelines treat efficiency as a 'pro-competitive effect' in that an efficiency increase achieved by the merged company may increase the merged company's competitive conduct (Id. at §IV. 2 (7)).

holding companies (which had formed the core of the economy-wide concentration regulation) was lifted in the 1997 AMA amendment. The AMA clauses on economy-wide concentration currently consists of (1) regulation of ‘excessive concentration of economic power’ (AMA Article 9) and (2) regulation of stockholdings by banks and insurance companies (Article 11). Both prohibitions are narrowly construed in order to limit the discretion of the JFTC.

#### **5.13.10 Assessment of effectiveness and areas for improvement in merger regulation**

The JFTC’s merger regulation is the area of the AMA most closely in accord with the best-practice standard exhibited by the US and EU, as reported by the ICN and OECD. Nevertheless, the JFTC’s constant use of the informal consultation system has rendered the merger examination opaque. The JFTC’s adoption in 2011 of a formal system of phase I and phase II examinations is a great improvement in making merger examination more transparent, as well as speedy.

In relation to market delineation, the JFTC needs to increase the usage of the hypothetical monopolist test, because the traditional test (similarity in usage and utility) leads to arbitrary delineation of markets and is biased in favor of the regulators. The objective test for market delineation is particularly vital with regard to geographical markets, because an increasing number of mergers have involved global players, i.e. the merger of Nippon Steel/Sumitomo Metal (2011).<sup>87</sup> The JFTC was pressed to properly delineate geographical market in order to accurately take into account companies outside Japan.

Regulation of economy-wide concentration no longer has relevance, as recent refinements in the JFTC’s merger regulation have realized effective regulation of market concentrations. Furthermore, the special conditions of the Japanese economy that justified regulation of economy-wide concentrations have largely disappeared.

## **6. OUTLOOK OF COMPETITION LAW AND POLICY**

The Japanese economy has stagnated for more than two decades. Japan has lost its top tier status among the advanced economies, with its GDP

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<sup>87</sup> The JFTC approved this merger with conditions on 14 December 2011. See <http://www.jftc.go.jp/en/pressreleases/archives/individual-000457.html> (last accessed 15 December 2011).

per capita ranked 24th in the world, and its competitiveness ranked as mediocre. Japan needs to reform its society and economy in order to revitalize itself. To achieve this objective, an increase in competition is a key factor. The inefficiency of the Japanese domestic economy is evidenced by the low productivity of its agriculture and service sectors as well as its domestic industries, which are largely shielded from competition. The devastating combination of an earthquake, tsunami and nuclear accident in March 2011 is expected to energize both the people and the government to accomplish the necessary reforms.

The Japanese political system has been ineffective in checking special interests. Nevertheless, Japan's membership in the WTO (and other international institutions) obliged Japan to observe free trade, thus opening Japanese manufacturing to international competition, resulting in globally strong manufacturing companies. Yet the WTO has proved insufficient to open up the agriculture and service sectors – Japan's weak points. In order to bring competition to agriculture, services and domestic industry, the Japanese government should enter into FTAs with the US, EU, China and other major economies. The first step is now envisaged to be participation by Japan in the Trans-Pacific Partnership (TPP) – an FTA currently being negotiated, which currently has nine member participants, namely the US, Australia, Vietnam and several Asian countries.

As for the competition law, which is the focal point of competition policy, the AMA has basically functioned effectively in checking anti-competitive conduct. From a global perspective, the AMA has been able to prevent anti-competitive interference from various industrial policies. Moreover, the AMA is broadly applicable to business activities by national and local governments. These merits need to be preserved.

Nevertheless, the AMA and its enforcement by the JFTC have been revealed to have serious weaknesses. These are summarized at the end of each subsection of Section 5. Most importantly, the use of the unfair trade practice (UTP) prohibition needs to be drastically curtailed by removing a large part of UTP regulation to legislation separate from the AMA. Second, the penalty system needs to be reformed to allow the JFTC discretion over the amount of fines as well as whether to levy fines or not. Third, the JFTC needs to establish new guidelines on horizontal and vertical restraints.

As a prerequisite for AMA revisions and new guidelines, the Diet, the government and the JFTC need to firmly establish that the objective of the AMA is to maximize consumer welfare. The current ambiguous objective of the AMA has engendered a preoccupation with the interests of politically powerful SMEs. Most typically, the 2009 AMA amendment excessively extended fines in order to benefit SMEs, thus

compromising sound economic logic and consequently sacrificing consumer welfare.

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