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**VARIOUS REQUIREMENTS UNDER JAPAN'S TOBACCO
EXCISE TAX LAW AND TOBACCO BUSINESS LAW
ARE INCONSISTENT WITH JAPAN'S WTO OBLIGATIONS**

This paper reviews the consistency of the Japanese specific excise tax regime, as set forth in the Tobacco Excise Tax Law¹ as well as the Leaf Purchase Obligation ("LPO") and retail list price approval system provided for in the Tobacco Business Law² imposed under the Tobacco Business Law with Japan's obligations under the law of the World Trade Organization ("WTO").

The Tobacco Excise Tax Law and the Tobacco Business Law were jointly adopted in 1984 to reorganize the tobacco market in Japan following the termination of the monopoly system. The purpose of this reorganization "is to foster the sound development of the Japanese tobacco industry, and thereby contribute to the stable maintenance of fiscal revenue and the sound development of the national economy, by making necessary adjustments with respect to the production and purchase of domestically produced leaf tobacco as the raw material of manufactured tobacco, and with respect to business operations and the like pertaining to the manufacture and sale of manufactured tobacco."³

As detailed below, measures provided for under the Tobacco Excise Tax Law and Tobacco Business Law have distorted the conditions of competition to the benefit Japan Tobacco Incorporated ("JT"), the sole producer of tobacco products in Japan. These measures have also served to ensure unwarranted protection to domestic tobacco growers as JT is purchasing the entire domestic production of tobacco leaf at prices significantly higher than those of competing imported tobacco leaf. The opacity of the retail list price approval system also makes it difficult for imported tobacco products to access the Japanese market at fair and competitive price levels.

¹ Tobacco Excise Tax Law of 10 August 1984, as last amended on 2 December 2011.

² Tobacco Business Law of 10 August 1984 (Law No. 68) as last amended by Law No. 147 of 1 December 2004.

³ *Id.*, Article 1.

1. Japan's two-tier excise tax system is inconsistent with the non-discrimination obligation of GATT Article III:2

As a rule, under Japan's Tobacco Excise Tax Law, cigarettes are subject to a specific excise tax of 5,302 Yen per mille.⁴

Tobacco Excise Tax			
Category	National Tax		
	Tobacco Excise Tax	Special Tobacco Tax	Subtotal
	(Yen per mil sticks)		
Cigarettes	5,302	820	6,122
Pipe			
Cigars			
RYO, Chew and Snuff Tobacco			
Former Third Grade Tobacco	2,517	389	2,906

Source: Ministry of Finance Japan, www.mof.go.jp/tax_policy/summary/consumption/127.htm

However, pursuant to this same law, certain cigarettes, i.e., cigarette brands that were formerly classified as "Third Grade" brands at the time of abolition of the tobacco monopoly in 1985, are subject to a much lower specific excise tax of 2,517 Yen per mille.⁵ The Third Grade brands to which this exceptional and favorable tax rate applies, were all launched by the Japan Tobacco Corporation, the predecessor of JT, during the monopoly period.⁶ Only the brands listed as classified Third Grade brands in 1985, and thus only JT brands, enjoy the beneficial tax treatment.

In sum, brands imported and distributed in Japan by British American Tobacco Japan and Phillip Morris Japan are subject to the standard specific excise tax rate 5,302 Yen per mille and will never be able to benefit from the favorable tax rate that applies to domestic former Third Grade brands.

Third Grade brands have benefited from Japan's excise-tier system as their market share doubled between 2010 and 2012.⁷ Market research reveals that traditional consumers of imported cigarette brands in Japan switched to these former Third Grade brands.

⁴ *Id.*, Article 11.

⁵ *Id.*, Supplementary Provision, Article 2. In practice, this means that a Third Grade product currently costs on average 240 Yen, of which 116 Yen (about 47% of the price) is the amount of tax paid while a mainstream cigarette price sells for on average 410 Yen of which more than 244 Yen (about 60% of the price) is the amount of taxes paid.

⁶ It concerns the following brands: Golden Bat, Shinsei, Echo, Wakaba, Uruma and Violet.

⁷ These Third Grade brands had a 4% market share in 2012, a significant increase compared with their market shares before 2010. This increase is a result of the increased gap between the price of mainstream products and the very low cost Third Grade brands as a consequence of the difference in excise taxes.

In particular since the tax hike of October 2010 which made all products significantly more expensive, the appeal of the more affordable Third Grade products has increased.

EU-27 Cigarette Exports to Japan

2010		2011		2012	
Volume (kg)	Value (€)	Volume (kg)	Value (€)	Volume (kg)	Value (€)
48,266,800	420,364,545	65,936,700	495,741,136	55,834,000	427,715,578

Source: EUROSTAT

Pursuant to the "National Treatment" principle set forth in Article III of the WTO General Agreement on Tariffs and Trade ("GATT"), Japan must ensure that its excise tax regime does not discriminate against like imported products. However, Japan's two-tier tax system that benefits domestic Third Grade products violates Japan's obligations in respect of this National Treatment principle.

- a. ***Japan's favorable excise treatment for Third Grade brands imposes a higher tax burden on imported like products and thus violates GATT Article III:2, first sentence***

GATT Article III:2, first sentence, provides that imported products of WTO Members "shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products." Excise taxes qualify as such "internal taxes" within the meaning of Article III:2.⁸ Pursuant to this provision, Japan is therefore required to ensure that imported products are not subject to taxes that are in excess of the taxes imposed on like domestic products. Any difference in taxation, no matter how small, between "like" domestic and imported cigarettes that imposes a higher tax burden on like imported cigarettes violates the National Treatment provision of GATT Article III:2, first sentence.⁹

The WTO Appellate Body has determined that the question of whether a measure is consistent with the first sentence of Article III:2 requires the following two-step questioning: (a) are imported and domestic products "like products" and (b) are imported products subject to an internal tax "in excess of" that applied to the domestic like products? If the answer to both of these questions is affirmative, there is a violation of the first sentence of Article III:2.¹⁰

⁸ Appellate Body Report, *Canada – Certain Measures Concerning Periodicals*, WT/DS31/AB/R, adopted 30 July 1997, p. 18.

⁹ Appellate Body Report, *Japan – Alcoholic Beverages II*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, p. 23.

¹⁰ See, in particular, Appellate Body Report, *Canada –Periodicals*, p. 22-23.

The "like product" test under the first sentence of Article III:2 requires an examination of the following relevant factors: (i) the product's end-uses in a given market; (ii) consumers' tastes and habits; (iii) the product's properties, nature and quality; and (iv) tariff classification.¹¹ Other relevant factors may also be considered on a case-by-case basis.¹² In *Thailand – Cigarettes*, the parties tended to agree that imported and domestic cigarettes are like, at least in terms of physical characteristics, end-uses and classification under the Harmonized System.¹³ Domestic Third Grade cigarettes and imported cigarettes share the same physical characteristics, are made from similar materials and have a similar presentation. They are both composed of a paper tube; a mix of tobacco and additives that fills the tube; a filter; and they are presented and packed in a virtually identical manner in all relevant aspects. Any difference in the blend of tobacco leaf used in Third Grade cigarettes and imported cigarettes cannot be such as to establish a significant distinction between these products. Third Grade and imported cigarettes also have the same use, i.e., smoking. Imported brands and domestic Third Grade brands are thus "like" products.

The Appellate Body has indicated that the notion of like products, under the first sentence of Article III:2 must be construed narrowly.¹⁴ This has led panels to consider that cigarettes within a price segment are like within the meaning of the first sentence of Article III:2.¹⁵ If considering the situation from the perspective of consumer preferences, as reflected in the current market situation and the different price tiers in the market, it is clear that domestic Third Grade and imported brands are "like" products. It is important to note that the existing difference in retail prices between imported brands which are sold for about 410 Yen per pack and former Third Grade brands which are sold for 240 – 250 Yen per pack, is mainly due to the difference in the excise duty rates to which they are subject. If Third Grade brands were subject to the standard excise duty rate, their retail prices would be in line with those of imported brands. Imported and currently favorably treated domestic products would thus operate in the same market segment, absent the preferable tax treatment. This is confirmed by recent market studies which show that Japanese consumers consider imported brands as directly substitutable with Third Grade brands since they switched from the latter brands. For all of these reasons, it is clear that Third Grade brands are "like" imported brands.

¹¹ Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 21.

¹² In *Thailand – Cigarettes (Philippines)*, for example, the Panel considered in particular consumer habits and preferences. Panel Report, *Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines*, WT/DS371/AB/R, adopted 15 July 2011, p. 237 -241.

¹³ Id., para. 7.439.

¹⁴ Appellate Body Report, *Japan – Alcoholic Beverages*, para. 118. The Appellate Body then went on to state that "While perfectly substitutable products fall within Article III:2 first sentence, imperfectly substitutable products can be assessed under Article III:2, second sentence".

¹⁵ In a number of cigarettes-related WTO disputes, the likeness analysis was conducted based on the tax burdens in different price segments. In *Thailand – Cigarettes (Philippines)* and *Dominican Republic – Import and Sale of Cigarettes*, which both involved claims of tax discriminations, panels established likeness within distinct market segments. Panel Report, *Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines*, WT/DS371/AB/R, adopted 15 July 2011, p. 240 and Panel Report, *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes*, WT/DS302/R, adopted 19 May 2005, p. 187.

No imported cigarette brand, no matter how low the retail price is, would ever be able to benefit from the favorable tax treatment given that none is on the list of Third Grade brands established at the end of the monopoly in 1985. So, an imported brand that uses the same ingredients, is of the same size and shape, of the same tar level etc., is still paying the higher specific excise tax, while its domestic competitor brand listed as a former Third Grade brand pays the lower excise tax. As indicated above, domestic former Third Grade cigarettes are subject to a specific excise tax of less than half of that imposed on imported cigarettes. Thus, imported cigarettes are subject to an excise tax that is "in excess of" that imposed on "like" domestic Third Grade brand cigarettes, in violation of the National Treatment provision of GATT Article III:2, first sentence.¹⁶

b. *Japan's favorable excise treatment for Third Grade brands imposes dissimilar taxation burdens on imported and directly competitive or substitutable domestic products of such a magnitude and in such a manner as to afford protection and thus violates GATT Article III:2, second sentence*

The second sentence of GATT Article III:2 imposes a similar National Treatment obligation in respect of internal tax measures affecting imported and "directly competitive or substitutable" domestic products. To the extent that it could be argued that low priced Third Grade cigarettes are sold in a different price segment or are of inferior quality and are for that reason not "like" higher priced imported brands, it is clear that all cigarettes sold in Japan are at least directly competitive or substitutable products based on their similarity in channels of distribution and cross-price elasticity as well as their, generally speaking, common physical characteristics, end uses, consumer tastes and tariff classification. The fact that Third Grade brands have been stealing market share from imported brands only confirms this competitive relationship.

The second sentence of GATT Article III:2 requires that such directly competitive or substitutable products must be "similarly taxed", in law or in fact, and that any difference in taxation must not be "so as to afford protection" to domestic products.¹⁷ If there is dissimilar taxation of even some imported products as compared to directly competitive or substitutable domestic products, the first requirement for finding a violation of GATT Article III:2, second sentence will be met.¹⁸ Clearly, imported brands are subject to "dissimilar" taxation when compared with domestic former Third Grade brands given that domestic Third Grade brands are subject to a significantly lower specific excise tax rate.

The only question remaining is whether the dissimilar taxation is "so as to afford protection" to domestic products.

¹⁶ Even when the excise tax is viewed in relation to the price of the products in question, the conclusion is the same. As noted before, the effective tax burden on mainstream products is around 60% while the tax burden on Third Grade products is only 47%. In fact, if imported products seek to compete with Third Grade cigarettes at the same low price level, the disadvantage for imported products will only become more significant given the specific nature of the excise tax system in Japan.

¹⁷ Article III:2 second sentence of the GATT needs to be read in the light of the Ad Note to Article III:2. Appellate Body Report, *Philippines – Taxes on Distilled Spirits*, WT/DS396/AB/R, WT/DS403/AB/R, adopted 20 January 2012, para. 259.

¹⁸ Appellate Body Report, *Canada –Periodicals*, p. 29 (referring to *Japan – Alcoholic Beverages*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, p. 27).

The “design, architecture, and structure” of the excise tax regime which was established at the end of the monopoly period, and expressly listed a number of JT brands which were deliberately given preferential tax treatment so that these brands would not be affected by the tax harmonization that was introduced at the time, reveals that the measure is imposed so as to afford protection to domestic Third Grade brands. As indicated above, one of the stated purpose of the Tobacco Business Law is “to foster the sound development of the Japanese tobacco industry”.¹⁹ In addition, the magnitude of the tax differential²⁰ applicable to imported and domestic Third Grade cigarettes which pay less than half of the excise tax, confirms the “protective nature” of the regime.²¹ As noted before, no imported brands can ever qualify as a Third Grade brand and imported cigarettes are thus consistently subject to an excise tax that is significantly higher and in fact more than the double of that imposed on this group of exclusively domestic products, thereby providing protection to the directly competitive Third Grade brands.²²

In sum, Japan imposes dissimilar tax burdens on imported and directly competitive or substitutable domestic Third Grade brands providing protection and modifying the conditions of competition in favor of these domestic brands. Therefore, Japan is in any case acting in violation of its obligations under GATT Article III:2, second sentence. The fact that many domestic, non-Third Grade brands are also paying the higher tax rate does not undo the discrimination. All of the favorably treated Third Grade products are domestic, and can only be domestic given the closed nature of the 1985 list, while all of the imported brands are subject to the higher taxes, thus confirming the discrimination.²³

Therefore, Japan’s excise tax system that favors domestic former Third Grade brands violates the WTO obligations of Japan as set forth in GATT Article III:2 on National Treatment.

2. Japan’s Tobacco Leaf Purchase Obligation violates the national treatment obligation of GATT Article III:4

The section of Japan’s Tobacco Business Law concerning the “Production and Purchase of Domestically Produced Leaf Tobacco for Raw Materials” imposes a number of obligations on JT, the sole producer of tobacco products in Japan. JT is required to conclude advance contracts relating to the purchase of domestically-grown tobacco leaf with all Japanese tobacco growers for the supply of tobacco for the manufacture of tobacco products.²⁴

¹⁹ Tobacco Business Law, Article 1.

²⁰ As noted before, the specific tax level for domestic Third Grade cigarettes is less than half that of imported cigarettes.

²¹ Appellate Body Reports, *Philippines – Distilled Spirits*, , paras. 255 - 257.

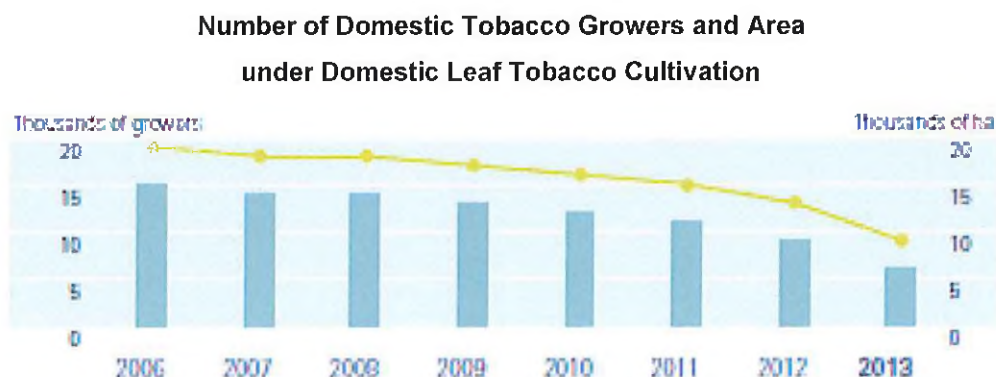
²² Similarly, in *Philippines – Distilled Spirits* the higher excise tax applied to all imported distilled spirits. Appellate Body Reports, *Philippines – Distilled Spirits*, , para. 258.

²³ See, Appellate Body Report, *Chile – Taxes on Alcoholic Beverages*, WT/DS87/AB/R, WT/DS110/AB/R, adopted 12 January 2000, DSR 2000:I, p. 281, paras. 67 - 68.

²⁴ *Id.*, Article 3.1.

It must purchase the entirety of tobacco leaf produced pursuant to the contracts concluded with tobacco growers, with the only exception being for leaf not suited for the manufacture of tobacco products.²⁵ In an information note for domestic tobacco growers, the Japan Tobacco Growers Association confirms that “to cultivate tobacco leaf, it is necessary to enter into a ‘sale and purchase contract’ with JT”. The Tobacco Business Law does not require JT to enter into agreements similar to those concluded with domestic tobacco growers for the purchase of imported tobacco leaf.

The contracts between JT and domestic tobacco growers are concluded after consultation of the Tobacco Leaf Advisory Council, a body that exists within JT and that is composed of growers’ representatives and individuals with academic experience approved by the Ministry of Finance. Contracts set forth the cultivated area, per type of tobacco leaf, as well as the price, per type and quality.²⁶ In recent years, the volume of imports of tobacco leaf has increased as a consequence of the decrease in the number of domestic tobacco growers and the reduction of the tobacco growing area in Japan.²⁷ However, domestic production of tobacco leaf remains significant in absolute and relative terms.



In 2012, 19,673 tons of tobacco leaf were produced in Japan²⁸ and 54,059 tons were imported.²⁹ JT used all domestically-grown tobacco for the manufacture of tobacco products.³⁰ The selling price of tobacco grown in Japan is more than three times higher than the average selling price of imported tobacco despite being of no higher and possibly somewhat lower quality than competing imported tobacco leaf, providing a substantial advantage in treatment to domestic tobacco growers as compared to importers of imported tobacco leaf.³¹

²⁵ *Id.*, Article 3.4. The Trade Policy Review (“TPR”) Report issued by the WTO Secretariat within the framework of the most recent TPR of Japan also refers to the obligations imposed on JT to purchase all tobacco leaf grown in Japan, WT/TPR/S/276, p. 32.

²⁶ Tobacco Business Law, Article 3.2.

²⁷ 2013 Annual Report (www.jt.com/investors/results/annual_report/pdf/annual2013_E_all.pdf), JT, p. 163.

²⁸ Japan Tobacco Growers Association.

²⁹ Trade Statistics of Japan, Ministry of Finance.

³⁰ 2013 Annual Report, JT, p. 135.

³¹ The average value of Japan’s tobacco leaf was 1,957 Yen/Kg and the average value of imported tobacco was 574 Yen/Kg.

Tobacco leaf price comparison, Japan vs. Imported Leaf in 2012

	Value (thousand Yen)	Quantity (KG)	Value/KG (Thousand Yen)
Japan	38,497,000	19,673,000	1.957
Imported	31,030,498	54,059,446	0.574

GATT Article III:4, first sentence, provides that products imported from WTO Members "shall be accorded treatment no less favorable than that accorded to like products of domestic origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use." The WTO Appellate Body has confirmed that the three following elements must be satisfied for a violation of Article III:4 to be established: (a) the domestic and imported products at issue must be "like products"; (b) the measure concerned is a "law, regulation or requirement affecting their internal sale, offering for sale, purchase, transportation, distribution or use"; and (c) the imported products are accorded "less favorable" treatment than that accorded to like domestic products.³²

As detailed above, the analysis of the first criterion, *i.e.*, the product "likeness", requires an examination of the following relevant factors: (a) the properties, nature and quality of the products; (b) the end-uses of the products; (c) consumers' tastes and habits; and (d) the tariff classification of the products.³³ Japan produces both Burley and Virginia tobacco leaf³⁴ and also imports these two types of leaf. Domestically-grown and imported leaf share the same physical characteristics; are both used as raw materials for the manufacture of tobacco products by JT; and have the same tariff classification.

A determination of likeness under Article III:4 of the GATT 1994 is "fundamentally, a determination about the nature and extent of a competitive relationship between and among products."³⁵ Panels have therefore established that, where "[o]rigin [is] the sole criterion distinguishing the products, it is correct to treat such products as like products within the meaning of Article III:4."³⁶ The Tobacco Business Law solely imposes an LPO for "domestically produced tobacco leaf". Tobacco leaf grown outside of Japan is not entitled to benefit from the annual purchase obligation imposed on JT for the manufacture of tobacco products. Because domestically-grown and imported tobacco leaf satisfy the relevant factors and the LPO only applies to tobacco grown in Japan, domestic and imported leaf are "like" products under Article III:4.

³² See, in particular, Appellate Body Report, *Korea — Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, adopted 10 January 2001, para. 113.

³³ See, in particular, Appellate Body Report, *Japan — Alcoholic Beverages*, para. 114.

³⁴ 2012 Supply & Demand Report, Universal Leaf Tobacco Company, Inc.

³⁵ See, Appellate Body Report, *European Communities — Measures Affecting Asbestos and Products Containing Asbestos*, WT/DS135/AB/R, adopted 5 April 2001, para. 99.

³⁶ See, Panel Report, *India — Measures Affecting the Automotive Sector*, WT/DS146/R, adopted 5 April 2002, paras. 7.174-7.176.

There is no doubt that the LPO scheme satisfies the second criterion of Article III:4 because the Tobacco Business Law directly affects the internal sale, offering for sale, purchase and use of tobacco leaf in Japan. The disputed section, which is titled "Production and Purchase of Domestically Produced Tobacco Leaf for Raw Material", imposes an obligation on JT to "purchase" domestically-grown tobacco leaf from growers "selling" it for "use" in manufactured tobacco products.³⁷

With respect to the last criterion, panels have established that the standard of effective equality of competitive conditions for imported and domestic like products on the internal market set by the Appellate Body³⁸ is the standard of national treatment that is required, not only with regard to Article III generally, but also, more particularly with regard to the "no less favorable" treatment of Article III:4.³⁹ The provisions of Japan's Tobacco Business Law obliging JT to purchase all tobacco leaf grown in Japan modify the conditions of competition between domestically grown and imported leaf to the detriment of the latter. Because the LPO only benefits tobacco leaf grown in Japan, imported leaf is not subject to the same opportunities as domestic leaf. The protection granted by the LPO through the requirement to purchase domestically grown tobacco leaf allows domestic growers to dispose of all their production and contributes to the very significant price difference between tobacco leaf grown in Japan and imported leaf, which cannot be justified on commercial grounds and which amounts to a significant distortion in the conditions of competition by shielding locally grown tobacco from any import competition and by giving the domestic growers substantially advantageous prices.

Considering the above, the LPO imposed by the Tobacco Business Law violates the WTO obligations of Japan as set forth in GATT Article III:4 on National Treatment.

The provisions of Articles III:8(a) and (b) cannot be invoked by Japan to justify the LPO. The exception of Article III:8(a) only applies to "laws regulations or requirements governing the procurement by governmental agencies of products purchased for governmental purposes and not with a view to commercial resale or with a view to use in the production of goods for commercial resale". Even though the Japanese government still owns 33.3 percent of JT's shares,⁴⁰ none of the tobacco leaf purchased domestically is used for governmental purposes. Domestically-grown tobacco leaf is used for the manufacture of tobacco products that are commercially sold within and outside of Japan. The provisions of Article III:8(b) are aimed at permitting the payment of subsidies exclusively to domestic producers but cannot be invoked to justify the violation of Article III:4.

³⁷ Tobacco Business Law, Article 3.

³⁸ See, Appellate Body Report, *Japan—Alcoholic Beverages*, p. 16.

³⁹ See Panel Report, *Japan - Measures Affecting Consumer Photographic Film and Paper*, WT/DS44/R, adopted 22 April 1998, para. 10.379.

⁴⁰ 2013 Annual Report of JT, p. 170.

In addition to violating Article III:4, the LPO scheme could be considered as a subsidy under the WTO Agreement on Subsidies and Countervailing Measures ("SCM Agreement") if JT is required to purchase domestically grown tobacco leaf for more than "adequate remuneration". The Tobacco Business Law requires the Tobacco Leaf Advisory Council to determine the price of tobacco leaf "with reference to production costs, commodity prices and with other economic circumstances, and with the intent of securing the production of tobacco leaf"⁴¹ but it is unclear how prices are actually set. If the price paid to Japanese growers under the LPO scheme was found to constitute a subsidy within the meaning of the SCM Agreement, the resulting adverse effects to the interests of WTO Members would also have to be established for the subsidy to be actionable, *i.e.*, challengeable, before the WTO.

3. Japan has failed to publish sufficient information regarding the retail list price approval system in violation of GATT Article X

Article 33.1 of the Tobacco Business Law requires JT and distributors of imported tobacco products to have the retail list price of any new tobacco products approved by the Minister of Finance prior to shipment from the place of manufacture or importation. After the initial retail price approval, pursuant to Article 33.2 of the Tobacco Business Law, JT and distributors of imported tobacco products must also obtain the prior approval of the Minister of Finance to change the approved retail list price. Article 36 of the Tobacco Business Law provides that distributors of imported tobacco products can only sell products at the approved retail list prices and that products for which no prices have been approved may not be sold in Japan.

The Tobacco Business Law and its Enforcement Order⁴² and Enforcement Regulations⁴³ provide very limited guidance on the retail list price approval conditions. Article 34.1 of the Tobacco Business Law only stipulates that the Minister of Finance must approve a retail list price request or a request for a change in an approved retail list price except in the following two conditions:

1. When it is deemed that sales at the retail list price pertaining to the pertinent application would unduly damage the welfare of consumers
2. When it is deemed that the retail price list pertaining to the pertinent application is unduly low in light of, for the Company [JT], the maximum sales price prescribed by Article 9, paragraph 1 (including cases which apply *mutatis mutandis* pursuant to Article 9, paragraph 6) and, for the Designated Dealers [distributors of imported products], the import price (refers to the price calculated according to the provisions from Article 4 to Article 4, part 8 of the Customs Tariff Law (Law No. 54 of the year 1910).

⁴¹ Tobacco Business Law, Article 4.2.

⁴² Tobacco Business Law Enforcement Order, Cabinet Order No. 21 of 5 March 1985.

⁴³ Tobacco Business Law Enforcement Regulations, Ministry of Finance Ordinance No. 5 of 5 March 1985.

No information is publicly available on the factors that the Minister of Finance takes into account when establishing whether a requested retail list price "would unduly damage the welfare of consumers" or "is unduly low" under paragraphs 1 and 2 respectively of Article 34.1. Distributors of imported products are therefore unable to determine retail list prices that are likely to be approved.

Article X:1(1) of the GATT requires Japan to promptly publish all laws, regulations, judicial decisions and administrative rulings of a general application that affect, in particular, the sale and distribution of imported products so as to enable governments and traders to become acquainted with them. The publication of all measures of general application affecting trade is essential for economic operators in the conduct of business.

While it has published the Tobacco Business Law and its Enforcement Order and Enforcement Regulations, Japan has not made public all the elements taken into account by the Minister of Finance when deciding on requests for listed retail prices or changes to approved prices and in particular the factors considered when reviewing the consistency of proposed prices with Article 34.1 of the Tobacco Business Law. The elements and factors considered by the Minister of Finance when deciding on requests for the approval of retail list prices are "regulations ... of general application" within the meaning of Article X:1 as they apply to JT and all the distributors of imported tobacco products in Japan.⁴⁴ The absence of published rules regarding all the conditions that must be satisfied for a retail list price to be approved by the Ministry of Finance makes it impossible for distributors of imported tobacco products and other directly affected economic operators to predict the outcome of requests for price/price change approval. This absence of predictability and transparency negatively affects imports of tobacco products into Japan. Japan, by failing to publish all the rules regarding the conditions regarding the approval of retail list prices and changes to these prices violates its obligations under Article X:1(1) of the GATT.

The retail list price approval system also amounts to a maximum price control mechanism as authorities in Japan play an active role in setting approved prices.⁴⁵ This system may be used to limit competition within the Japanese market between domestic and imported brands of tobacco products. Article III:9 of the GATT requires Members maintaining price control measures to take into account the interests of exporting Members with a view to avoiding the prejudicial effect that such measures can have on imports.

⁴⁴ See Appellate Body Report, *United States – Restrictions on Imports of Cotton and Man-made Fibre Underwear*, WT/DS24/AB/R, adopted 25 February p. 21,

⁴⁵ See, for example, Across-the-board JCT pass-on to be derailed: Tobacco price increase to be 3% in total, with some SKU prices even to be frozen - Major tobacco makers say, The Jiji Press, 15 October 2013.

To prevent any possible price discrimination and allow greater competition and more flexibility, Japanese authorities should consider the adoption of a declaratory system instead of the current prior approval system. Such a new system would serve to address the GATT Article X:1(1) violation and would prevent any price discrimination between domestic and imported products.