COUNTRY STUDIES

Japan – Monitoring Review

2004

Introduction

The Review is one of a series of country reports carried out under the OECD's Regulatory Reform Programme, in response to the 1997 mandate by OECD Ministers. This report on the role of competition policy in regulatory reform analyses the institutional set-up and use of policy instruments in Japan. It is monitoring developments since the 1999 OECD Report on Regulatory Reform in Japan, with particular attention to the implementation of its recommendations. This report was prepared by Mr. Michael Wise for the OECD.

Overview

Related Topics

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REGULATORY REFORM

-- Monitoring Review of Japan --

Competition delegates will find attached FOR INFORMATION the final version of the monitoring report of Japan. It was revised in light of the Committee's review in June 2004 and to include some factual changes.

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REGULATORY REFORM

MONITORING REVIEW OF JAPAN

1. This Report is part of the monitoring of developments since the 1999 OECD Report on Regulatory Reform in Japan ("1999 Report"), with particular attention to the implementation of its recommendations. Japan has made substantial progress in the most important competition policy areas that were highlighted in the 1999 Report. Key issues identified at that time included the scope of exemptions from competition law and non-competitive tendencies in regulation, including the penchant for administrative "supply-demand" balancing to control entry and administrative guidance to encourage industry co-ordination. The 1999 Report recommended that regulators and sectoral ministries, including those in traditional monopolies such as telecoms, electric power and transport, be given a mandate to support competition. For the competition enforcement agency, the Fair Trade Commission (FTC), the 1999 Report called for increasing its independent policy stature and improving its resources, more transparency in its decisions and reasoning and expanded co-operation with other enforcers. To expand the scope of enforcement, the 1999 Report recommended stronger private rights of action, which could be supported by ending the quota limiting the size of the legal profession. Finally, the 1999 Report called attention to the undeveloped linkage between competition policy and consumer issues.

2. This monitoring report follows the same outline as 1999 Report, dealing with substantive law and application, institutions, coverage and policy issues. The recommendations of the 1999 Report and developments related to their implementation since 1999 are highlighted in boxes. Progress in the reform of economic regulation is demonstrated by the removal from most sectors of supply-demand balancing as a consideration for controlling entry and the elimination of most exemptions from the competition law. Notably, removing the exemption for "inherent monopoly" has permitted the FTC to take more enforcement actions in regulated network industries. The FTC's independence was underlined by moving it to the Cabinet office in 2003. The FTC has a new economic unit (the Competition Policy Research Centre) and substantially more resources, most of them dedicated to investigation and enforcement. A new law takes some steps against administrative tolerance of collusion, by giving the FTC new powers to deal with official involvement in bid-rigging. Private suits are now authorised to seek orders as well as damages, and many have been attempted. The March 2004 Cabinet Decision concerning the 3-year regulatory reform plan shows continued government support for active competition policy to make markets function effectively.

3. Improving the enforcement of competition law is now a high priority. The FTC's principal enforcement target for the last several years has been bid rigging, one of the most serious problems in the domestic political economy. Results have been mixed. A major prosecution that was filed in 1999 was finally concluded with convictions in March 2004. The next one to be brought was referred for prosecution in late 2003, against repeat offenders, and also resulted in convictions. A change in the law appears to have made sanctions much stronger, because the maximum fine for corporations was increased from ¥100 million to ¥500 million, but until prosecution becomes a more serious threat, the increase is a symbolic gesture. Repeat offences and the persistence of *dango* bid-coordination show that deterrence still falls short, despite the efforts of the last 10 years to strengthen the system. A Study Group on the Antimonopoly Act recently undertook a comprehensive review of the entire system of administrative and criminal remedies. The Study Group Report, issued in October 2003, recommended major reforms to the

enforcement system. The most important would be to revise the system of financial penalties imposed in the administrative process, to authorise impositions that are more consistent with the sanctions that are being applied now in other major jurisdictions.

Substantive law and applications

4. The fundamental substantive rule of the Antimonopoly Act (AMA) prohibits "private monopolisation or unreasonable restraint of trade" (Sec. 3). In practice, the most important element has been the prohibition against restraints of trade, which is the strongest law the FTC can apply against horizontal price fixing and bid rigging agreements. Although horizontal price-fixing is considered anti-competitive "in principle" (by the FTC's Guidelines), the FTC may still need to show that the restraint has been significant or that it has had some actual effect. This requirement makes enforcement more difficult than it is in jurisdictions with a true *per se* rule against horizontal price fixing.[1] Trade associations, a common location for horizontal restraints, are subject to a particular prohibition against imposing any "substantial restraint on competition."[2] For nearly all other kinds of competition issues, the FTC relies principally on the section of the law that prohibits "unfair practices" (Sec. 19). Here the burden of proof is lower, but the only sanction the FTC can impose is an order to correct the violation. The FTC uses Sec. 19 for cases ranging from distribution restraints, discrimination and tying to refusals to deal and exclusion.[3]

5. The AMA also contains rules aimed at the particular risks to competition due to the positions of unusually large firms, but most of these rules are not used. There have been only 15 cases in more than 50 years invoking the AMA's prohibition of "private monopolisation" (Sec. 3), which is analogous to other jurisdictions' prohibition of abuse of dominance. It appears that the FTC typically deals with large-firm abuses as unfair practices. This approach, which does not involve extensive evidence about market power and effects, preserves enforcement resources for horizontal matters, but it may also be less effective at curbing monopolising practices than the prospect of fines or divestiture that enforcers can employ in Europe and the US. Restructuring and divestiture of monopoly firms appear to be authorised by the special rule for a "monopolistic situation" (Sec. 8-4), but this has never been used. Especially if this static, formalistic provision is repealed, consideration should be given to authorising divestiture and similar structural remedies in appropriate cases brought under Sec. 3, as the Study Group recommended.[4] Repeal of the "inherent monopoly" exemption from the AMA in 2000 has enabled the FTC to pay more attention to issues of network access. Notably, the FTC has examined claims that the incumbent telecoms firms were discriminating against entrants about ADSL facilities, services and pricing practices.

6. The Study Group Report included proposals for further changes to the law about dominant firms. The AMA's rules about parallel pricing in concentrated industries have not proven to be useful or important in practice, and these should be eliminated. The other principal recommendation in this area was to authorise the FTC to order access to "essential facilities." Although this basis for regulating discrimination and refusal to deal has parallels in several other jurisdictions, defining the circumstances in which a firm has a duty to deal with customers and with potential rivals is a complex and controversial task. The issue is likely to receive further study before any formal proposal appears for new legislation. One common setting for these controversies is traditional "network" monopolies such as energy, telecoms and transport, but issues in many other industries, from financial services to software, can also be framed in the same terms. In principle, the FTC could already deal with such conduct under Sec. 3. To be sure, many cases about these subjects under Sec. 3 would be complex and time consuming, and remedies could be difficult to craft. There may be some controversy about whether Sec. 3 could support an order to restore or create conditions supporting competition, for example through information disclosures. The complexity of the issues and remedies are also reasons to proceed carefully in designing statutes to deal with the problems. Indeed, if the FTC brought more Sec. 3 cases against monopolising conduct, there would be a broader base of experience on which to draw for that purpose. The FTC might facilitate the process by developing guidelines about the interpretation of Sec. 3 in these circumstances.

7. Merger standards, as set out in the FTC's Guidelines, are being revised. The AMA's merger control rule prohibits mergers whose effect may be substantially to restrain competition in any particular field of trade. The guidelines adopted in 1998 describe structural conditions that would normally permit a merger to proceed without further inquiry: post-merger market share under 10%; or, under 25%, if the industry is not oligopolistic, the merged firm is not the top-ranked firm and entry, including through imports, is easy. On the other hand, the Guidelines imply that 3-firm concentration greater than 70% would typically be a cause for concern, for horizontal mergers. For vertical or conglomerate mergers, there are no structure-based presumptions or safe harbours. New merger guidelines were issued for in May 2004. Among other things, these incorporate the HHI index that is used now in other major jurisdictions and set out general safe harbours based on market share and structure that would apply to all kinds of mergers.

8. The process of pre-notification consultation about mergers has been clarified. Under the statutory scheme, merging parties must notify the FTC of their plans and wait 30 days from that time before proceeding. After a size threshold was added to the AMA in 1998,[5] the number of mergers requiring prior FTC approval dropped by 90%. This notification and waiting process is not usually the occasion for examining and deciding upon the transaction, though; rather, application of merger control relies on prior consultation and negotiated correction where necessary, as parties to mergers that might raise problems seek to avoid the risk that the FTC will block their plans after they enter the formal statutory procedure. The FTC's December 2002 policy statement about consultation aims to clarify the informal process by setting a timeline for advising the parties whether a merger requires more serious investigation and possibly relief. These are targets, not legally binding deadlines on the FTC's actions. Nonetheless, this commitment represents a step toward the kind of 2-phase investigation process that is becoming standard in other major jurisdictions, and it seeks greater transparency. A condition for following the consultation process set out in the policy statement is that the parties agree that the FTC will explain its action publicly at the end of the process, even if it advises the parties that it has problems with their proposal.

Box 1. Transparency

Publicise actions and reasoning, to educate the public and the business community about the effects and benefits of competition policy and law enforcement.

Already in 1999, the FTC was taking steps to deal with long-standing concerns of lack of transparency, by issuing detailed, updated guidelines based on its actual decisions, and by devising ways to explain to the public the cases it has disposed of without formal decisions. The Report urged the FTC to continue its efforts to explain its decisions and to open up its own regulatory process, in part to be a model for other ministries to study. Detailed explanations of FTC decisions would assist businesses in understanding their obligations and develop public support for competition enforcement by demonstrating how it protects the public interest.

The results of this effort become clear in 2001, when the extent of information announced about FTC actions and policies increased notably, particularly for non-Japanese observers. Mergers are a matter of particular interest. Because the review process is non-public, it had been difficult to identify transactions that might have been rejected. There has only been one formal FTC decision rejecting a merger in more than 35 years. Increasingly since 1999, the FTC has tried to publish outlines explaining its treatment of merger matters. In 2002, for the first time, the FTC issued a release in connection with a consultation in which it told the parties that it had concerns which caused the parties to abandon their plans. The proposed consolidation would have produced a near- monopoly in certain key components of paper-making machinery; on hearing that the FTC would object, the parties withdrew their application. The FTC also issued several other releases in 2002 explaining corrective measures and undertakings that it had negotiated in connection with mergers that were ultimately permitted.

An important part of the new consultation process is that the FTC wants to make its actions public—something that merging parties themselves may not want, even though it is valuable for the public at large. The merger consultation process and the basic statutory review process are consistent with the "no-action letter" system that the government introduced in 2001, to encourage prompt, public responses to requests about application or interpretation of laws and regulations.

9. Unfair competition is an important part of the FTC's work; some, but not all, of this enforcement agenda is related to consumer protection. Under the AMA, the FTC has many cases about sales at prices that are "unjustly" low, which are typically competitor complaints about their rivals' price-cutting. Most cases against "unjust low price sales" are about sales below invoice price, most are resolved by warnings or cautions, and most involve the liquor industry—in 2001, there were 2500 in that sector alone—and gas stations. The FTC explains its disproportionate attention to the liquor industry, which includes formal guidelines about price cutting, because prices in that sector were deregulated in 2000, and the industry was struggling to adapt to the new conditions. The FTC enforces legislation to protect small businesses by preventing abuses of bargaining power in subcontracting transactions. The Premiums and Misrepresentations Act regulates misleading advertising and unjustifiable premium offers by treating them as a form of unfair competition. Even against misrepresentations that actually harm consumers, an order is the strongest remedy the FTC can impose in these cases.[6] Applying the Premiums and Representations law involves a degree of industry self-regulation, through nearly a hundred fair trade associations and their fair trade codes. The FTC authorises and monitors these institutions and attends their annual meetings. They have been used to establish industry-wide standards about what practices would be considered fair under this legislation; the FTC would like them to concentrate on consumer protection and complaints about misleading advertising.

Box 2. Consumer-competition policy link

Establish a clear, public, effective relationship between consumer policy and competition policy.

The 1999 Report recommended that competition policy be connected more clearly to consumer policy. This might require setting up a stronger authority for consumer protection matters. Alternatively, the relationship might be underscored by assigning to the FTC the responsibility for implementing a market-oriented consumer protection policy complementary to the AMA. The Report noted that this could be built on the FTC's responsibility for special statutes, such as those concerning premiums and representations, and on provisions of the AMA that can be conceived in terms of consumer protection policy.

Japan does not yet have a comprehensive consumer protection law or enforcement authority, other than these functions of the FTC. To the extent there are agencies and NGOs with interests in consumer issues, there has been some effort to recognise common interests and co-ordinate actions. The Study Group on Consumer Transactions made some proposals in 2002 of items that the FTC ought to address in the context of consumer transactions. And there have been some exchanges with the "quality of life" policy bureau and the National Consumer Affairs Centre of Japan about consumer transaction issues. New provisions about consumer protection are under consideration.

Institutions and processes

10. The FTC was created as an independent body. For several years, the perception of its independence was compromised by its position as an external organ of the Ministry of Public Management, Home Affairs, Posts and Telecommunications. The issue became more acute as changes in law meant that FTC could take more enforcement action in industries that this ministry regulates. To overcome that perception of conflict, and to re-enforce the FTC's enforcement independence, in 2003 the FTC was made an "extra ministerial body" of the Cabinet Office.

Box 3. FTC status

Increase the visibility and impact of FTC participation in policy-making.

Establishing a forum for discussing and clearly deciding about matters that affect competition in the context of overall economic policy is critical for reform to succeed. The 1999 Report called for the FTC to become in fact what it is in theory, the principal "horizontal" authority responsible for assessing as well as applying competition policy. This would require preserving the FTC's independence from political direction while permitting it to take a more central role in policy formation. The Report suggested that the FTC could build on its then-current roles under the deregulation program and the Deregulation Council, as well as its existing statutory responsibilities and opportunities for consultation.

The move to the Cabinet Office implies a potentially stronger role in government-wide reform. That prospect is probably more important than correcting the appearance of conflict in its previous position attached to the ministry. But it remains a promise, as the FTC role in policy matters appears to be about the same now as it was in 1999.

Other organisational connections to reform, notably to the Council on Regulatory Reform, also remain works-in-progress. Although there had been discussion at the time of the 1999 Report about a formal relationship between the secretariats of the FTC and CRR, that was not actually put in place. The relationship between the 2 institutions is nonetheless good. The CRR Report issued 2 years ago recommending strengthening the FTC led to the Study Group Report and the proposals about enforcement that are now under consideration. The new regulatory reform structure again envisions a connection with the FTC. The chairman of the FTC would be a member of the government "headquarters" unit, supporting the advisory board.

Although the FTC will be involved in the new reform format, some consider it more important to participate in the behind-the-scenes inter-ministerial consultations. It may be that low-key, non-public advice can achieve results on particular projects and build trust within the bureaucracy. It does little, though, to develop public awareness of the relationship between regulation and competition.

11. The FTC has concentrated its attention on the violations which cause the greatest economic harm, namely horizontal cartels and bid rigging. The FTC has tried to keep abreast of novel policy challenges, such as competition issues in areas subject to social regulation, sectors undergoing deregulation and problems of high technology and intellectual property rights. A special unit about information technology and public utility businesses was set up in the Investigation Bureau in 2001; this unit has produced cases in electric power, bus transport and telecoms. But traditional topics remain the mainstays of its enforcement practice. The most common complaint received at the FTC is about excessive discounts in retailing (that is, "too much competition"), while the most frequent target of actual enforcement action is bid-rigging in construction. The number of formal actions peaked in 2001, at 42. Since 1999-2000, the annual total of sanctions imposed (as surcharges) has dropped substantially—from ¥18,433 million to only ¥2,700 million in 2002—perhaps because parties are insisting on taking cases to full hearings rather than pay the surcharge demanded.

Box 4. FTC Resources

Improve the FTC's economic and legal resources, to enable it to undertake more sophisticated merger and monopoly enforcement, prepare more successful cartel cases and resolve market access problems.

To support increased FTC attention to cartels and bid-rigging, and also to do economically sophisticated cases about mergers and dominance, the 1999 Report recommended that the FTC deepen staff expertise and improve the mix of skills, with greater emphasis on both economic analysis and on investigative and legal techniques.

Overall, the resources available for competition enforcement have continued to increase. The FTC's budget has grown more quickly than that of the government as a whole. Even so, they may still be insufficient, in kind if not in amount, for dealing with an economy as large as Japan's. The budget for FY2004 calls for an FTC staff totalling 672, compared to about 607 in 2002 and only 478 in 1991. Most of the additional staff hired in the last few years have been investigation officials. Not all are involved in competition policy and enforcement, though, because the FTC is also responsible for deception, marketing and subcontracting cases. The FTC contends that it still needs several hundred more people for AMA enforcement. Government-wide administrative reform policies impose ceilings on staff increases, so the FTC would need to justify an exception from the ceiling on the grounds that it would be consistent with the purposes of the reforms.

More important than the number of staff, though, is their expertise profile. This is improving, but here too more remains to be done. The FTC still has only a few graduate-degree economists on its staff. To facilitate contacts between the FTC and academic experts, in 2003 the FTC established the Competition Policy Research Centre within its General Secretariat. The head of this Centre is Prof. Kotaro Suzumura, of Hitotsubashi University. It is staffed now by eight economists and six legal scholars. The 1999 Report also suggested bringing in experienced prosecutors and other legal experts. A judge is now assigned to be the vice-chair of hearing bodies. In addition, the FTC staff now includes 3 prosecutors, seconded to the FTC to work on investigations and litigation, plus 3 attorneys to work on hearings and one to work on litigation.

12. Some aspects of the administrative enforcement process seem informal, but that represents a realistic accommodation to the delays and costs of full proceedings. Most enforcement orders and financial sanctions are imposed through "recommendation" decisions, which are issued when the parties do not contest the FTC's claims and proposed relief. If the respondent rejects the recommendation, the case goes to a hearing process, presided over by another official (or even the FTC itself) in order to separate the functions of prosecution and decision-making. The hearing process can take 2 years or more to produce a decision by the FTC, which might then be appealed in court. The full hearing process takes too long for time-sensitive matters such as complaints about network access; because delay is intolerable, these must often be resolved with only a non-binding warning. Parties are increasingly demanding hearings in order to contest surcharge calculations. There were over 150 hearing cases pending at the end of 2003, compared to 35 in 1998 and 91 in 2002. The Study Group made proposals to streamline proceedings, and several are included in the plans for amendment that the FTC announced in April 2004. One would be to streamline the process, eliminating the "recommendation" step and moving directly to an order; this would entail creating some additional due process protections for parties at that stage. To reduce somewhat the party's incentive to appeal simply to delay payment of surcharges, interest due on the amount imposed would accrue during the appeal. And the FTC's orders would be backed by stronger sanctions against companies that violated them.

Box 5. International cooperation agreements

Improve capacities to address international competition problems by reaching agreements with other countries on cooperation and enforcement.

The 1999 Report recommended greater use of bilateral co-operation agreements with other major international competition agencies. Without clear arrangements with the enforcement authorities of its major trading partners, the FTC will be at an increasing disadvantage in taking accurate, timely action in enforcement matters with significant international dimensions.

Since then, Japan has reached agreements with the US (1999), Singapore (2002) and the EC (2003), and is discussing agreements with others, including Canada. The agreements typically call for notification, cooperation, coordination, request for enforcement action and consideration of the important interest of the other government. Such agreements are clearly leading to expanded co-operation and co-ordination with other enforcers. In one world-wide price-fixing investigation in 2003, searches and interviews were co-ordinated among enforcement officials from Japan, the US, Canada, and the EC. (Hammond, 2003)

Sanctions for violations and proposals for reform

13. The enforcement system has many elements, some of them not very effective. The FTC's own proceedings can result in cease and desist orders ("elimination measures"), and, for certain violations involving effects on price, in a financial imposition, termed a "surcharge." If a case is referred to the prosecutor, at the end of the criminal trial a court could impose criminal fines or even imprisonment. Parties can seek civil damages, and they can now seek court orders too. And there are some special remedies for particular settings, such as termination of subsidy payments and disqualification from bidding. Thus, the law seems to threaten violators with many consequences. Yet reluctance actually to impose large sanctions means that deterrence is weaker than would appear. The 2003 Study Group Report focussed on this issue. In December 2003 the FTC released an outline of its response to the report, which was followed in April 2004 by a more specific proposal for amendments to the AMA to strengthen sanctions and investigative powers.

14. The principal change would be to increase the surcharge that the FTC can impose. This imposition is analogous to the administrative fines that are applied by many other competition enforcers. It is one of the most important remedial measures the FTC can employ. Surcharges are exacted for violations such as price fixing and output restriction. The surcharge is computed as a percentage of the firm's sales of the affected product during the period of the restraint. The rate is fixed by statute, and the FTC has no discretion to vary it, regardless of any other factors in the case or of the firm's actual "unjust" profits from the violation, even though the surcharge was first conceived as an administrative measure to recapture such profits. This system has advantages of certainty and simplicity, which probably make enforcement more efficient. When the surcharge system was first adopted, the rate was so low—only 1.5%—that the surcharge looked like a cartel license fee. The current rate, of 6% of covered commerce, still looks low by international standards. Deterrence is weakened further by reductions in the rate for violations by small business (to 3%) and in retail (2%) and wholesale (1%) trade.

15. The Study Group Report recommended raising the surcharge rate, although it did not recommend a particular level. The FTC's April announcement proposes that the current rates be approximately doubled. The rate would still be applied only to the commerce affected by the violation. Rates applied to small businesses and to wholesale and retail trade would also be increased, but they would remain below the basic rate. The FTC also proposes to add about 50% to the surcharge for repeat violators.

16. Amendments may also apply surcharges to a wider range of AMA violations. Now, the surcharge remedy applies to restraint-of-trade violations that are related to prices, including those that affect price by

controlling output. The FTC proposes that surcharges would be applied to a wider range of violations of Sec. 3. These would include restraints of trade about price, volume, market share or customer allocation. It would also be applied to purchasing cartels. In addition, surcharges could be imposed against those types of "private monopolisation" that, by controlling other firms, had the same price-related effect as a hard-core cartel. Fines or surcharges could be appropriate for especially egregious acts of monopolisation. This would be appropriate when applied to restrictions or exclusionary tactics that have the effect of maintaining non-competitive market conditions. It seems clear from the Study Group Report and the FTC's subsequent proposals that surcharges are not being considered as a remedy for simple exploitation of market power by charging supra-competitive prices.

17. Proposals to change the surcharge system have revived questions about the system's rationale and jurisprudential foundations. It would be unfortunate if extended debate over these issues delayed necessary strengthening of the sanction system. In concept, surcharges are an administrative measure to control or prevent conduct contrary to the AMA rules. Because the current rate is not doing so effectively, the Study Group recommended raising the rate for that purpose. The Study Group Report argued that the existing rate collects the benefit to the party, that is, the unreasonable profits, and that raising the percentage will improve deterrence by making the surcharge higher than the party's gain from the violation. This implies a belief that 6% is a sound estimate of the likely unreasonable profits from violations. The reported experiences of OECD members about hard-core cartels indicate that gains from collusion are often much higher than 6%. A financial imposition that is greater than the gain to the violator is consistent with economic theory about deterrence, to correct for the possibility that the violator could avoid detection. To reach a level that deters effectively, the rate needs to be much higher than 6%.

18. The relationships among the surcharge system, criminal penalties and private damages recoveries have drawn attention. The Study Group Report contrasted a "sanctions" system, involving discretion in setting the level of the sanction, considering the violator's culpability and the losses incurred and correcting for the likelihood of detection, with the "administrative" fixed-rate surcharge system, which is intended to have the same practical effect of economic deterrence of violations but is simpler and more certain. Because setting the surcharge by reference to unjustified gain might make it resemble the criminal sanction, the Study Group called for changing the conceptual basis of the surcharge, from taking back "unjust" profits to recovering the losses inflicted on society, including social losses from consumption foregone or distorted. Yet the Study Group Report argued that surcharges based on losses incurred by victims and society will not duplicate civil damages. The original motivation of the surcharge system in 1977 was the confiscation of unjust enrichment, to distinguish it from the criminal penalty that was already in place. The Study Group Report's concept of recovering the social loss is also a means of distinguishing the surcharge from the criminal penalty. Of course, an objection to imposing sanctions and criminal fines in the same case on grounds such as "double jeopardy" could be overcome by making some appropriate adjustment, such as applying one sum as a credit against the other. The FTC's April announcement calls for deducting half of any criminal fines from the surcharge imposed in the same matter.

19. Offsetting fines would not usually make a significant difference to the surcharge. Surcharges are a much more substantial financial deterrent, because surcharges can be much larger than fines, even at a rate of only 6%. A fine may be levied upon conviction in a criminal trial for violation of Sec. 3 or for a restraint imposed by a trade association. The highest possible fine, ¥500 million (for an organisation, such as a company), is commensurate with fines that apply to other economic crimes in Japan, but it is substantially lower than fines being imposed in many other jurisdictions now against price fixing conspiracies. Individual violators might also be punished by up to 3 years in prison and a ¥5 million fine. The practical deterrent effect of these theoretical punishments is hard to identify, because there are few criminal cases, so fines of any magnitude, against companies or individuals, are rarely imposed. Since 1990, 6 cases have resulted in fines; the highest total fines imposed in a single case, against all defendants,

was ¥460 million. Prison sentences are even rarer, and execution of sentence has always been suspended. No one has ever gone to jail for violating the AMA.[7]

20. To make enforcement effective, sanctions must be credible. A rate about double the present level would still be lower than the cap on fines in most other jurisdictions. Because the surcharge percentage is a fixed amount, it is not directly comparable to those percentage-based caps on discretionary fines. The fines that are actually imposed in those other jurisdictions are usually well below those caps. Nonetheless, comparison suggests differences in conceptions of effective deterrence. In the systems commonly found in Europe, administrative fines can be as high as 10% of total firm turnover, not just of the commerce affected. In the UK, fines can be up to 10% of turnover over the period of the violation (up to 3 years). Korea, which also conceives its administrative fine as a surcharge, intends to increase the rate to 10% of covered commerce. In several countries, sanctions may be based on the gain from the violation or the harm it caused, estimated in the individual case. In the US, the fine may be up to 2 times the gain or the loss; in Germany and New Zealand, the fine may be up to 3 times the gain. Increasing the rate in Japan will bring it more into line with these levels of deterrence.

21. A figure well above 10% of covered commerce could be justified, given the difficulties of detection and proof as well as the likelihood that gains and losses due to hard-core conduct are significantly greater. Reports from OECD Members about their experiences are instructive. The Netherlands imposed a fine that amounted to about 18% of covered commerce against a cartel in veterinary medicines; Germany, of 12% against a concrete cartel; Canada, from 11% to 20% against cartels in citric acid, lysine, vitamins and sorbates; EC, 11% against a cartel in graphite electrodes; US, 46% against a cartel in marine construction.[8] If harm resulting from the cartel is the conceptual basis for setting the level, and the harm is typically greater than the gain to the violator, and the gain to the violators from hard core cartels is typically at least 10-15% of turnover (an estimate that is supported by OECD surveys of its Members' experiences), then a fixed level of 10% of covered commerce would be on the low side.

Criminal process

22. Criminal penalties are employed to some extent, but the threat does not yet deter effectively. For several years, the FTC has announced a "crack down" on horizontal violations and a general policy of seeking criminal penalties against them.[9] Over the 40 year period before the FTC announced a stricter policy in 1990, there had been only six criminal cases; despite the higher priority, there have been only seven more since then. And at the end of the process, serious sanctions have not been applied. In the 7 cases referred since 1990, over 90 individuals were prosecuted, but execution of all of their sentences was suspended. The largest fine against a company was 80% of the statutory maximum that was then allowed (¥100 million). That level was reached for the first time in the 2004 jet fuel case. Ineffective deterrence invites repeated violations. The firms that were recently convicted of rigging bids for municipal water meters had previous convictions.

23. The capacity to prosecute price-fixing violations of the AMA appears constrained. Before the recent water meter case, the last criminal case had been filed in 1999, and it was not decided until March 2004. To be sure, it was a substantial case, against 11 firms and 9 individuals for rigging the bids to supply jet fuel to the Self Defence Agency, and all the defendants were convicted (except one firm that had gone out of business in the meantime). The Board of Audit, which uncovered this scheme in its oversight of the procurement office's role in it, estimated it resulted in losses over three years totalling ¥49 billion—a figure that is several hundred times larger than the fines that were ultimately imposed. The FTC is now pursuing dozens of bid rigging matters every year. But the prosecutors evidently can only handle one AMA case at a time.[10] That capacity should be expanded, if the AMA's criminal penalties against horizontal cartels and bid rigging are to be applied credibly. This will require overcoming two sets of problems:

prosecutors have been reluctant to accept referrals and the FTC operates under handicaps in getting the necessary evidence. (Boling 2003)

24. The FTC has sole discretion to refer a matter to the Public Prosecutor General, but it cannot prosecute itself. The referral process begins with dialogue between the FTC and the prosecutors' office, to explore whether there is enough evidence to convict, applying a "no ordinary man would doubt" standard. If it appears likely that this standard would be met, the details of the referral are worked out and it is then approved by the FTC. Criminal AMA cases are handled by the Tokyo High Public Prosecutor, which does the criminal investigation with the aid of the Special Investigations Bureau of the Tokyo District Public Prosecutor, which specialises in white collar crime and corruption cases. But the FTC's evidence is usually the core of the case (although for prosecution, much of that evidence must be re-assembled pursuant to the procedural requirements of the criminal law).

25. Prosecutors appear to have been wary of the risks of competition cases. A 2001 report about the AMA by the Research Council on Corporate Crime, set up under the Research and Training Institute of the Ministry of Justice, speculated that competition values are relative and matters of convention, that is, that violations of the AMA are not like real crimes. In addition, the report observed that seeking criminal penalties looks like redundant effort, crowding out higher priority prosecutions, if surcharges are also imposed. The FTC has difficulty obtaining the kind of evidence that could overcome scepticism. Notably, the FTC cannot prosecute refusal to comply with its investigative demands. Even if the FTC can nonetheless obtain evidence that meets its standard for administrative relief, it probably cannot get enough to meet the standard for criminal conviction. Moreover, prosecutors in Japan appear wary of taking on uncertain cases. The rate of successful convictions (for all crimes) is over 99%, Thus they may be particularly wary of trying to prove price-fixing violations, where prospects for conviction are complicated by the lack of a clear *per se* rule against the practice.

26. Despite the problems, the possibility of criminal prosecution is likely to be retained. The Study Group Report strove to make its analysis consistent with imposing criminal penalties against "heinous, serious cases" for which administrative disposition is considered insufficient. The Study Group Report recommended several technical legal changes to make the criminal enforcement process more flexible, in particular, expanding the venues where cases may be filed and thus making the process in competition cases look more like the process that is used to prosecute other kinds of crimes. The FTC's April proposal calls for authorising compulsory investigative measures for criminal investigations and for expanding venues so criminal cases could be tried in district courts (so that the Tokyo High Court would not be the first instance venue).

Leniency programs

27. The FTC has been considering whether and how to adopt a formal leniency program, offering lower sanctions to violators who come forward early, to make enforcement more effective. A prerequisite for a leniency program is usually some means of varying the sanction, so that the enforcer can be lenient in appropriate cases. For example, leniency might in theory take the form of reducing or forgoing surcharges for one company. This is difficult if the surcharge is conceived as a fixed, administrative charge. Nonetheless, since Japan's criminal law does not usually countenance the use of leniency in this fashion, a leniency program would have to be applied in administrative proceedings. One approach could be to create a true "administrative fine" sanction under the AMA, similar to sanctions applied in some other areas such as tax law. Another approach could be to extend leniency to individuals, by not recommending prosecution, in order to obtain evidence about corporate violations. A general measure to protect "whistleblowers" against retribution from their employers was recently approved in the Diet.

28. The Study Group Report recommended a leniency program in connection with the surcharge system and proposed ways to implement it. The law would set a lower surcharge rate (even 0) for a company that voluntarily informed the FTC of its conduct before the FTC was investigating and that voluntarily ceased that conduct. Other issues and procedures would be specified in guidelines and FTC policies. Consistent with aspects of effective leniency programs that have developed in other jurisdictions, the program would make clear that total immunity from the surcharge could go only to the first party to come in; those who come in later could get some reduction for co-operation. To ensure that leniency concerning surcharges is not inconsistent with the potential to apply criminal penalties, it may be necessary to make clarifications about criminal liability in the statute too, although that result might be achieved by an FTC promise not to refer for prosecution. The FTC's April announcement includes plans for immunity or reduction in surcharges under conditions to be defined in the statute.

Private initiatives

29. Public enforcement of competition law is complemented, in theory, by private rights of action. To recover damages, an injured party may file suit under a special provision of the AMA, as well as under the more general provisions of the Civil Code.[11] A claim for damages under the AMA's special provision is only possible after the FTC has found a violation, either after a hearing or through a "recommendation" decision. The private party can then use the decision of the FTC (and the evidence from the hearing, if there is one) to support its claim; an FTC finding of violation means the violator cannot try to avoid private liability by claiming its conduct was not wilful or negligent. Despite these intended advantages, the cases have proved difficult to win. In theory, the recovery appears to be nearly automatic, but in practice, the courts have erected hurdles concerning proof. Moreover, the FTC rarely issues a formal decision with record and opinion providing detailed evidence on which private litigants could rely, although the FTC has been willing to respond to plaintiffs' requests for materials to use in court. Some recent reforms have tried to make private remedies more effective.

Box 6. Private litigation

Strengthen rights of private action by providing for injunctions in independent private suits, easing the proof of damages in competition cases, and facilitating consumer and customer recoveries in price-fixing cases. The quota on new lawyers should be eliminated.

The 1999 Report argued that these steps would apply more resources to competition policy issues, expand the base of support for it, and enlist other institutions in developing important policy principles.

A new kind of private relief is now possible under the AMA. Consumers or business may seek an order to correct or prevent unfair practices (that is, violations of Sec. 19) and restraints imposed by trade associations. These suits may not seek damages, though, and there are some controls to discourage frivolous litigation. These cases are filed in local district courts, which must advise the FTC of the filings and may seek the FTC's views about them. The legislation that created this new remedy also improved parties' ability to collect damages after an FTC final decision. Since the new injunction remedy became available in 2001, there have been 25 cases (as of 1 May 2004), mostly about distribution restraints. Plaintiffs have lost the final judgments that have been issued to date, but at least one suit was settled. The new type of action is likely to be useful as an outlet for claimants who cannot persuade the FTC that their problems are serious. But it may be used for important matters, too.

And there has been some action to remove the restraints on the legal profession. The number of new lawyers admitted through the traditional process, based on examination, is increasing. Currently 1500 in 2004, the plan is to reach 3000 by 2010. In addition, a new legal education system was introduced in 2004, involving law schools, examinations, and legal apprenticeship. A kind of lateral-entry expansion may also develop, if partnerships between foreign and domestic lawyers are permitted.

Coverage of competition law and policy

30. Overt or implicit interference in competitive markets through administrative guidance and other channels of official influence appears to be declining, but changes are difficult to identify or measure. If a government entity is involved in anticompetitive conduct, it remains difficult to correct it with the AMA unless the activity is organised through a commercial enterprise. But not impossible: there have been several cases over the years using the AMA to examine such activities as management of a slaughterhouse by a municipality, sales of New Year's cards by a ministry and price surveys done by an incorporated foundation connected to a ministry. The sensitivities raised by applying competition law to official conduct are illustrated by the modesty of the improvement made through the new law, effective in 2003, about public officials' responsibility for or complicity in bid rigging. The FTC can order the procuring agency to investigate the situation, and it can require the agency to take disciplinary action against the individual official involved and to demand indemnity from the official (after the agency's own investigation). But the FTC has no power to issue a fine or other sanction against the agency or the official. If the agency denies the FTC's requirement or order, the only consequence it faces is the embarrassment of bad publicity.[12]

Box 7. Administrative Guidance

Target enforcement on practices that have been tolerated or promoted by informal administrative guidance, to reinforce the shift in regulatory philosophy away from central direction.

Because a central goal of the reform agenda should be to end anti-competitive co-ordination sponsored by Ministries, the 1999 Report called for exemplary enforcement actions to implement the principles set out in the 1994 FTC guidelines about administrative guidance. Beyond consulting with other ministries and asking them to stop encouraging or tolerating non-competitive behaviour, the Report recommended applying effective and visible sanctions to private parties who try to use the cover of ministerial authorisation in order to prevent competition. FTC oversight of trade association activities, where much of the impact of administrative guidance is felt, must be maintained and even intensified.

The 1994 Guidelines are still in place, and a Cabinet Decision in March 2003 reminded the relevant ministries and government agencies that, bearing in mind the aim of the Guidelines for Administrative Guidance under the AMA, they should have sufficient prior consultation with the FTC to ensure that government regulations are not replaced by anti-competitive administrative guidance after deregulation. The FTC does not report any new, significant cases in recent years challenging conduct that the parties claimed should be excused because it was undertaken pursuant to administrative support or instruction. Perhaps because of reforms there have been fewer problems than the 1999 Report suggested. Or, perhaps it is still too difficult to take these problems on through enforcement action, because ministries that interfere with markets are still powerful and the firms affected by the interference are still reluctant to complain.

31. Reduction in the number of statutory exemptions from the AMA represents a substantial reform of competition policy. The list of explicit exemptions is not unusually long now—once there were over a thousand—nor are the items that remain exempted particularly unusual. Exemptions for exercise of intellectual property rights and agricultural co-operatives resemble those found in nearly all Members countries. Agreements among insurance companies (other than life insurance) related to risk and to certain kinds of compulsory coverage are exempted, largely to permit pooling of risks and assembly of information needed for actuarial reliability. Transport agreements are permitted to facilitate interline operations and joint fares. Export cartels are exempted, presumably because their effects, if any, are likely to be felt elsewhere. And merger control does not apply to share or assets acquisitions in bankruptcy restructuring, where speed and asset preservation are paramount concerns. Of course, repealing an exemption will not by itself change industry behaviour. Instead, the once-exempted industry is likely to try to find ways to continue its cartel behaviour, perhaps with official blessing. An example is harbour services. The exemption from the AMA for ports cartels was abolished in the late 1990s, but as of 2003 the industry association was still reportedly trying to control entry and police competition.

Box 8. Exemptions

Complete the planned elimination and narrowing of sectoral and other exemptions from the AMA.

These plans were underway for many years, in many stages. The 1999 Report found that it was time for action, to follow through on the plans already announced and, for those items calling for further study, to complete that process and draft legislation to narrow any remaining exemptions as much as possible.

The process of eliminating and narrowing exemptions has been substantially completed. Comprehensive legislation enacted in 1999 abolished the system for depression and rationalisation cartels and a long list of other exemption systems, while limiting the scope of many others. In March 1999, there had been 57 systems of exemption from the AMA; these had been reduced to 21 by the end of 2003. These are summarised in the Annex. In many of these systems, particular agreements must be individually approved in order to be exempted, and for several, none have been approved recently. (Even before repeal, some provisions for exemption had fallen into disuse. For example, the last approved depression cartel had been terminated in 1989). Agreements that are exempted based on individual laws must typically be approved by the Minister with jurisdiction, following consultation with or notification to the FTC. Approval under these legislative schemes is typically conditioned on meeting requirements concerning the necessity of the exemption to achieve the legislative purpose. Some competition standards are typically imposed, too, such as non-discrimination. Often, the "exemption" does not extend to unfair practices that are prohibited by the AMA.

32. Eliminating the exemption for "inherent monopoly" in 2000 occurred in the context of the liberalisation of electric power. This change has expanded the potential application of the AMA in other network industry settings, too. In telecoms, the FTC has issued Guidelines jointly with the Ministry of Public Management, Home Affairs, Posts & Telecommunications which describe conduct that would violate both the AMA and the telecoms law. Similar guidelines about electric power and natural gas have been developed between the FTC and METI. Co-ordination with sectoral regulatory authorities is evidently informal, without explicit protocols or rules requiring joint action, deferral to one or the other body in particular cases or agreement between them on findings about market power.

Box 9. Wider responsibility for competition policy

Explicitly include in the mandates of sectoral ministries and regulators the responsibility to support competition principles and enforcement.

The 1999 Report argued that making other ministries responsible for eliminating constraints on competition within their own jurisdiction would also extend the scope of competition policy and emphasise its broad, horizontal importance. To maintain the FTC's central responsibility, ministries should also be held responsible for co-ordinating with the FTC so that enforcement issues are referred there quickly. The 1999 Report suggested that major ministries might have antitrust bureaux to work with the FTC and to advise industries about their compliance obligations. These steps could be elements of the revisions of the ministries' foundation laws to clarify the relationship between the administration and the market, which were recommended in Chapter 2 of the 1999 Report.

Implementation of this recommendation has been mixed. In telecoms, "promoting competition" is now one of the purposes of regulation. The purposes also include the "public interest" and "sound development" of the industry. These broad and ill-defined concepts give the regulator substantial discretion. Nonetheless, regulation has often stressed helping new competitive entrants overcome incumbent obstruction. But there has been no substantial entry by facilities-based firms, although there are many new firms in services and mobile telecoms. Controversy continues over whether universal service requirements and interconnection charge policies are protecting the interests of the historic incumbents. The FTC has taken some enforcement actions in telecoms, but these have not been co-ordinated with the regulator. The FTC has a case pending concerning NTT's charges for fibre-to-the-home service; this was also the subject of guidance from the Ministry under the telecoms law.

In electric power, by contrast, the principle of promoting competition was not included among the purposes of sectoral regulation. The ministry, METI, still combines the functions of market development and regulation. Its approach to regulation is shifting slowly from prescription to monitoring, preparing for greater competition in the market. The market is responding as competition expands: when sales to consumers using over 500kW became contestable in April 2004, the Kansai Electric Power Company cut daytime power tariffs for them by up to a fifth. Natural gas is also a METI responsibility, and regulation is being designed to encourage more competition in stages. New legislation will expand provisions for third party access to LNG terminals and pipelines, while requiring accounting separation and non-discrimination.

33. The most significant remaining basis for limiting the scope of the AMA is the system of exemptions for co-operative organisations of small and medium sized businesses. It only exempts co-operative groups that comply with the AMA's rules, and the exemption does not extend to unfair practices or substantial restraints of competition that lead to "unjust" price increases. That proviso makes it difficult to see what purpose the exemption serves, as there would be no need to exempt conduct that did not violate the law anyway. The exemption does appear to have an effect, if only as an admonition from the legislature to tread lightly here. Actual enforcement against an SME co-operative for exceeding the statutory bounds is very rare. SMEs might also benefit from an exemption that permits agreements on prices and opening hours to prevent "excess competition" in personal services such as hair cutting. Although co-ordination among micro-enterprises could improve efficiency, a habit of overly-permissive exemption could reduce competitive pressure in what should be highly competitive settings. The FTC has not authorised any exemptions for agreements among these "hygienically related businesses" for several years. The provision evidently remains in the law as a symbolic protection for SMEs.

34. Another potentially significant exemption permits resale price maintenance for copyrighted works, to promote culture and preserve diversity of views and home delivery of newspapers. Some mechanism to spread risks is common for these products (and a similar exemption from competition law is often found in other jurisdictions), and maximum resale price maintenance might well benefit consumers in some cases. But complete exemption from a basic rule is a striking inconsistency. Another round of consultations about this exemption among publishers, consumer interests and the FTC began in 2003.

35. How competition policy should apply to social issues is becoming an important issue. In Japan, this topic includes not only education and health, but also agriculture. Legislation about agriculture exempts co-ops in that sector from the AMA by cross-reference to the exemption for SME co-operatives. The Council on Regulatory Reform is considering whether to revisit the scope of this exemption. In a potentially significant experiment, reforms in some special zones permit corporations to enter agricultural production (by leasing land). The same issue, that permission to enter a sector may be based on the form of doing business, is arising with respect to other public and social services. Such preferences can distort competition. Government decisions on entry into providing health or education services favour entities that are technically considered "non-profit." Decisions about whether to permit entry by a new for-profit provider are up to local councils, which include representatives of these incumbent "non-profit" providers.

Policy studies and advocacy

36. A steady accumulation of incremental reforms over the past decade, often ones promoted by the Council on Regulatory Reform and the FTC and its Study Group on Government Regulations and Competition Policy, have led to wide-ranging, pro-competitive changes in Japan's regulatory system. Most notably and fundamentally, competition-suppressing administrative controls on price and entry have generally been eliminated.

Box 10. Supply-demand balancing

Eliminate all "supply-demand balancing" aspects of permitting, licensing and other forms of advice or intervention, formal or informal, within a fixed period, such as one year. Fix sunset dates of preferably less than two years on all such requirements that remain.

The most important recommendation in the 1999 Report was the elimination of all "supply-demand balancing" functions that were used to control and prevent pro-competitive entry. The reform programme that was envisioned then promised to move in the right direction, but the Report found that its concrete content was disappointingly limited and the target dates were imprecise. The major constraints, such as limits on entry into transport sectors, were well known, and the Report recommended setting a firm, short deadline for their repeal.

After some steps under the first 3 year reform plan (1995-98), the pace of change accelerated. Regulations setting prices and controlling entry based on ministerial assessment of the balance between supply and demand in the market have been removed from trucking, airlines, ports, petroleum, housing, banking, securities and telecoms. Similar reform of taxicab services is in process now, although the commitment to the principle is ambiguous: control of entry based on supply-demand considerations has in principle been abolished, but the minister can step in if there is excess competition in an area. The most recent regulatory reform plan calls for abolishing the supply-demand criterion for entry in coastal shipping.

But there are points of backsliding and resistance. For example, supply-demand considerations are no longer supposed to be used in issuing licenses for locating retail liquor stores; however, local finance offices are reportedly administering temporary laws to control supposed oversupply. And outside of 9 major harbours, supply-demand considerations are still used to restrict entry into providing port services.

37. Since the 1999 Reform report, the FTC's Study Group on Government Regulations and Competition Policy has produced 10 more studies and recommendations about competition policy and reform in electricity (2 reports), natural gas, domestic aviation, postal services, public utilities, telecoms and broadcast (3 reports) and social regulation. Under the current reform plan, health care, welfare, labour and education are the principal themes, and this study group issued a report in November 2002 on promoting competition in the area of social regulation.

38. The study group's proposals about telecoms included eliminating the distinction between carriers with and without physical facilities, transparent interconnections and increased competition to reduce interconnection access charges, and allocating spectrum through auctions. Its report doubted that the holding company structure for NTT was likely to promote competition and urged that it reduce its holding in mobile telephone service. Many of these recommendations have been adopted, some of them in the revision of the telecommunications law that was proposed by the Telecommunications Council, a group organised to offer advice to the Minister. The study group has also recommended increased competition in postal services. Its 2000 report called for liberalising delivery of commercial bulk mail and value-added mail service and fixing low quantitative thresholds for determining which services are subject to competition. There has been some progress, as the historic incumbent was corporatised in 2003 and service has been liberalised, in principle. In practice, because the design of the universal service obligation discourages entry where that is an issue, there is competition only for commercial services.

Conclusions and recommendations

39. Important wide-ranging reform measures have been achieved, notably the reduction in reliance on supply-demand balancing and the elimination of a host of measures authorising exemptions from the AMA. In telecoms, the sector regulator is accepting responsibility to support improvement in competition. Changes are most striking in telecoms, distribution, trucking and financial services. Problems due to reduced competition and hence higher costs remain in some sectors, due to industry and regulatory habits

that are resistant to change. The legal profession is opening up, but slowly. Issues in particular sectors are described in more detail in the special chapter on product market competition in the 2004 OECD *Economic Survey* of Japan.

40. Some of the benefits resulting from these changes are measurable and striking. The Cabinet Office has tried to estimate the effects of implementing some of the major changes in the 3 year regulatory reform programs, in terms of increased consumer surplus (that is, without considering effects such as reducing producer costs). The latest estimate, in 2003, dealt with the effects of reforms in mobile telephony, trucking, domestic airlines, car inspections, electric power, gas, oil, securities commissions, insurance, beverages and food, and products where resale prices had been designated such as cosmetics and pharmaceuticals. In total, the Cabinet Office estimated that these reforms increased consumer surplus by ¥13.4 trillion per annum, or ¥112,000 per capita: this amounts to about 4% of GDP. One reform that the 1999 Report pointed out, ending rate and entry regulation in trucking, accounted for ¥3.9 trillion of this total.

41. The FTC's profile in reform has improved, with its move to the Cabinet Office. It has taken steps to make its policies and especially its reasoning in particular decisions more transparent. The FTC recognises its need for more sophisticated economic analysis and legal expertise in complex cartel investigations. Additional resources are concentrating on those areas, but even more could be needed. Improvements in competition law enforcement include the new form of private legal action. As much of the system of conventional economic regulation has been reformed, competition policy now faces new circumstances. The major challenge now is making enforcement more effective, in part to preserve the benefits of reform.

Policy options for consideration

Sanctions actually applied must be effective to deter hard-core violations: surcharges must be much higher, especially if criminal prosecution remains rare.

42. Proposals to double the surcharge level would bring Japan closer to the emerging international consensus about the need for strong action against the most serious abuses. Because it is based on covered commerce, not total turnover, the proposed doubled rate might still be too low to deter effectively, though. Adding only 50% to the surcharge for repeat offenders might not be enough to get their attention; that percentage probably should be significantly higher. Retaining distinctions in the surcharge system for different violators is problematic. The rationale for maintaining these distinctions for small business and for wholesale and retail trade is not that there is less need for enforcement in those settings, but that because margins are smaller, smaller sanctions would still have adequate deterrent effect. Even if that were true, retaining these special lower rates preserves a loophole that weakens enforcement. If the threat of criminal sanctions is to be taken seriously, the FTC needs stronger investigative powers and closer co-operation with the prosecutors, to develop the evidence that is needed to support referrals and obtain convictions.

Implement a leniency program to detect and deter cartels.

43. The proposals for a leniency program are also consistent with the emerging consensus among competition law enforcers. Such a system would make Japanese enforcement more effective and may facilitate co-operation with other enforcers, to deal with wide-ranging cartels that harm Japanese consumers. Where there is a very clear advantage to being the first party to come forward (and thus, a very substantial risk in not being the first), and there is some advantage to coming forward even after an investigation has started, some cartels have broken down in a race to confess. Proper attention to matters of process and design of an effective leniency program, such as the relationship between the surcharge system

and criminal prosecution, is important, and the FTC's plans show that this issue has received considerable attention. The most important consideration, though, is the enforcement climate: the promise of leniency is an effective enforcement tool only if the threatened sanction that is avoided is substantial and credible.

Strengthen consumer protection and its relationship to competition policy.

44. Japanese consumers still need a stronger voice in the policy process and stronger protections in the law. The relationship between competition enforcement and consumer interests is not always clear enough. At least, the surprisingly large number of FTC actions about price cutting would not inspire confidence in consumers that competition enforcement is promoting their interests. Laws and institutions protecting consumers in Japan need to be strengthened. Giving that responsibility to the FTC could help to focus competition law enforcement on consumer interests, too.

Complete the process of eliminating unnecessary controls on competitive entry.

45. It is no longer common for entry to be controlled by means of licensing or other administrative decisions based on the balance of supply and demand. A few pockets of resistance to reform remain, though, where these habits persist unnecessarily or where other administrative measures are used to protect incumbents against unwelcome competition. Most of this principal recommendation from the 1999 Report has been achieved, but it would still be beneficial to eliminate the rest of these constraints—and it will be important to sustaining the benefits of reform to prevent them from reappearing in other forms.

Table 1. Implementation of 1999 Recommendations

Recommendation of 1999 Review	Actions taken since the 1999 Review	Assessment and recommendation
Strengthen rights of private action by providing for injunctions in independent private suits, easing the proof of damages in competition cases, and facilitating consumer and customer recoveries in price-fixing cases. The quota on new lawyers should be eliminated.	Consumers or business may now seek a court order to correct or prevent unfair practices and restraints imposed by trade associations. The number new lawyers admitted through examination is increasing,: from 1500 in 2004, the plan is to reach 3000 by 2010. A new legal education system introduced in 2004 will make an alternative path to entry available.	The new private action is a useful outlet, particularly for minor disputes and competitor complaints. It is not available for major cases under Sec. 3 about unreasonable restraints and private monopolisation; for these, the FTC remains the primary, if not the sole, decision-maker.
Increase the visibility and impact of FTC participation in policy-making.	The FTC was moved to the Cabinet Office in 2003.	Stronger ties with the formal regulatory reform process, promised in 1999, would still be valuable. The FTC's independent image could be improved further by appointing commissioners from a broader range of backgrounds.
Explicitly include in the mandates of sectoral ministries and regulators the responsibility to support competition principles and enforcement.	Done for telecoms, but not for others, including electric power.	Making the responsibility to support competition explicit concerning transport and energy would also be valuable.
Establish a clear, public, effective relationship between consumer policy and competition policy.	Consultations between the FTC and consumer agencies have continued as before.	A stronger consumer protection system is needed, with a role for the FTC.
Complete the planned elimination and narrowing of sectoral and other	Substantially done, through enactment of legislation to remove statutory	Compliance with the terms of the remaining exemptions, particularly

Recommendation of 1999 Review	Actions taken since the 1999 Review	Assessment and recommendation
exemptions from the AMA.	authorities for exemption.	concerning SMEs, should be monitored.
Improve the FTC's economic and legal resources, to enable it to undertake more sophisticated merger and monopoly enforcement, prepare more successful cartel cases and resolve market access problems.	Resources have continued to increase. The FTC staff level is now 672, compared to only 478 in 1991. A policy unit has been set up to improve its economic analysis, and more legal expertise has been brought in.	Stepped-up enforcement and new procedures will probably require even more bolstering of legal expertise. Developing a stronger career path at the FTC would reduce the need to rely on seconded personnel.
Target enforcement on practices that have been tolerated or promoted by informal administrative guidance, to reinforce the shift in regulatory philosophy away from central direction.	The 1994 Guidelines are still in place, and a Cabinet Decision in March 2003 reminded Ministries of their obligations to consult with the FTC.	Continued monitoring is necessary. The new, limited powers about official involvement in bid-rigging violations should be applied to the maximum extent.
Publicise actions and reasoning, to educate the public and the business community about the effects and benefits of competition policy and law enforcement.	More information about decisions is available on the FTC website and in other outlets. The merger consultation process has tried to create an outlet for explaining FTC reasoning in particular merger cases.	More extensive use of the merger consultation process and public explanations of FTC reasoning would strengthen confidence in the consistency and effects of policy.
Eliminate all "supply-demand balancing" aspects of permitting, licensing, and other forms of advice or intervention, formal or informal, within a fixed period, such as one year. Fix sunset dates of preferably less than two years on all such requirements that remain.	Substantially done, through a variety of measures eliminating such criteria for licensing entry.	Some unfinished work remains concerning aspects of transport, and the same process, of protecting the profits of incumbent firms against threat from entry, should not be allowed through different, indirect measures.
Improve capacities to address international competition problems by reaching agreements with other countries on cooperation and enforcement.	Japan has reached agreements with the US (1999), Singapore (2002) and the EC (2003), and is discussing agreements with others.	These capacities are now being used.

Table 2. Exemptions from AMA

Ministry or agency	Sector or description	Legislative basis	Date of legislation	Exemptions authorised, 2003
Justice	Acquisition of shares of companies under reorganisation	Corporation Reorganisation Law	1952	
Education, Culture, Sports, Science and Technology	Agreements on music licensing fees	Copyright Law	1970	
Financial Services Agency	Insurance cartels	Insurance Business Law	1951	8
	Compulsory automobile and earthquake insurance	Law concerning Non-Life Insurance Rating Organisations	1998	2

Finance	Rationalisation cartels	Law Concerning Liquor Business Associations and Measures for Securing Revenue from Liquor Tax	1959	0
Health, Labour and Welfare	Agreements to prevent excessive competition	Law Concerning Coordination and Improvement of Hygienically Regulated Business	1957	0
Agriculture, Forestry and Fisheries	Federation of agricultural co-operatives	Agricultural Cooperative Association Law	1999	
	Agricultural association corporation		1999	
Economy, Trade and Industry	Export cartels	Export-import Trading Law	1952	0
	Federation of small business associations	Law on Cooperative Association of Small and Medium Enterprises.	1999	
	Joint economic undertakings	Law on Cooperatives of Medium and Small-Sized Enterprises	1957	
Land, Infrastructure and Transport	Maritime transportation cartels (international)	Maritime Transportation Law	1949	[211]
	Maritime transportation cartels (coastal)		1949	10
	Transportation cartels	Road Transportation Law	1951	3 (1)
	Aviation cartels (international)	Civil Aeronautics Law	1952	[292]
	Aviation cartels (domestic)		1952	0
	Maritime transportation cartels (coastal)	Coastal Shipping Association Law	1957	1 (1)
	Joint shipping businesses		1957	

Source: FTC. Figures for international maritime and aviation agreements are the number of notifications received by the Ministry concerning concluding, amending, or terminating an exempted agreement, not the total number of such agreements in force. In road and coastal transportation, agreements involving one party may apply to several routes or subjects.

NOTES

1. The original AMA rule about price fixing was a per se rule, that is, one that did not require showing an actual effect in the particular case, and it was explicitly repealed back in 1953..

2. Members can be required to pay surcharges. The FTC keeps its Guidelines about trade association conduct current; they were last re-issued in 1995.

3. A separate section provides a basis for designating products for which resale price contracts are permissible.

4. Other means for regulating industry investment structures are vestiges of the AMA's recently-repealed ban against holding companies. An amendment to the AMA effective in 2002 repeals the restriction on total shareholding by a "giant company" (Sec. 9-2), while generalising the prohibition against establishment of (or transformation of an existing company into) a company with an "excessive concentration of economic power" (Sec. 9). In addition there are some restrictions on share holdings by banks and insurance companies.

5. The basic threshold is assets or turnover totalling over ¥10B for the combined entity and exceeding ¥1B for the acquired entity.

6. There is also a criminal law about unfair competition, which is applied to violations concerning trademark or country of origin and is enforced by the police and prosecutor.

7. On occasion, individuals may be sentenced for bid-rigging under a separate provision of the criminal law, while the companies involved are subject to surcharges for violating the AMA.

8. In some of these cases, the figure was estimated *ex post*, since the proportion of covered commerce was not necessarily used as the basis for computing the fine.

9. The FTC says it is its "active policy to apply criminal penalties to violations that a) substantially restrict competition … such as price cartels, supply restraint cartels, market allocation agreements, bid-rigging and boycotts, which constitute serious cases that are likely to have a widespread influence on the national economy; or b) involve firms or industries that are repeat offenders, or do not take appropriate measures to eliminate the violation, and where the administrative measures of the FTC are not considered sufficient to meet the aims of the AMA." (FTC, 2002, p. 6)

10. There have been many more prosecutions under the special provisions of the Penal Code about obstruction and collusion in bidding, though.

11. In addition, citizens can bring actions under the Local Autonomy Act to recover losses due to practices such as bid rigging. These suits have been more numerous, and more successful, than damages claims about AMA violations.

12. The official might face prosecution, if the misconduct amounts to corruption.

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