

(Tentative Translation)

**Report from the Government of Japan
on the EU-Japan Business Dialogue Round Table (the BDRT) Recommendations**

April 2004

(The contents of this report are based on the situation in Japan as of February 2004.)

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The 1st Working Party (Trade and Investment)

1. Conclusion of a Framework Agreement on the Enhancement of Foreign Direct Investment (FDI) between Japan and the EU

(1) Summary of the BDRT recommendations

A proactive stance should be adopted toward increasing direct investment.

- (a) The agreement should clearly state the benefits to Japan and the EU of a mutual increase in FDI.
- (b) The agreement should contain a commitment to cooperate at the highest level to promote the benefits of foreign investment to the public.

(2) State of the measures taken thus far

- In the General Policy Speech given by Prime Minister Junichiro Koizumi on January 31, 2003, he announced a policy based on the belief that foreign direct investment in Japan would bring about new technologies and innovative management, which will increase opportunities for employment. The prime minister said, therefore, that such investment should not be regarded as a threat, and that the government of Japan (GOJ) would take measures to make Japan an attractive investment destination for foreign businesses, with the aim of doubling the cumulative amount of investment in Japan within five years.
- Following the policy speech, the EU leaders stated, in the joint press statement of the 12th Japan-EU Summit on May 2, 2003, that they welcome the policy of the government of Japan.
- While recognizing the necessity of the joint efforts to encourage more European companies to invest in Japan as well as more Japanese companies to invest in Europe, the leaders of Japan and the EU released a statement on the “Japan-EU Initiatives on Investment,” and the following effective measures have been implemented to promote mutual investments over a one-year period.

① Hosting and participating in investment seminars. (Seminars were held in Sweden and Finland in November 2003 and in Paris, Munich, Brussels, and Luxembourg in December of the same year.) Participating in the seminar on EU enlargement hosted by the European Commission (November 2003.).

② Holding exchange meetings between institutions in charge of promoting investment (in February 2004, representatives of the relevant institutions from France, Belgium, Poland, Czech Republic and several Japanese prefectures, such as Saitama, Mie, and Fukuoka, as well as officials from JETRO, gathered to introduce their programs and to exchange opinions.).

③ Conducting a European press tour on investment in Japan for five days from March 1, 2004. Fifteen people, each from an EU member state, were invited to join the tour of the investment environment in Japan.

④ Holding the “Japan-EU Regulatory Reform Dialogue.” (The meetings were held in Tokyo in November 2004 and in Brussels in February 2004 and the discussions focused on the improvement of the business environment and on regulatory reforms that promote mutual investment.)

⑤ Providing a one-stop service to foreign investors (JETRO launched a one-stop service in May 2003) and establishing Invest Japan, a general information center concerning foreign direct investment in Japan, at related ministries and agencies (May 2003), etc. As mentioned above, both Japan and the EU have expressed a proactive position toward increasing foreign direct investment.

(3) Future outlook

The GOJ is considering the possible measures that can be taken for the further promotion of mutual investment between Japan and the EU, while exchanging opinions with interested parties in the European Commission, with the BDRT and other related parties.

2. Eliminating tax-related barriers to investment

(1) Summary of the BDRT recommendations

(a) Prevention of double taxation

- ① An agreement should be concluded providing for an exemption from withholding taxation on dividend payments between parent and subsidiary companies and on interest and royalty payments among affiliated companies between Japan and the EU.
- ② It should be agreed that Japan-EU investments be mutually exempt from controlled foreign corporation (CFC) taxation (so-called tax haven taxation). Based on the agreement, treaties to prevent double taxation concluded between Japan and each EU member state should be revised to provide for the mutual exemption of CFC taxation. Abuse of this exemption should be addressed through provisions to prevent such abuse set out in the treaties.
- ③ An agreement should be reached to expand the application of the foreign tax credit system. Based on this agreement, the foreign tax credit systems should be revised in Japan and the EU member states.

(b) Transfer pricing taxation

- ① Agree to extend the application of the EU Arbitration Convention that provides for arbitration in the case of disagreements between the tax authorities in the EU member states to include transactions between Japan and the EU.
- ② Agree to simplify and make consistent the documentation requirements and develop mutually acceptable standards for best practice concerning methodologies, including clearer interpretation of OECD guidelines to reduce the costs associated with complying with the transfer pricing regulations.
- ③ Agree to establish guidelines on unilateral and bilateral advance price agreements (APAs) for transactions taking place between Japan and the EU, working towards improving the system so that it functions more smoothly.

(2) State of the measures taken thus far

(a) Avoiding double taxation

For all aspects of the tax reform, see the appendix attached at the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

(b) Transfer pricing taxation

① For all aspects of the tax reform, see the appendix attached at the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

② Concerning the agreement to simplify and make consistent the documentation requirements to reduce the costs associated with complying with transfer pricing regulations:

Japan has an understanding regarding the fact that taxpayers have been facing costly double administrative requirements to comply with the documentation standards for transfer pricing under different taxation authorities. Japan has also understood that the shared standards regarding documentation on transfer pricing will provide materials that are beneficial in the analysis of external related transactions for taxation authorities and will reduce possible disputes that may arise in transfer pricing.

The Transfer Pricing Documentation Package was developed with respect to this issue, not with the EU, but between the member states of the Pacific Association of Tax Administrators (PATA), consisting of Australia, Canada, the United States and Japan. This package proposes three principles and sets forth in detail contemporaneous documentation for materials required in examinations. This documentation denotes that which exists or is brought into existence no later than the due date, under the relevant PATA member's rules, of a timely filed income tax return for the taxation year for the controlled transactions at issue, including relevant information on transactions that have arisen by this date.

(i) Multinational enterprises (MNEs) need to make reasonable efforts, as determined by the tax administration

of each PATA member, to establish transfer prices in compliance with the arm's length principle.

(ii) MNEs need to produce and maintain contemporaneous documentation of their efforts to comply with the principle of remaining at arm's length.

(iii) MNEs need to submit the documentation immediately upon the request of the tax administrator of a PATA member.

Taxpayers are not forced to use this model documentation package related to transfer pricing, and they are not subject to any legal obligation beyond the law of the PATA member states. While Japan has not laid down any rules for contemporaneous documentation regarding transfer pricing, the materials required by a transfer pricing examination in Japan are consistent with the PATA model documentation package.

③ Concerning the development of mutually acceptable standards of best practice concerning methodologies including clearer interpretation of OECD guidelines:

The interpretation of the OECD guidelines is an issue to be discussed with OECD member states. Therefore, greater efforts will be made for further clarification in discussions at the OECD in the coming months.

④ As Japan has recognized the effectiveness of bilateral APAs, it has dealt with the APAs according to the requests of taxpayers. Japan's system of advance pricing agreement has mainly been managed between the two nations and mutual discussions concerning bilateral APAs have progressed smoothly with the EU member states. During this time, no particular issues have arisen.

When it comes to the transfer pricing taxation, including the advance pricing agreement system, Japan has engaged in discussions at OECD jointly with the EU member states. Therefore, it is considered that, through these discussions, Japan and the EU member states have developed a consensus. If any guidelines between Japan and the EU are examined, they should be based on discussions at OECD. Consequently, it is considered appropriate that, for the time being, the consensus should be built between the member states, including Japan and the EU.

The administration and management guidance for Japan's advance pricing agreement system was issued in June 2001 and the APA program report was released on the website of the National Tax Agency in September last year. Please refer to this material for information about Japan's advance pricing agreement system and its state of implementation.

(3) Future outlook

(a) Avoiding double taxation

For all aspects of the tax reform, see the appendix attached at the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

(b) Transfer pricing taxation

① For all aspects of the tax reform, see the appendix attached at the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

② While Japan has agreed on the model documentation package set forth at PATA, it is considered that the possibility of holding discussions at OECD should be examined in the coming months to promote the sharing of required documentation in examinations by TP.

③ As mentioned above, while evaluation, including the bilateral advance pricing agreement system, has progressed at the OECD, there are currently no plans for Japan and the EU to, on their own, develop any joint guidelines regarding the advance price agreement system.

3. Facilitating business development: The perspective of human resources

(1) Summary of the BDRT recommendations

- (a) An agreement should be reached to speed up work and procedures for acquiring resident's permits for intra-company transfers between Japan and the EU, to enable transferred personnel to submit applications for permits after entering the destination country, and to grant the same rights to spouses.
- (b) Under the FDI Enhancement Agreement, a commitment should be made to conclude social security treaties between all member states and Japan at the earliest possible date. In addition, ways to expedite the conclusion of such treaties should be studied, including the possible conclusion of a model social security treaty between Japan and the EU.

(2) State of the measures taken thus far

(a) Work permits

- ① Concerning the acquisition of the status of residence of "Intra-company Transferee," even in the event of a person entering Japan for a purpose other than engaging in activities as an Intra-company Transferee, he/she may submit applications for work and residence permits, and efforts are being made to speed up the procedure of such applications.
- ② If the understanding is correct that the recommendation is that the same rights should be granted to spouses concerning work and residence permits in Japan, even under the existing rules, a spouse who meets the requirements provided for in the Immigration Control and Refugee Recognition Act may acquire the status of residence permitting work and will therefore be able to work.

(b) Social security agreements

- ① Japan has concluded social security agreements with Germany and the United Kingdom. In addition, we have signed social security agreements with South Korea and the United States, and these agreements are scheduled to be submitted to the current Diet session for ratification.
(Note: The Agreement with South Korea was signed on February 17 and that with the United States was signed on February 19. These agreements will be submitted to the current Diet session.)
- ② The GOJ is now negotiating with France and Belgium regarding social security agreements and is making efforts to conclude them at an early date.

(3) Future outlook

(a) Work and resident permits

- ① The GOJ intends to further review the BDRT recommendations.
- ② The GOJ intends to further review the BDRT recommendations.

(b) Social security agreements

- ① Concerning social security agreements, the GOJ makes its decision with which country it will start its negotiations, taking into account general factors such as the necessity of the agreements with countries including EU member states, and requests from the business community. Therefore, with regard to agreements with each EU member state, we will start negotiations with each country in turn, according to the order of priority based on such general viewpoints.
- ② In addition, as the social security systems of the EU member states differ in terms of their scheme and structure (see note below), the contents of each agreement concluded after the negotiations differ significantly from state to state. (The detailed contents of the existing social security agreements concluded between each EU member state and non-member states are different for each EU member state.)

For these reasons, to conclude social security agreements with each EU member state will take considerable time since it is necessary to coordinate the differences in the social security systems with

each state. Therefore, it may also be difficult for Japan to commit at an early stage to concluding social security agreements with all EU member states from a technical point of view.

- ③ With regard to a model social security agreement (treaty), as mentioned in (2) above, the social security systems vary from country to country and so the contents of social security agreements vary. It is also considered that producing a model social security agreement that is common to all or a number of EU member states would be time consuming. Therefore, a model social security agreement will not be an effective way to facilitate the conclusion of agreements between Japan and each EU member state.
- ④ However, as the government of Japan recognizes the importance of concluding agreements with EU member states, given the requests received from the business community, we intend to advance these issues as quickly as possible.

Note: The longer the history of a social security system in a particular country, the greater the number of systems in existence according to job categories and purposes of establishment, and the more complicated the interim measures. This principle applies in Japan and a number of other foreign countries. (It is particularly prominent in the EU member states, as many have social security systems with a long history.)

4. Facilitating corporate reorganization: Legal and tax perspectives

(1) Summary of the BDRT recommendations

The Japanese Commercial Code and the company laws in the EU member states should be amended to allow for cross-border share exchanges between Japan and the EU. The relevant tax laws should also be amended so that tax may be deferred.

(2) State of the measures taken thus far

Discussions regarding the modernization of corporate legislation are currently underway at the Corporate Law Subcommittee on the modernization of the Justice Ministry's Legislative Council and the Ministry of Justice has been examining possibilities for introducing some modern organizational restructuring methods. These methods include flexible counter value for mergers, such as triangular mergers and cash mergers, and short-form mergers.

A draft proposal including matters regarding the introduction of these organizational restructuring methods was released to the public on October 29, 2003 to receive Public Comments. For all aspects of the tax reform, see the appendix attached at the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

(3) Future outlook

The Corporate Law Subcommittee on the modernization of the Justice Ministry's Legislative Council intends to continue discussions in the coming months with the aim of amending the corporate legislation regarding modernization, currently scheduled for 2005.

5. Facilitating business development through regulatory reform

(1) Summary of BDRT recommendations

- (a) Direct investment should be enhanced by revising regulations concerning market access, including regulations on the transfer of assets, services and intellectual property. Other areas subject to review should include regulations on capital, and the establishment of an open business environment that does not place new market entrants at a competitive disadvantage.
- (b) An acknowledgement of the negative affect of regulatory barriers on foreign investment should contain further commitments from both Japan and the EU to create competitive internal markets through regulatory reform.
- (c) A commitment between Japanese and EU regulatory authorities to cooperate on creating an open regulatory environment for trade and investment
- (d) A commitment that the authorities of Japan and the EU will work to eliminate unreasonable procedures for the approval of products and services

(2) State of the measures taken thus far

(a) Following the policy of doubling the cumulative amount of inward foreign direct investment in Japan within five years compared with that in 2001, as announced in the General Policy Speech given by the Prime Minister in January 2003, it has been decided at the Japan Investment Council, chaired by the Prime Minister, to adopt the Program for the Promotion of Foreign Direct Investment in Japan. The program consists of 74 items over five fields. In accordance with this program, the following major measures have been carried out thus far.

- In May 2003, a single contact point, Invest Japan was established at related ministries and at JETRO to provide investment related information to foreign companies interested in direct investment in Japan.
- Implementing proactive domestic and overseas PR activities, including the production and broadcasting of commercials that introduce the attractions of and initiatives taken by Japan as an attractive investment destination. In this context, symposiums and seminars were held overseas to invite investment in Japan.
- In April 2003, the measure of flexible counter value for mergers was introduced. This measure was a special exception of the Commercial Act with the amendment Industrial Revitalization. Its purpose was to ease cross-border mergers and acquisitions.
- In September 2003, the administration of public facilities was opened to private enterprises with the enforcement of the partially revised law of the Local Autonomy Law.
- In September 2003, a measure was introduced to provide people who complete a school program at any international school with the qualifications to enter colleges in Japan. This measure accompanied the revision of the School Education Law.

(b) and (c)

Since 1994, Japan has been conducting successful Japan-EU regulatory reform dialogues with the EU at the official level to develop two-way trade and investment relations through the promotion of regulatory reform and improvements of the business environment in both Japan and the EU.

During FY2003, the dialogues were held in Tokyo in November 2003 and in Brussels in February 2004. Progress has been made in many areas, as follows:

EU proposals to Japan

- Active initiatives to promote investment in accordance with the program proposed by the Japan Investment Council
- Initiatives to enlarge measures taken in special zones for structural reform to nationwide
- Examination for raising the maximum amount of the penalty and for extending periods of elimination relating to competition law
- Examination for raising the maximum amount for defined-contribution portable pension plans
- Increasing the ratio of addition applied to innovative new drugs (from 40% to 100%)
- Examination for protecting intellectual property rights for new drugs
- Reduction of the commission for extraordinary opening of the customs house by about half

Japan proposals to the EU

- Introduction of the community patent system
- EC's participation in the Madrid Agreement Protocol concerning trademarks

- Standard contract clauses under the directive of personal information protection
- Operation of anti-dumping regulations
- Exemption of NiCd batteries from the directive covering discarded batteries
- Improvement in operation of the resident permits and work permits in each member state
- The treatment of Japanese driver's licenses
- Offset of profits and losses across multiple member states, and the legal framework allowing mergers across national borders.

For the initiatives taken to enhance the mutual investments between the EU government and the GOJ, see 1 (a).

(d) In accordance with the “Three-Year Programme for Promoting Deregulation (Further Revised),” the following reforms have been implemented in the field of standard and recognition.

With respect to the systems of standards and recognition reached through the autonomous actions of enterprises, the GOJ is conducting a comprehensive review to determine whether the systems involving government should be maintained.

Concerning the international harmonization of standards, the GOJ is promoting coordination of Japanese standards with established international standards where appropriate. Where such international standards do not exist, Japan has proposed and worked on the establishment of international standards in accordance with the Japanese standards. Japan has also promoted the acceptance and mutual recognition of overseas data.

With a view to reducing the burden on enterprises, necessary measures will be taken to eliminate duplication of inspection for similar inspection items, where it is conducted regarding several standards.

(3) Future outlook

FY2004

(a)

- The aim of steadily implementing the Program for the Promotion of Foreign Direct Investment into Japan will continue in the coming months and reviews and additions will be conducted if required.
- Symposiums and seminars focus on investment in Japan will continue to be held overseas, as a series of Japan-U.S. investment initiatives and Japan-EU investment initiatives.
- Special measures such as regulations implemented in special zones for structural reform will be evaluated. A nationwide rollout will be promoted for those that do not cause any particular problems. For example, the possibility of rolling out a measure to increase the resident period will be examined, and this has in fact been implemented in some designated districts to accept foreigners with relevant expertise and skills. This measure may contribute to increasing economic activity and improving technical abilities in Japan. (Over three to five years)
- The flexible counter value for mergers will enable mergers to occur with shares of parent companies, including foreign companies, as well as cash and other assets. To modernize the corporate legislation based on a draft proposal that includes the introduction of a flexible system as a permanent measure and the opinions submitted in response to the proposal, a review will be conducted to introduce the permanent measure.
- In FY2004, it is scheduled that the maximum amount of premiums for defined contribution pension plans (the contribution), in which the portability is secured, will be increased. The increase will cope with both the reform of the pension program and the labor movement.
- To accommodate the needs of venture companies looking for investments by funds and companies engaged in business revitalization, a bill will be submitted to revise part of the law regarding the limited partnership agreement for investments. The bill relates to small and medium-sized enterprises. The core component of the bill is the addition of the loan function and the elimination of requirements concerning small and medium-sized and unlisted companies.

(b) and (c)

In the coming months, Japan will continue to use dialogue between the EU and the GOJ, including the framework of the Japan-EU Regulatory Reform Dialogue.

(d) In the coming months, Japan will conduct further reviews in accordance with the “Three-Year Programme for Promoting Deregulation (Further Revised).”

6. Promoting economic growth

(1) Summary of the BDRT recommendations

- (a) More effective use of monetary and fiscal policy should be made to combat price and asset deflation.
- (b) More efforts should be made to re-capitalize the banking system and clean up the situation with bad loans.
- (c) Public spending should be redirected to more productive areas of the economy.

(2) State of the measures taken thus far

- (a) Under the policy of “No growth without reform,” the GOJ has devoted itself to reform of the financial markets, taxation, regulatory and annual expenditure to overcome deflation and activate the economy.

Under these circumstances, the Japanese economy has been steadily recovering, thanks to a recovery in company earnings and increased capital spending, led by private-sector demand. In addition, GDP grew by 1.7% in the fourth quarter of 2003, compared to the previous quarter. Moreover, nominal GDP has remained positive for the past three quarters, and the decline in consumer prices has shown signs of ending. In employment, the active opening ratio has increased for six straight months while the overall unemployment rate dropped to the 4% level for the first time in 30 months.

- (b) The GOJ developed the program for financial revival, which aims to halve the ratio of bad loans at major banks from the level at the end of March 2002 by the end of March 2005 and to build a much stronger financial system that supports structural reform (October 2002). Following the implementation of this program, the government has quickly and steadily implemented a range of measures relating to the tightening of asset assessment, the fulfillment of net worth and improved governance.

As a result of these initiatives, the outstanding balance of bad loans at major banks as of the end of September 2003 was 17.5 trillion yen, down 34.9% from the end of March 2002. In addition, the bad loan ratio was 6.5%, down 1.9 points over one and half years from the end of March 2002, indicating a steady reduction towards the target set out in the program for financial revival.

The GOJ has been attempting to resolve the issue of bad loans by bolstering the functions of small and medium-sized regional financial institutions and has been promoting initiatives to revitalize small and medium-sized enterprises and to activate regional economies. These initiatives have been conducted in accordance with the action program regarding the strengthening of the functions of relationship banking (March 2003). The GOJ has been promoting the measures included in this program as well as following up the plan for enforced functions developed by each financial institution to encourage steady implementation of the plan.

While activating regional economies has become a challenging issue under the current economic conditions, it has become a crucial task for financial institutions to strengthen their ability to deal with risks, including the handling of such issues as corporate revitalization and bad loans. Given these conditions, the required bills have already been submitted to the Diet. The purpose of the bills is to contribute to the activation of regional economies and the stability and of the financial system to create a new public funding system for the reinforcement of financial functions.

- (c) The government has given priority to increasing the vitality of the private sector while maintaining fiscal discipline. The government’s objective is to activate the economy led by the private sector through the effective allocation of budgets to energize society and the economy in the budget for FY2004 under tough fiscal conditions.

The overall scale of public spending has been continuously reduced from the preceding fiscal year. Centering on the four main fields, such as the revitalization of cities and the activation of regional areas, the budget was selectively allocated to fields that will contribute to employment and private sector demand.

With respect to the expenses for promoting science and technology, there has been a stricter selection of the fields to be focused on with a view to improving the development of the nation. The budget was allocated effectively according to the priority of measures (the four stages of SABC) to promote creativity in science and technology. The fields to be focused on include the life sciences, information communications, environment and nanotechnology and materials. The initiative is to enhance the international competitive edge, to build a safe, secure and comfortable society, and to provide research and development projects to activate the economy.

The expenses for small and medium-sized businesses consist of the government actively supporting new businesses, such as start-ups and innovative management. The government aims at providing a safety

net and providing smooth funding for small and medium-sized enterprises that are capable and willing. The government will provide assistance for the development of human resources and the utilization of technological expertise.

(3) Future outlook

- (a) To facilitate the development of the results of reform, the government will distribute the results throughout regional areas and will continue to promote reform, aiming at sustained economic growth led by demand in the private sector.
- ① While general-account expenditures in FY2004 were kept to levels below those of the preceding fiscal year, the government made an effective allocation of the budget to areas that will benefit society and the economy and provide security for the people of Japan.
 - ② Comprehensive reform of taxation revenue was instituted over several fiscal years. In accordance with the taxation reform implemented in FY2003, considerable tax reduction equivalent to 1.5 trillion yen will continue in FY2004. Also in relation to taxation reform in FY2004, ongoing measures will be implemented to activate the economy. These measures include an extended period for the homebuyers' tax break and reduced taxation on the transfer of lands and stock investment trusts.
 - ③ With the objective of resolving the issue of bad loans in FY2004, the government will make every effort to promote a range of measures in accordance with the financial revitalization program. At the same time, the government will aim to revitalize small to medium-sized enterprises and activate regional economies by improving the functions of small to medium-sized regional financial institutions.
 - ④ Taking advantage of the designated structural reform districts, the GOJ will continue to address regulatory reform and support regional voluntary initiatives as a national initiative. In this way, the government will promote vital regional areas and create characteristic areas. These initiatives include promoting the nationwide revitalization of cities from Wakkanai to Ishigaki and creating a tourism nation aiming at establishing one tourism site in one area.
While promoting policy initiatives to expand and accelerate structural reform, the responses for the financial sector, such as the initiatives by the GOJ in building a much stronger financial system and the initiatives taken by the Bank of Japan to enhance the mechanism for spreading financial policies are crucial in defeating deflation. It is expected that such responses will lead to increased financing. It is also expected that the Bank of Japan will implement financial policy management with increased effectiveness in defeating deflation as quickly as possible.
- (b) No clear statement can be made concerning cleaning up bad loans in the coming months. This is in part because the amount of new bad debts depends on future economic trends. However, with the aim of resolving the issue on bad loans in FY2004 and of building a much stronger financial system that supports structural reform, the GOJ plans to steadily carry out these measures in the coming months.
- (c) While strictly controlling expenditure to restore fiscal health, the GOJ will continue to focus on areas that will contribute to economic growth led by the private sector. This strategy includes supporting start-ups and creating new businesses. It also includes the challenges made by small to medium-sized enterprises, and the strategic and stricter selection of a focus on science and technology. In addition to the reform of expenditure through consistent and coherent implementation of structural reform throughout fields such as regulation, finance and taxation, the government is aiming to achieve sustainable economic growth led by demand from the private sector.

7. Championing business activities at the local level

(1) Summary of BDRT recommendations

- (a) More private sector involvement in the delivery of public services should be encouraged through the use of PFI/PPP schemes.
- (b) Local governments should take a more proactive role in attracting investment beyond current efforts, for example, by offering special tax and/or regulatory incentives to potential investors.

(2) State of the measures taken thus far

- (a) Some local government have already utilized PFI/PPP schemes to arrange and operate a range of facilities. They include an environmental center, a facility for using waste heat, a study center to experience general marine culture, a youth plaza, a recycling waste disposal facility, a library, a civic cultural center, an area for parking bicycles, a recycling center, an information communications museum of science, a care house, an aged-people's home, a natural house for boys, a lifetime education center, and an NPO center. Therefore, the significance of the schemes has been understood to a certain extent, and their implementation has progressed. At the national level, PFI/PPP schemes have been adopted to construct and operate a housing complex for public servants, a research building and a student exchange building at college.
- (b)
 - ① Initiatives to attract enterprises implemented by local government in areas subject to the regional development laws include preferential treatment in taxation and other preferential measures, such as the grant of subsidies and loans with low interest rates in accordance with the laws. In areas that are not subject to these laws, each organization has implemented unique preferential measures subject to the prevailing conditions in the respective areas. These measures include granting subsidies and loans with low interest rates proportional to the amount of local taxes. Recently, initiatives have been implemented to use the structural reform system for designated districts and to fulfill the supporting system for enterprises.
 - ② The GOJ has been conducting a review of the administrative procedures to support such voluntary initiatives by local government in accordance with the Program for the Promotion of Foreign Direct Investment into Japan (March 2003, approved at the Japan Investment Council). In this way, each organization is able to provide flexible and spontaneous conditions to suitable areas.

(3) Future outlook

- (a) Taking advantage of the collection of examples of PFI/PPP schemes in Europe, which will be publicly released by the European Commission over the next few days, the GOJ will use the examples and review the possibility of holding a seminar to educate people about the significance and validity of the schemes and expertise to help the schemes be successful.
- (b) The GOJ will continue to implement the measures set out in the Program for the Promotion of Foreign Direct Investment into Japan in a consistent manner.

8. Cross border share exchanges (and related tax implications)

(1) Summary of BDRT recommendations

- (a) Reforms to the corporate revitalization laws allowing for triangular mergers between Japanese and foreign corporations should be implemented as soon as possible.
- (b) Relevant tax laws should be amended to allow for the deferral of taxation on capital gains and related asset transfers as a result of share-exchanges that take advantage of this new “triangular merger” tool.
- (c) The reforms should be incorporated into the Japanese Commercial Code (and relevant tax laws) in the next round of revisions to the Commercial Code.

(2) State of the measures taken thus far

- (a) In April 2003, the Industrial Revitalization Law was revised, and the measure of flexible counter values for mergers was introduced as a special exception of the Commercial Code (enacted on April 9). The objective of this law is to improve the productivity of Japan’s economy. From this point of view, the Minister of Economy, Trade and Industry authorizes a business plan that is intended to meet the objective and quantitative criteria. This law has enabled organizational restructuring through a merger or through share exchanges within Japan where the shares of the foreign parent company are used as a counter value.
- (b) For all aspects of the tax reform, see the appendix attached at the end of the replies in the 2nd Working Party (Accounting and Tax Systems).
- (c) Discussions regarding modernization of the corporate legislation are currently underway at the Corporate Law Subcommittee on the modernization of the Justice Ministry’s Legislative Council. Through these discussions, the Ministry of Justice has been examining the possibility of introducing modern organizational restructuring methods such as flexible counter value for mergers, including triangular mergers, cash mergers and short-form mergers.

A draft proposal concerning the organizational restructuring methods was publicly released on October 29, 2003, and Public Comments were solicited.

(3) Future outlook

- (a) The Industrial Revitalization Law was revised in April 2003. As a special exception of the Commercial Code, the measure for the flexible counter value for mergers was introduced.
- (b) For all aspects of the tax reform, see the appendix attached at the end of the replies in the 2nd Working Party (Accounting and Tax Systems).
- (c) The Corporate Law Subcommittee on the modernization of the Justice Ministry’s Legislative Council intends to continue discussions in the coming months, aiming at amending the corporate legislation regarding modernization, which is currently scheduled for 2005.

9. Legal services

(1) Summary of BDRT recommendations

- (a) Legislation before the Diet allowing Japanese and foreign lawyers to form partnerships and allowing foreign lawyers to employ Japanese lawyers as associates should be implemented as soon as possible.
- (b) Follow-on legislation should allow foreign lawyers to incorporate their law offices in the same way as Japanese lawyers are currently allowed to do.

(2) State of the measures taken thus far

- (a) The Special Measures Law concerning the Handling of Legal Business by Foreign Lawyers was amended and promulgated on July 25, 2003. The amended law will come into effect within two years of promulgation of the law based on the Cabinet order.
According to the amendment, it becomes possible for gaikokuho-jimu-bengoshi to run a joint enterprise in all legal areas with a Japanese lawyer. Also, not only offices run jointly but offices run by a gaikokuho-jimu-bengoshi alone may employ Japanese lawyers.
- (b) A bengoshi has been permitted to establish a legal professional corporation since 2004, but a gaikokuho-jimu-bengoshi is not permitted at present.

(3) Future outlook

- (a) This amendment has changed fundamentally the previous institutional framework of the association between gaikokuho-jimu-bengoshi and bengoshi and introduced the completely new system.
We imagine that it will take considerable time to conduct the various preparations required for the introduction of this new system and decided on the date of enforcement, namely “the day stipulated by Cabinet Order within the limit of two years counted from the day of promulgation.”
The Japan Federation of Bar Associations is preparing and making modifications to its rules to enforce the amended law. The GOJ also explained the interpretation of the amended law to the Japan Federation of Bar Associations. We hope to be able to bring the amended law into force as soon as possible.
- (b) To appropriately respond to the rising needs for international legal services, it is pointed out that gaikokuho-jimu-bengoshi should be permitted to establish a professional corporation as well as bengoshi. Taking this point into account, the development of needs for international legal services in Japan, the number of registrations of gaikokuho-jimu-bengoshi and also the status of the joint enterprise between gaikokuho-jimu-bengoshi and bengoshi or legal professional corporations (gaikokuho-kyoudou-jigyou), the GOJ plans to consider the possibility of permitting the establishment of gaikokuho-jimu-bengoshi professional corporations.

10. Regulatory transparency

(1) Summary of BDRT recommendations

- (a) Japanese regulators should take a proactive stance in promoting regulatory transparency and clarity. Requests for clarification, including requests for clarification outside of the “no-action letter system” should be dealt with swiftly and the findings quickly made public.
- (b) The current “no-action letter” system should be strengthened to make it legally binding and more widely used by regulators in Japan.
- (c) As a matter of standard practice, all requests for clarification, including requests for clarification received outside of the “no-action letter system” should be answered in writing.
- (d) The scope of reform should be expanded for tax-related issues to include not only requests for clarification, but also explicit prior-clearance for specific transactions, including corporate restructuring.
- (e) Further consistency is requested from the National Tax Administration in the application of relevant tax laws.

(2) State of the measures taken thus far

- (a) As indicated in the “Three-Year Programme for Promoting Deregulation (Further Revised),” as determined by the Cabinet at its meeting on March 28, 2003, the GOJ has so far adopted the following steps:
 - ① Abiding by the Administrative Procedure Laws (Law No. 88, 1993), and securing transparency in administrative procedures for giving permission/authorization and administrative guidance
 - ② Opening regulation-related administrative information through the smooth implementation of the Law Concerning Access to Information Held by Administrative Bodies, and thereby securing transparency in the effects and burdens of the regulations
 - ③ Seeking improvements in the transparency of, and ensuring fairness in, the decision-making process related to setting, amending and abolishing regulations through the procedure for submitting opinions regarding these matters (the so-called Public Comments procedure)
 - ④ Improving the predictability of the actions of private enterprises through the procedure for prior confirmation of compliance with the laws (the so-called Japanese version of the “no-action-letter” system) followed by administrative agencies, as well as securing fairness and enhancing transparency amongst administrative agencies
- (b) Although it is not clear what “legally binding” means, the reply document only shows the view based solely on facts submitted. As such, we believe it is inappropriate to provide legal-binding force to the reply document. Each ministry has exercised individual judgment concerning the extension of the subject scope.
- (c) As for the “no-action letter” system, all inquiries are to be responded to in writing. Therefore, the fact is misinterpreted.
- (d) Japanese tax authorities have taken the following steps as part of their service to taxpayers, to ensure uniformity and transparency in the handling of taxation and predictability in interpretation and application of the tax law for taxpayers.

① Instituting notices about the legal interpretation of general tax laws, announcing them through the website of the National Tax Agency while tax offices and tax offices respond to requests for consultation about individual tax transactions.

② Based on Administrative Guidelines that the National Tax Agency has released, providing written replies to pre-declaration inquiries that meet certain requirements with regard to taxation of individual transactions, and announcing their content through the website of the National Tax Agency. While the GOJ acknowledges that there are certain requirements in the subjects replied in written form in Western countries that have similar systems, the tax authorities are planning to review the requirement within this fiscal year using examples in the United States as a reference.

As the written replies suggest certain prevailing views as part of the services provided to taxpayers, and these views are premised on the relevance of the facts revealed in the pre-declaration inquiry prior to the

deadline for the declaration, it is difficult to make actual transactions legally binding.

③It is difficult to give replies that are legally binding in relation to tax systems concerning corporate restructuring. However, the national tax authorities have deployed consultants at tax bureaus around the country and implemented other initiatives to streamline the handling of specific prior inquiries from taxpayers concerning the implementation of the tax system for corporate restructuring in an effort to provide accurate responses.

(e) The related tax laws are applied appropriately to ensure appropriate and fair taxation.

(3) Future outlook

(a) According to the “Three-Year Programme for Promoting Deregulation (Further Revised),” the Japanese tax authorities plan to continue to ensure transparency regarding the regulations in the future.

(b) and (c)

The GOJ believes that the “no-action letter” system will continue to be managed by the ministries and agencies in accordance with the Cabinet decision in the coming months.

Incidentally, with respect to (b) above, the EU side stated at the Japan-EU Regulatory Reform Dialogue held in November 2003 that “legally binding” might not be the appropriate expression.

(d) Japanese tax authorities will continue to take steps to ensure uniformity and transparency in the handling of taxation and predictability in the interpretation and application of tax laws for taxpayers.

11. Telecommunications

(1) Summary of BDRT recommendations

- (a) Interconnection charges should be reduced immediately to the level of acceptable international benchmarks.
- (b) The new Telecommunications Business Law (TBL) and subsequent ministerial ordinances should contain the following:
- ① An internationally accepted methodology for competition analysis and review (The dominance of NTT companies should not be restricted to the instances of bottleneck facilities.)
 - ② Stronger regulatory accounting and information disclosure requirements on the NTT Group, and more investigative powers to the industry's prime regulator (the Ministry of Public Management, Home Affairs, Posts and Telecommunications), as well as a legal requirement for the regulator to publish the results of its investigations
 - ③ Stronger "ring-fencing" rules to prevent NTT from leveraging its dominance in the local loop to gain entry to new business areas
 - ④ An effective methodology to regulate all dominant carrier tariffs (similar in substance to the Stack Test of OFTEL)
 - ⑤ No tariff-filing requirements for non-dominant carriers, even for those designated as providing "universal services," such as local call services, under the new law
 - ⑥ Establishment of a formal appeals mechanism for regulatory decisions
 - ⑦ A requirement for the Ministry of Public Management, Home Affairs, Posts and Telecommunications to publish an annual management plan to give consumer groups and the industry advance notice of consultation on issues that may affect them
 - ⑧ A requirement that the Ministry of Public Management, Home Affairs, Posts and Telecommunications issue consultation documents setting out preliminary proposals on particular issues to draw in the views of the industry and the public
 - ⑨ A requirement that the Ministry of Public Management, Home Affairs, Posts and Telecommunications allow a minimum of six weeks for public consultations
- (c) In the long term, an independent regulator with a pro-competitive mandate should be established to supervise the telecommunications sector in Japan.

(2) State of the measures taken thus far

- (a) With the adoption of the Long-Run Incremental Cost Method in the calculation of interconnection charges in FY2000, Japan has been making efforts to reduce interconnection charges through the calculation of costs with the elimination of inefficiency in monopolistic local telecommunications networks.
- In the report made at the Telecommunications Council in March last year where the existing interconnection charges were approved, it was stated that a method based on major changes in the environment, such as a reduction in the volume of traffic and a slowdown in new investments, would be examined in relation to the method of calculating interconnection charges from FY2005. Using the Study Group on the Long-Run Incremental Cost Model, the Japanese government has been examining a long-run incremental cost model that can be used to calculate the interconnection charges from FY2005.
- (b)
- ① In November last year, the Ministry of Public Management, Home Affairs, Posts and Telecommunications developed a basic policy concerning the evaluation of the state of competition in the field of telecommunications and the details on implementation for FY2003. The Ministry is currently evaluating the state of competition in Internet connection.
 - ② In the recently revised Telecommunications Business Law, such measures were maintained as interconnection regulations on NTT East and West, regulation against anti-competitive activities, the firewall regulation within NTT Group and strict ex-ante regulations to ensure fair competition,

including those that obligate public release of accounts.

- ③ Where NTT East and West intend to conduct an operation in a new business field other than the regional telecommunications, they must meet requirements such as not obstructing fair competition in telecommunications, and are obliged to obtain authorization from the Minister of Public Management, Home Affairs, Posts and Telecommunications.

Guidelines have been established to clarify criteria to obtain authorization from the Minister of Public Management, Home Affairs, Posts and Telecommunications. In principle, Public Comments are invited concerning determinations of whether an individual application may be authorized.

- ④ The Ministry of Public Management, Home Affairs, Posts and Telecommunications is currently verifying the validity of the relationship between user fees and the related interconnection charges according to each service category at the time of authorization of interconnection charges and at the time of the revision of interconnection charges every year. The revised law stipulates the following in relation to dominant carrier fees.

(i) Where telecommunications carriers install Category I designated telecommunications facilities to provide services that cannot be provided by other carriers, the security tariff shall be established and notified.

(ii) Charges for services that fall under (i) above that have by their nature a significant impact on the users, shall be subject to a price cap within the limit of the charge standard laid down by the administration.

Further, when the charges for the services provided by the carrier concerned impede the benefits of users through unfair competition, an administrative order for business improvement may be issued.

- ⑤ Even before this revision of the Telecommunications Business Law, non-dominant carriers were not required to make an application for the authorization of charges. It was sufficient only to provide notification. Under the revised Telecommunications Business Law, the obligation to make a report concerning charges and tariffs has, in principle, been abolished. However, the obligation to report the tariffs (including the charges) is imposed to maintain universal services for all the people in Japan.

- ⑥ The Administrative Appeal Law and the Administrative Case Litigation Law have already been enacted. Therefore, anyone can protest against decisions made by the administration. For this reason, the Japanese government considers that there is no need to set up a mechanism to deal with appeals.

- ⑦ ~ ⑨ In accordance with the Cabinet decision, the Japanese government has, since April 1999, made a wide call for Public Comments through its websites and other means concerning the development of governmental and ministerial ordinances and their formulation, revision and abolition of regulations. The purpose of the Public Comments is to obtain the opinions, information and expertise of the public and to ensure fairness and transparency in the processes. When soliciting opinions and information, a time limit of one month has been set as standard, and this time limit is clearly indicated when the public announcement is made.

- (c) The Ministry of Public Management, Home Affairs, Posts and Telecommunications is independent of any telecommunications carrier. Therefore, independence from the telecommunications carriers, required under the WTO Agreement, has already been attained.

(3) Future outlook

- (a) Based on the reviews of the Long-Run Incremental Cost Model Study Group, the Ministry of Public Management, Home Affairs, Posts and Telecommunications continues to make efforts to set appropriate interconnection charges.

- (b) ① It is scheduled that, by the end of March 2004, the demarcation of the market and an analysis of the state of competition will be complete and a summary of the results released.

② ~ ⑥ As the state of the measures taken thus far suggests, the arrangement of required systems that will provide appropriate treatment is currently underway.

⑦ ~ ⑨ The Ministry of Public Management, Home Affairs, Posts and Telecommunications will

continue to invite Public Comments in an appropriate manner to obtain the opinions, information and expertise of the public and businesses, to ensure fairness and to improve transparency in the process of administrative decision-making.

- (c) With respect to the modality of regulations and regulatory bodies, each country should adopt an optimum system for the purpose of promoting competition. Japan has been successful in the creation of a competitive market in the telecommunications field. Therefore, we consider that there is no need to change the existing system.

12. Universal Banking

(1) Summary of the BDRT recommendations

- (a) The GOJ should, in full compliance with the spirit of the financial Big Bang, continue to work towards liberalizing all of the artificial barriers, or “firewalls,” separating banking, securities, asset management and insurance industries. It can do so while ensuring an appropriate product regulatory and approval framework, the protection of client information, and renewed emphasis on the fiduciary duties of financial intermediaries.
- (b) Article 65 of the Banking Law, which prevents banking firms from conducting securities business and vice versa, should be abolished.

(2) State of the measures taken thus far

- (a) As financial institutions have a public responsibility with respect to their business, it is appropriate to restrict their activities in other businesses to maintain soundness, to ensure fair competition and to prevent conflicts of interest. On the other hand, the GOJ lifted the ban on the establishment of financial holding companies in March 1998, which enabled the establishment of financial groups consisting of several types of businesses. This action was taken in response to changes in the economic and social environment to promote competition, to streamline management in the financial field and to respond to user needs for greater sophistication and diversity.
- (b) In April 1993, the ban on entering the securities market through a subsidiary was lifted.
In December 1998, the ban on over-the-counter sales of investment trusts by parent banks was lifted.
In October 1999, the limit on the scope of operations engaged in by the subsidiaries of securities firms was abolished.

(3) Future outlook

A bill to lift the ban on intermediary businesses by banks for securities (intermediaries for shares and corporate bonds, etc.) is scheduled to be submitted at the current session of the Diet.

13. Food additives

(1) Summary of the BDRT recommendations

The 46 food additives submitted by the Ministry of Health, Labor and Welfare (MHLW) to the Food and Sanitation Control Council on December 19, 2002 should be reviewed and approved for use in Japan by the end of 2003.

(2) State of the measures taken thus far

In accordance with the risk assessment conducted at the Food Safety Commission, the Pharmaceutical/Food and Sanitation Control Council of the Ministry of Health, Labor and Welfare will conduct risk management for the 46 food additives submitted to the Pharmaceutical/Food and Sanitation Control Council. The safety of these 46 food additives has been confirmed at an international committee of experts (Joint FAO/WHO Expert Committee on Food Additives: JECFA) and their use has been widely approved in European nations, irrespective of the request for designation from businesses. The GOJ will take the lead with respect to the approval of these 46 food additives, and progress has been made, starting with items for which necessary information has been prepared.

Fragrant materials that are widely used internationally are treated in the same manner as the 46 food additives mentioned above. In accordance with the method of safety assessment decided in January this year, the safety of each ingredient in each fragrant material is to be assessed.

So far, the Food Safety Commission has been requested to assess the safety of seven food additives, including polysorbate, and six fragrant materials.

The Ministry of Health, Labor and Welfare has been conducting as quick an assessment as possible through the collection of information and the implementation of the required additional tests. The Ministry of Health, Labor and Welfare would like to ask the EU to cooperate with the Japanese side to facilitate these procedures through the provision of information that forms the basis of such scientific assessment.

(3) Future outlook

Since its establishment on July 1, 2003, the Food Safety Commission has been in charge of assessing the risks of food additives and their impact on health. By respecting the assessment of the effects of the food additives on health to Food Safety Commission, the Ministry of Health, Labor and Welfare will continue to prepare data of food additives whose assessment is complete. As a risk management body, the Pharmaceutical/Food and Sanitation Control Council will examine sequentially whether the food additives for which data has been prepared can be approved as food additives.

14. Insurance

(1) Summary of the BDRT recommendations

All requirements for prior product approval and pricing involving the FSA should be abolished in favor of a regulatory regime that focuses on macro-level supervision of solvency ratios, capital adequacy and modern accounting practices.

(2) State of the measures taken thus far

With respect to non-life commercial product lines, the system of notification-in-principle was introduced in August 1999. For most of the other products, the notification system was introduced in July 2001. In this way, major deregulation has progressed. On the other hand, when it comes to personal product lines, the GOJ considers that the aspect of protection of policyholders is crucial. Therefore, only some product lines are subject to the notification system. We think that regulations at a certain level should be required also in terms of premium rates.

(3) Future outlook

Given a move to review “the file and use system” even overseas, the reduced level of freedom in product development resulting from the fact that all examination items and standards need to be defined in a comprehensive manner as a precondition for the introduction, and the need for adequate screening for the protection of policyholders, the GOJ is not planning to go beyond the existing system and introduce the “the file and use system” or the notification system. It is not planning to reduce the requirements for product approval set out by the authorities, including abolition of the approval system, either.

15. In-vitro diagnostic products

(1) Summary of the BDRT recommendations

- (a) Reforms of the regulations governing the approval of the in-vitro diagnostic products (IVDs) in Japan with changes to the Pharmaceutical Affairs Law (PAL) establishing a risk-classification mechanism should be fully compatible with international practice and result in meaningful deregulation of the product approval process.
- (b) Any new regulations governing the quality system should also be based on global standards.

(2) State of the measures taken thus far

Concerning the approval of IVDs, according to the revised PAL to be implemented on April 1, 2005, to ensure international standards, Public Comments were invited for the introduction of the standards of the basic requirements agreed upon at the Global Harmonization Task Force (GHTF) and STED to be used as a format for the outline of the data attached to the application form for approval.

According to the revised PAL to be implemented on April 1, 2005, it is scheduled that the quality control rules applied to the IVDs will follow ISO13485:2003. Public Comments were also invited for this matter.

Based on the submitted comments, the necessary procedures have been conducted for implementation of the revised PAL.

(3) Future outlook

To facilitate the implementation of the revised PAL on April 1, 2005, it is scheduled that the required ministerial ordinances and notices will be issued during FY2004, concerning the procedures related to the approval of the IVDs and detailed regulations, such as the quality control rules.

To ensure consistency between the regulations concerning IVDs and the international regulations, the GOJ intends to incorporate, if required, the results of discussions at GHTF, in which Japan and the EU will participate.

16. Animal health products

(1) Summary of the BDRT recommendations

- (a) The mandatory national assay for biological products should be replaced with a system that allows for speedy batch release with a simple notification report submitted by manufacturers based on in-house controls, as is common practice in Europe. The reliability of in-house testing can be confirmed by testing the first few production batches, followed by random sampling thereafter.
- (b) The mandatory national assay for all in-vitro diagnostic products should be eliminated immediately.
- (c) The national assay for manufactured/imported feed additives should be abolished after the introduction of Good Manufacturing Practice (GMP) on an industry-wide basis. In the meantime, producers that already employ GMP should be given an exemption from the national assay requirement. Sampling procedures should also be rationalized (e.g. by using attached samples) to eliminate the waste associated with current practices.
- (d) Reports prepared for New Animal Drug Application should be accepted in their original language with a summary in Japanese, as is currently the practice for pharmaceutical products intended for human use.
- (e) The acute toxicity study employing animals for mycelical (feed grade) products, a test unique to Japan, required for each batch to detect toxic substances should be eliminated.

(2) State of the measures taken thus far

- (a) According to the results of national assay, the partial abolition and simplification of national assay approval regarding animal-use biological agents have been gradually implemented since 1985, based on the results of national approval. Principal cases of partial abolition or simplification have been as follows:
 - FY1985 Abolition of quantitative tests for antiseptic agents and qualitative tests for concentration cerebral agents.
 - FY1986 Abolition of the national assay approval system for some IVD (antibody measurement).
 - FY1992 Abolition of special property tests and humidity-inclusive tests.
 - FY1995 Abolition of pH testing, and partial abolition of abnormal toxicity denial tests.
 - FY 1996 Relaxation of the sealing units of national assay approval certification stamps.
 - FY1999 Abolition of titer tests for some agents.
- (b) As mentioned above, the test for in-vitro diagnostic products was abolished for those whose antibodies are measured.
- (c) As GMP has been introduced since July 1, 2003, the national examination has been abolished for feed additives manufactured at establishments that comply with the standards.
- (d) Where documents attached to applications for veterinary products are written in foreign languages, the attachment of full Japanese translations is required. For figures, however, the original language is permitted.
- (e) As a result of reviewing the necessity of the acute toxicity test for each batch, the test has been abolished since July 1, 2003.

(3) Future outlook

- (a) The national examination for biological drugs for animals has been conducted for vaccines where agents of disease are used in the manufacturing process and where a considerable level of expertise is required in manufacturing the vaccines and in ensuring safety, in accordance with the Pharmaceutical Affairs Law. As around 1% of the samples currently fail the examination every year, it is necessary to maintain this system.
- (b) The in-vitro diagnostic products requiring the national assay have a direct impact on the measures to prevent epidemics at the national level in accordance with the result of such diagnosis. Therefore, it is necessary to approve the distribution only of those whose effectiveness has been confirmed.
- (c) Since July 1, 2003, the national examination has been exempted for feed additives manufactured at establishments that comply with the standards.
- (d) It is necessary to attach a range of information to the application for approval of new animal drugs. This information needs to be translated into Japanese to allow the examination to proceed smoothly.
- (e) The test concerned was abolished on July 1, 2003.

17. Tax reform to facilitate investment in Japan

(1) Summary of the BDRT recommendations

We recommend the GOJ review the following two points, which we have positioned as future issues to continue the revitalization of the Japanese economy.

(a) A new rule for the participation exemption of dividends and capital gains from taxation

To promote direct investments into Japan, participation exemption is implemented, by which dividends and capital gains received from business investment are exempted from taxation.

(b) Improvement of the CFC (tax haven) tax system

It is necessary to improve the Japanese CFC tax system and to examine it to establish a stable legal framework that is not influenced by yearly performance.

(2) State of the measures taken thus far

For all aspects of the tax reform, see the appendix attached to the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

(3) Future outlook

For all aspects of the tax reform, see the appendix attached to the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

The 2nd Working Party (accounting and tax issues)

18. Adoption of international accounting standards

(1) Summary of the BDRT recommendations

- (a) We hope that the GOJ and the EC will closely observe the progress of IASB projects, encourage extensive discussions among all stakeholders, seek to integrate their opinions, and be involved actively in the formation of IAS through the activities of the International Organization of Securities Commissions (IOSCO) and the Standard Advisory Commission (SAC) with the IASB.
- (b) Further, to address our particular concerns about performance reporting, we ask the GOJ and the EC to convey our opinions on this subject to the professional bodies advising them, and to the IASB.
- (c) We recommend that the GOJ commits itself to IAS and established a timetable for adoption of IAS by listed companies in Japan.

(2) State of the measures taken thus far

The GOJ has been involved in the formation of the international accounting standards (IAS) through activities of the International Organization of Securities Commissions (IOSCO) and the Standard Advisory Commission (SAC) with the IASB. The Financial Services Agency has submitted a comment concerning the review of the articles of association of the IASC Foundation, stating, “The IASB should set up sufficient opportunities to record the concerns of interested parties for its activities for setting accounting standards, and should give sufficient consideration to such concerns in the process of setting accounting standards.”

From Japan, the Accounting Standard Board of Japan (ASBJ), the primary body for setting accounting standards, has issued opinions to each accounting standard, including the performance report. The GOJ has also conveyed the concerns of interested private parties to the IASB.

Where overseas accounting standards are acknowledged as sufficient for the protection of investors in accordance with the Securities Exchange Law, it is permissible for a foreign company to submit financial documents produced in accordance with the accounting standards approved in its home country. The financial documents of German companies produced in accordance with IAS adopted by the German Commercial Code have been already acknowledged as acceptable.

(3) Future outlook

The GOJ will continue to be actively involved in the formation of the international accounting standard through activities of IOSCO and the SAC with the IASB. We consider that the ASBJ will continue to issue opinions on the maintenance of each accounting standards. The GOJ also intends to convey the concerns of interested private parties to the IASB.

The Accounting Standards Council is now examining how the financial documents based on IAS are positioned in terms of the Japanese legal system.

19. Transfer pricing

(1) Summary of the BDRT recommendations

We request further development of international common rules to prevent double taxation and to reduce compliance costs.

- (a) Implementation of rules consistent with the OECD's Transfer Pricing Guidelines
- (b) Support for discussion in the OECD on the standardization of Advance Pricing Agreements

(2) State of the measures taken thus far

- (a) Conventionally, the transfer pricing taxation in Japan has been implemented in accordance with the legal imperatives and the notices for interpretation of legal imperatives. The taxation system has been operated in compliance with the OECD's Transfer Pricing Guidelines. The basic policy concerning implementation of the administrative guidelines issued in June 2001 states that, "the GOJ will make an effort for appropriate implementation using the OECD's Transfer Pricing Guidelines as a reference if required."
- (b) The OECD has developed the Transfer Pricing Guidelines and identified the concepts regarding the arm's length principle for calculating transfer pricing, the method of calculating transfer pricing, the settlement of disputes regarding transfer pricing and for the prevention of double taxation and the procedures for mutual discussion (APA: Advance Pricing Agreements). Each authority has provided a policy for conducting transfer pricing taxation.

Recent discussions regarding transfer pricing taxation at the OECD have considered the issue of comparability and the application of the arm's length principle for transactions between head offices and branches. Therefore, the OECD has solicited extensively for opinions and comments from the private sector. Through the active participation in these discussions at the OECD, the GOJ has been trying to prevent double taxation and to reduce compliance costs.

(3) Future outlook

The GOJ will continue with the implementation in accordance with the OECD's Transfer Pricing Guidelines in the coming months, and will continue to be actively involved in discussions at the OECD to prevent double taxation and to reduce compliance costs.

20. Improvements to the consolidated tax system

(1) Summary of the BDRT recommendations

We hope that the GOJ will reform the system, abolishing the 2% surtax and allowing the carrying forward of tax losses in subsidiaries before the system came into effect. In accordance with the principle of tax neutrality, the discriminatory treatment of consolidated taxation should be abolished.

(2) State of the measures taken thus far

For all aspects of the tax reform, see the appendix attached to the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

(3) Future outlook

For all aspects of the tax reform, see the appendix attached to the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

21. Electronic commerce taxation

(1) Summary of the BDRT recommendations

Invite the GOJ to intensify its study of the OECD's principles on e-commerce taxation

(2) State of the measures taken thus far

For all aspects of the tax reform, see the appendix attached to the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

(3) Future outlook

For all aspects of the tax reform, see the appendix attached to the end of the replies in the 2nd Working Party (Accounting and Tax Systems).

(Appendix)

Proposals Related to the Taxation System

Taxation revisions are determined according to the discussions at the Tax Research Commission of the ruling party of the GOJ, with consideration given to the economic condition and the financial situation. The revisions are also determined according to the requests and opinions given by the ministries and the agencies to the tax authorities in the taxation revision process every year. Therefore, the opinions submitted by various bodies and organs, including the BDRT, have been used as a reference in producing requests for taxation revisions by the ministries and agencies, and have been incorporated in the taxation revisions every year.

In the 5th EU-Japan BDRT recommendations, proposals related to the taxation system were made in the following fields:

- The 1st Working Party – International Trade and Investment
 - 2. Eliminating tax-related barriers to investment (prevention of double taxation and transfer pricing taxation)
 - 4. Facilitating business developments: The arrangement of legal and tax systems
 - 8. Cross-border stock swaps and related tax implications
 - 17. Tax reform to facilitate investment in Japan
- The 2nd Working Party – Accounting and Tax Systems
 - 19. Transfer pricing taxation
 - 20. Improvements to the consolidated tax system
 - 21. Electronic commerce taxation

Of the above fields, the consolidated surtax mentioned in Item 20, Improvements to the consolidated tax system, will be abolished following the schedule of the draft taxation revisions for FY2004.

We would like to use requests that are deemed appropriate as a reference for improving the business environment.

To promote international exchanges in investment, the GOJ signed in November last year a newly reviewed treaty that will comprehensively renew the existing tax treaty with the United States (concluded in March). The new treaty is based on OECD's treaty model. Under the new treaty, taxation in a country where withholding tax is imposed on the payment of dividends, interest and loyalty will be significantly reduced. With the introduction of the reduced rates and exemptions, measures to prevent abuse of the treaty and the avoidance of taxation will be implemented.

Regarding the Japan-U.S. treaty as the basic policy, the GOJ intends to revise the existing tax treaty and conclude a new tax treaty with European nations if needed in the coming years.

The 3rd Working Party – Information and Communications Technology (ICT)

22. Attainment of the IT society aimed at by e-Japan/eEurope to promote economic growth and help solve social problems

(1) Summary of the BDRT recommendations

The following actions should be promoted to attain the IT society aimed at by eJapan/eEurope and to promote economic growth and help solve social problems

- (a) Solution of social problems (e.g. unemployment) through the eJapan/eEurope initiatives
- (b) Public authorities at the national level should lay down specific national targets for broadband subscribers
- (c) Development of solutions and business models
- (d) Global expansion of high-quality broadband networks and ensuring their interoperability
- (e) Creation of business opportunities through cooperation with communities
- (f) Development of new business models through linkage between telecommunications and broadcasting with the appropriate regulatory conditions

(2) State of the measures taken thus far

- (a) In e-Japan Strategy II, which was decided at the IT Strategic Headquarters in July 2003, pioneering initiatives were developed in seven leading areas that are crucial for Japanese people. These areas are: medical services, food, lifestyle, financing for small and medium-sized enterprises, expertise, employment and labor, and the public service. In the e-Japan Priority Policy Program 2003 that was decided at the IT Strategic Headquarters in August 2003, specific measures were included. The office and ministries in charge are currently engaged in the initiatives.

The IT Strategic Headquarters established the Acceleration Package for e-Japan Strategy II in February 2004, setting out the priority policies in six areas that the government should address. They are: international strategy in the IT field in Asia, the implementation of security policies (safety and security), the promotion of content policies, the promotion of IT regulatory reform, and promotion of the e-government and e-local government. These policies will strongly aid in the attainment of the IT society.

- (b) In August 2003, the government developed the e-Japan Priority Policy Program – 2003 to achieve the targets set out in e-Japan Strategy II. This program explicitly suggests specific measures in the seven main areas mentioned in e-Japan Strategy II, namely, medical services, food, lifestyle, financing of small and medium-sized enterprises, expertise, employment and labor, and the public service. While the public and private sectors are jointly promoting the use of the Internet infrastructure, the government intends to continue to address the five areas in which particular measures should be taken to attain the sophisticated information and communications network society set out in the e-Japan Strategy. The five areas are: the formation of the world's most sophisticated information and communications network; the development of human resources, education and learning; the promotion of electronic commerce; the promotion of administration and the use of information and communications technology in public areas; and the security, safety and reliability of a sophisticated information and communications network.

- (c) New solutions and business models have been created in a competitive market to allow businesses to develop in response to market needs. Adequate risks and cooperation between the players are a product of how well IT is utilized in corporate management. In the report of the Information Technology Strategy Council that was produced to promote the use of information technology, it has been pointed out that the management style in which information technology is used is directly linked to competitive advantage in business.

To promote e-government in Japan, a Chief Integration Officer (CIO) has been assigned to each ministry, as a means of using IT. The role of the CIO is to design the overall operational and system structures.

This system has also been implemented in private companies.

The government produced e-Japan Priority Policy Program – 2003, decided at the IT Strategic Headquarters in August 2003, to promote the manner in which it addresses the seven main areas in e-Japan Strategy II. The government should implement these measures quickly and in a focused manner. The related ministries and agencies are currently implementing these measures. To accelerate the initiatives set out in e-Japan Strategy II, the government produced the Acceleration Package for e-Japan Strategy II, decided at the IT Strategic Headquarters in February 2004. These policies are critical across

a number of ministries and agencies. The government will address these policies through cooperation between the ministries and agencies.

- (d) In the e-Japan Priority Policy Program – 2003, the GOJ has defined the means by which it will promote the development of international relations centered on IT. The GOJ has been implementing specific measures to promote international exchanges and activities for international standardization. These measures include joint experiments and research and development initiatives between nations. The GOJ has promoted research and development initiatives regarding the application of technology that assumes the ubiquitous network environment where all information devices and electronic devices inside and outside houses are connected. Since FY2003, the government has been engaged in a three-year research and development project into the sharing and standardization of the base technology for providing security for connectivity and operability of different information devices. The research has been directed toward abstracting and resolving issues, and had defined nine items that will enable sharing and standardization to be achieved by FY2005, including the authentication method and security.
- (e) The Small and Medium Enterprise Agency and the Japan Small Business Corporation have been offering consultation services, providing loans and holding seminars in support of small businesses using IT and networked businesses conducted by small or home offices. Support for networked businesses has also been provided at the level of local government as part of the support for small and medium-sized enterprises.
- (f) In accordance with the e-Japan Priority Policy Program – 2003, the GOJ supports the developers of the technology for the convergence of telecommunications and broadcasting through subsidies for development and the opening of the required facilities. This support promotes the digitization of broadcasting and places Japan ahead of other countries in creating a service where telecommunications and broadcasting are converged. This service enables members of the public to obtain and use different forms of information, such as public information, easily and safely without requiring them to undergo any special training in the combined use of digital broadcasting and the Internet. The initiatives are in accordance with the law concerning the promotion of development of technologies for communications and broadcasting convergence.

The government intends to set up an environment that facilitates distribution of digital content whose intellectual property rights are appropriately protected. This initiative is intended to enable desirable content to reach more people. The government will be involved in research and development to facilitate the clearing of copyrights and the distribution of content.

As part of the research and development, the government intends to develop a mechanism for managing access to multimedia information distribution services and membership services. The government intends to verify the effectiveness from the aspect of building of a service model based on the multi-functional IC chip framework and from the aspect of creating IT services in new fields.

(3) Future outlook

- (a) To implement e-Japan Strategy II, the GOJ will steadily promote the e-Japan Priority Policy Program – 2003 and the Acceleration Package for e-Japan Strategy II. The government will actively address achieving the e-Japan strategy through the development of e-Japan Priority Policy Program – 2004 in the coming summer.
- (b) Through the development of the Acceleration Package for e-Japan Strategy II in February 2004, the GOJ intends to accelerate e-Japan Strategy II. With the implementation of this package, the government intends to achieve its target of having 30 million households with access to high-speed Internet and 10 million households with access to ultra high-speed Internet by 2005.
- (c) New solutions and business models have been created in a competitive market to allow businesses to develop in response to market needs. Adequate risks and cooperation between the players are a product of how well IT is utilized in corporate management. In the report of the Information Technology Strategy Council that was produced to promote the use of information technology, it has been pointed out that the management style in which information technology is used is directly linked to the competitive advantage in business.

To promote e-government in Japan, a Chief Integration Officer (CIO) has been assigned to each ministry, as a means of using IT. The role of the CIO is to design the overall operational and system structures. This system has also been implemented in private companies.

- (d) The GOJ intends to fast-track the e-Japan Strategy II through the development of the Acceleration Package for e-Japan Strategy II in February 2004. We consider that the implementation of the measures in this package will facilitate the establishment of a network environment that connects the different parts of the world in a seamless, high-speed and high-quality manner.
- (e) Networked businesses that use IT will create employment opportunities for women, younger people and the elderly. Businesses will therefore be able to offer employment opportunities at home, thereby increasing the flexibility for managing children and their education and promoting development in regional areas. It is important to enable information to be exchanged much more cheaply and more smoothly through the accelerated introduction of the broadband service. The prompt exchange of software and content using IT will facilitate education over long distances and will contribute to educational and cultural exchange. When a local currency is circulated smoothly using IT, the local economy becomes energized, facilitating the provision of services and exchanges, resulting in reduced social anxiety and activation of the local area. The GOJ will continue to support networked businesses using IT in recognition of its significance.
- (f) The GOJ intends to accelerate e-Japan Strategy II through the development of the Acceleration Package for e-Japan Strategy II in February 2004. It is believed that implementation of the measures stipulated in the section, "Promoting Content Policies" in this package will promote the development of a new business model through cooperation between telecommunications and broadcasting.

23. Introduction of broadband services by the government and private sector (issues of the protection of copyrights, etc.)

(1) Summary of the BDRT recommendations

While the private sector should actively promote the construction and implementation of business models that capitalize on broadband services, the government should promote policies to develop an environment that facilitates the use of broadband services.

(2) State of the measures taken thus far

In the e-Japan Priority Policy Program – 2003, the government intends to arrange the environment for smooth distribution of digital content whose intellectual property rights are appropriately protected. This initiative is intended to enable desirable content to reach more people. The government will be involved in research and development to facilitate the clearing of copyrights and the distribution of content.

As part of the research and development, the government intends to develop a mechanism for managing access to multimedia information distribution services and membership services. The government intends to verify the effectiveness from the aspect of building of a service model based on the multi-functional IC chip framework and from the aspect of creating IT services in new fields.

To provide an environment in which high-speed and super high-speed Internet is accessible from anywhere in Japan, the GOJ has been strengthening the required regulatory reform, competition policies, research and development and tax incentives. The government has also been implementing special measures in areas where it is difficult for such services to be established as a business.

(3) Future outlook

The GOJ intends to accelerate e-Japan Strategy II through the development of the Acceleration Package for e-Japan Strategy II in February 2004. It is believed that implementation of the measures stipulated in the section, “Promoting Content Policies” in this package will strengthen the environment for promoting the use of broadband services.

24. Monitoring of the progress of eJapan/eEurope

(1) Summary of the BDRT recommendations

It is necessary to monitor the progress of eJapan/eEurope periodically. Both the government and the private sector should develop and implement the required actions.

(2) State of the measures taken thus far

The government has been conducting a follow-up survey twice a year to verify the progress of implementing the e-Japan Priority Policy Program developed each year by the government in accordance with e-Japan Strategy. The e-Japan Strategy is to be implemented quickly and in a focused manner to facilitate the establishment of a sophisticated information and communications network society.

In addition, the special assessment advisory committee was set up under the IT Strategic Headquarters in August 2003, and it has initiated assessments concerning the state of approaches taken by the government in terms of e-Japan Strategy II in relation to the private sector.

(3) Future outlook

The GOJ plans to continue conducting periodic follow-up surveys concerning the progress of the e-Japan Priority Policy Program.

In addition, it is scheduled that the special assessment advisory committee of the IT Strategic Headquarters will submit an interim report in April 2004. The government plans to incorporate the results of the report on the e-Japan Priority Policy Program – 2004 scheduled to be developed in the summer of this year.

25. Improvement of an environment to accelerate investment in broadband services

(1) Summary of the BDRT recommendations

With stimulation of investment in broadband infrastructures and services, a competitive environment that ensures that a level playing field exists for all markets participants should be established.

(2) State of the measures taken thus far

In the revised Telecommunications Business Law approved in July last year, the GOJ has been aiming to rationalize the regulations throughout the systems, including abolishing the business categories of Type I and Type II, etc. The government has been engaged in creating a competitive environment.

In the e-Japan Priority Policy Program – 2003, the government intends to accelerate the required regulatory reform, implement competition policies and conduct research and development to create an environment where high-speed and super high-speed Internet is accessible from anywhere in Japan. As a measure for promoting free competition and providing a level playing field, the government plans to improve the functions of the Telecommunications Business Dispute Settlement Commission and continue to implement a fundamental review of the systems relating to telecommunications and the functions of NTT. The government will implement these measures as quickly as possible, setting its sights on ensuring sovereign authority over telecommunications and the trends of international competition.

(3) Future outlook

With the development of the Acceleration Package for e-Japan Strategy II in February 2004, the GOJ intends to accelerate e-Japan Strategy II. Implementation of this package is considered a means of creating an environment to promote investment in broadband infrastructure and services.

The 4th Working Party (WTO)

26.

(1) Summary of the BDRT recommendations

- (a) We strongly believe that, at a time of growing global political concern and economic uncertainty, further liberalization of international trade and investment will have a decisive impact on world's economic growth.
- (b) We do reaffirm that it would be essential to achieve a successful and timely conclusion of the ambitious multilateral trade Round agreed in Doha. We urge all WTO members, including the European Union and Japan, to accelerate the process to complete negotiations by the target date of 1 January 2005. In particular, we encourage the European Union and Japan, together with the United States, to take a leading role to push the negotiation forward. We also note that European Union and Japan share a common position on many issues and expect both parties to pursue closer mutual cooperation.
- (c) We strongly support the comprehensive approach of a new round negotiation to address every negotiation agenda without excluding any specific agenda.
- (d) We encourage all WTO members to achieve a successful outcome of the Fifth WTO Ministerial Conference in Cancún, Mexico, in September 2003, to deliver the necessary progress, including the formal launch of negotiations on all the Singapore issues, which would allow for the timely completion of the Round under the single undertaking approach.
- (e) We recognize the central role of developing countries for the success of the new Round. We therefore expect the negotiation to incorporate consideration of the needs of developing countries in the process, and encourage the European Union and Japan to continue the effort for "capacity building," in order to allow more effective participation of developing countries in the WTO's decision-making process.
- (f) We emphasize that all WTO members should fully comply with all their WTO commitments.
We are deeply concerned about the emerging trend of protectionism and the move to trade distorting measures, which overshadow the WTO negotiation process. We ask all countries to conform to multilateral rules, and call for the European Union and Japan to confront protectionism by reinforcing the multilateral principles of openness and non-discrimination.
Recognizing the importance of intellectual property rights in today's economy, we urge in particular the European Union and Japan to monitor the infringements of these rights, and to take appropriate actions, when necessary.
- (g) We welcome the fact that the European Union and Japan are constructively working together with the aim of making progress in the negotiations and achieving successful results. We encourage the European Union and Japan to continue to maintain close contacts with the representatives of the private sector.
- (h) We hereby agree that we shall continue to study individual agenda items in detail, and to provide policy proposals from time to time in response to the progress of government to government negotiations.
(In addition, additional recommendations are mentioned in the appendix.)

December 18, 2003

The EU-Japan Business Dialogue Round Table

Joint Declaration Asking the World Trade Organization (WTO) for the Early Resumption of a New Round of Negotiations

With the progress of globalisation, it is indispensable for WTO member states to expand access to free markets for agricultural and non-agricultural products, and to establish rules that are suitable for the new economic environment. These rules include investment rules, the facilitation of international trade, the protection of intellectual property rights and anti-dumping regulations.

For the development of international trade in goods and services, multilateral solutions, including a means of bringing developing countries into the international system in a fair manner, are necessary. It is likely that a bilateral approach will not provide a satisfactory solution in the current economic environment.

Participants of the EU-Japan Business Dialogue Round Table regret that a consensus was not reached to allow new round of trade negotiations gain momentum at the WTO Ministerial Conference held in Cancun, Mexico, in September. It is likely that the failure to provide a new stimulus to world trade would have a negative impact on the current circumstances. Therefore, we must request again an early resumption of the negotiations.

In addition, the Round Table requests that all interested parties will exhibit flexibility to ensure that a result is achieved that will satisfy all interested parties as quickly as possible. From this point of view, we believe it is necessary to review how discussions are conducted at the WTO.

(2) State of the measures taken thus far

- Following the Doha Ministerial Declaration in 2001, we have been actively engaging in the Doha Development Agenda negotiations, which include the issues of agriculture, non-agricultural market access, services and rules such as anti-dumping rules. New areas known as the Singapore Issues, including trade facilitation and investment, are also subject to discussion. The GOJ has participated in the negotiations to obtain balanced and comprehensive results as early as possible, focusing not only on market access, but also on the areas of rule-making and its strengthening
- As the DDA round of negotiations aims at development, the GOJ has been intensifying dialogues with developing members and nations and has placed emphases on building the trade related capacity of developing members so that they can benefit sufficiently from the trade expansion.
- Protection of intellectual property rights is critical for the industries in Japan, and we have been observing the compliance of the TRIPS Agreement by WTO members such as China.

(3) Future outlook

- After the Ministerial Conference in Cancun in September last year, the DDA negotiations have stalled. Since the beginning of this year, however, the members have shown their will to reactivate the negotiations. Japan continues to make its utmost effort to reinvigorate the round so that an early conclusion can be reached with an ambitious and well-balanced package that responds to the interests of the members, including Japan.
- Specifically, we will aim at reaching a consensus regarding a realistic framework on agriculture and non-agricultural market access by the middle of this year. We will also make an effort to achieve meaningful outcomes in other areas, such as AD and the Singapore Issues.
- Negotiations on the Singapore Issues shall be initiated in areas where consensus can be reached, such as trade facilitation. Ways to address other issues shall be examined in a flexible manner within the WTO agenda.
- We will engage in restarting the negotiations, not only through the talks in Geneva, but also through various contacts with our counterparts in their capitals. We will offer meaningful inputs at Geneva through discussions with developed and developing members.
- The GOJ has made frequent contacts with the private sector, including exchanges of opinions with the Japan Federation of Economic Organizations. The government continues to cooperate with the private sector.