



Japan's Possible Entry Into the Trans-Pacific Partnership and Its Implications

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Summary

In late 2011, after a year of extended internal deliberations, the Japanese government decided to explore the possibility of joining the Trans-Pacific Partnership (TPP) negotiations. The TPP would be a free trade agreement (FTA) among at least 11 countries—Australia, Brunei, Canada, Chile, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States, and Vietnam. The United States and its TPP partners envision the agreement as “a comprehensive, next-generation regional agreement that liberalizes trade and investment and addresses new and traditional trade issues and 21st century challenges.”

Congress has a direct and oversight role in the issue of U.S. participation in the TPP. It must approve implementing legislation, if the TPP is to apply to the United States. Some Members of Congress have already weighed in on whether Japan should be allowed to participate in the TPP and under what conditions. More may do so as the process proceeds.

Although Japanese leaders have not made a final decision yet on the TPP, they have been engaging in discussions with each of nine TPP partners separate from the main TPP negotiations. (Canada and Mexico have not officially joined the discussions.) At this writing, Japan has completed discussions with six of the countries, all of which support Japan's participation and all of which already have been or are in the process of negotiating bilateral FTAs with Japan. Discussions with the United States, Australia, and New Zealand continue. The Obama Administration has identified three issues that Japan needs to address as “confidence building measures” if the United States is to support Japan's entry into the TPP: Japanese restrictions on imports of U.S. beef; market access in Japan for cars made by the Detroit-based U.S. manufacturers; and preferential treatment for insurance and express delivery subsidiaries of state-owned Japan Post. No deadlines have been set for completion of the consultations.

The TPP is the leading U.S. trade policy initiative of the Obama Administration and a core component of Administration efforts to “rebalance” U.S. foreign policy priorities toward the Asia-Pacific region by playing a more active role in shaping the region's rules and norms. As the second largest economy in Asia, the third largest economy in the world, and a key link in global supply/production chains, Japan's participation would be pivotal to enhancing the credibility and viability of the TPP as a regional free trade arrangement.

Japan's membership in the TPP with the United States would constitute a *de facto* U.S.-Japan FTA. A large segment of the U.S. business community has expressed support for Japanese participation in the TPP, if Japan can resolve long-standing issues on access to its markets for U.S. goods and services. However, the Detroit-based U.S. auto industry has expressed strong opposition to Japan participating in the TPP negotiations.

The question of whether to join the TPP trade talks has generated enormous attention and controversy inside Japan. Opposition to joining has been particularly strong among vested interest groups, such as the agricultural community and has divided both Japan's ruling party and largest opposition party. Many analysts believe that current Japanese prime minister Yoshihiko Noda is committed to entering Japan in the negotiations after he completes some domestic priorities in the late summer and early fall. However, Noda's hold on power is tenuous, and in August the major opposition parties forced him to promise to call parliamentary elections at “an early date,” presumably by early 2013. Noda's party, the Democratic Party of Japan, is widely expected to do poorly and perhaps lose the premiership. The largest opposition party has opposed the TPP unless

certain exceptions are allowed. Given Japan's political uncertainty, even if Japan succeeds in joining the negotiations, it is not clear if any government in Tokyo will be strong enough to overcome this opposition when it comes time to approving a final agreement.

The outlook for Japan's entry into the TPP negotiations remains unclear at this time and depends on a number of factors. Perhaps the most critical factor is whether Japanese political leaders can reach a political consensus on whether to proceed with the negotiations and then whether Japan can reach agreement with the TPP partners on conditions of its entry. The addition of Canada and Mexico, which will formally join the negotiations in the fall of 2012, could complicate the negotiations as well, as those two countries may have their own demands for Japan.

The TPP issue presents both risks and opportunities for the United States and Japan. On the one hand, if successful, it could reinvigorate an economic relationship that has remained steady but stagnant, by forcing the two countries to address long-standing, difficult issues, and allowing them to raise their relationship to a higher level. On the other hand, failure to do so could indicate that the underlying problems are too fundamental to overcome and could set back the relationship. It could signify the failure of the United States and/or Japan to deal with domestic opposition to a more open trade relationship.

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Introduction

The United States is engaged in negotiations with eight other countries to form a regional free trade agreement (FTA)—the Trans-Pacific Partnership Agreement (TPP).¹ In the negotiations, the United States and the other TPP partner-countries seek to build “a comprehensive, next-generation regional agreement that liberalizes trade and investment and addresses new and traditional trade issues and 21st century challenges.”² The TPP partners also envision the agreement to be a building block towards the establishment of a broader, Asian-Pacific regional FTA, sometimes referred to as the Free Trade Area of the Asia-Pacific (FTAAP).

Congress has a direct and oversight role in U.S. participation in the TPP. It must approve implementing legislation, if a final TPP agreement is to apply to the United States. Some Members of Congress have already weighed in on whether Japan should be allowed to participate in the TPP and under what conditions. More may do so as the process proceeds.

The Obama Administration has been proceeding in negotiating the TPP as if trade promotion authority were in force; it has been adhering to consultation requirements and notification deadlines that have been an integral part of previous TPA or fast-track statutes. To maintain this practice, the Obama Administration would have to notify both Houses of Congress 90 calendar days before it begins official negotiations (as opposed to preliminary discussions) with Japan on the TPP. It did so regarding Mexico and Canada, on July 9 and July 10, 2012, respectively.

In late 2011, after extended and delayed internal deliberations, the Japanese government decided to explore the possibility of joining the TPP negotiations. Prime Minister Yoshihiko Noda announced at a press conference on November 11, 2011, that “[Japan would] enter into consultations toward participating in the TPP negotiations with the countries concerned on the occasion of the [November 12-13, 2011] APEC Economic Leaders meeting in Honolulu, Hawaii.” Since then, Japan has engaged in discussions with each of the nine TPP partners. At this writing, Japan has completed discussions with six of the countries, all of which support Japan’s participation. Discussions with the United States, Australia, and New Zealand continue.³ As discussed below, the question of whether to join the TPP trade talks has generated enormous attention and controversy inside Japan. Opposition to joining has been particularly strong among vested interest groups, such as the agricultural lobby, and has divided both Japan’s ruling party and largest opposition party.

The TPP is the leading U.S. trade policy initiative of the Obama Administration and a pillar of its efforts to “rebalance” U.S. foreign policy priorities toward the Asia-Pacific region by playing a more active role in shaping the region’s rules and norms. As the second largest economy in Asia, the third largest economy in the world, and a key link in the global supply chain, Japan’s participation would be pivotal to the credibility and viability of the TPP as a regional trade

¹ The eight countries are: Australia, Brunei, Chile, Malaysia, New Zealand, Peru, Singapore, the United States, and Vietnam. The governments of Mexico and Canada also expressed interest and, after a series of consultations, were formally invited to join by the nine TPP partners on June 18 and June 19, 2012, respectively. They will join the negotiations officially in the fall of 2012.

² Trans-Pacific Partnership Leaders Statement, November 11, 2011.

³ *Inside U.S. Trade*, March 22, 2012.

arrangement. The inclusion of Japan would expand the amount of U.S. trade and foreign investment that the TPP would cover if implemented.

For Japan, participation in the TPP could potentially transform its economy by providing unprecedented access to the Japanese market for foreign exporters and investors. It could also force Tokyo to confront structural economic problems that have long impeded economic growth. It would also symbolize Japan's continued position as an economic power in East Asia, an image that has been tarnished by decades of economic stagnation and the growth of China.

Japan's participation in the TPP would have important implications for the U.S.-Japan relationship. For example, it already has renewed a focus on long-standing issues, such as access to Japan's markets for autos, agricultural products, and insurance, which have remained irritants in the relationship. These issues will likely have to be addressed in one form or another, perhaps even before Japan is approved as a full-fledged TPP participant. New issues will undoubtedly also be raised in the process. Additionally, a decision by Japan not to enter or by the United States not to approve Japan's entry could lead some to question the depth of the U.S.-Japan relationship and also the credibility of the TPP itself.

An Overview of the TPP

The TPP is an evolving regional free trade agreement (FTA). It was originally formed as the Trans-Pacific Strategic Economic Partnership—an FTA now in effect among Singapore, New Zealand, Chile, and Brunei (the so-called “P-4”). In the fall of 2008, the United States, along with Australia, Peru, and Vietnam, joined the negotiations to accede to the arrangement. Malaysia joined as the ninth negotiating partner in October 2010.

On November 14, 2009, President Obama committed the United States to engage with the TPP countries to transform the original P-4 pact into a regional arrangement with broad-based membership and “the high standards worthy of a 21st century trade agreement.”⁴ After several months of discussions, the nine partners announced a framework for the agreement in time for the ministerial meeting of the Asia-Pacific Economic Cooperation (APEC) forum in Honolulu, Hawaii, which was held November 8-13, 2011. The TPP partners have conducted 13 rounds of negotiations with the latest held in July 2012 in San Diego, California.

As reflected in the framework, the TPP partners envision a comprehensive arrangement covering a broad range of trade and trade-related activities, similar in structure to a number of recently-concluded U.S. FTAs. These activities include market access for goods and services; government procurement; foreign investment; technical barriers to trade; trade remedies; sanitary and phytosanitary measures;⁵ intellectual property rights; worker rights; and environmental protection. The TPP countries also agreed to pursue cross-cutting issues such as regulatory coherence, competitiveness and business facilitation, also known as transnational supply and production chains; the participation of small and medium-sized companies; economic development; and potential disciplines on the state-owned enterprises (SOEs).

⁴ Remarks of President Obama at Suntory Hall, Tokyo, Japan, November 14, 2009.

⁵ Sanitary and Phytosanitary measures are procedures used by government agencies to ensure the animal and plant products are safe for consumption.

The TPP participants also envision the TPP to go beyond typical FTAs by being:

- a regional agreement that facilitates trade by minimizing the “noodle bowl” effect that has been created by different sets of rules under the more than 100 bilateral and regional FTAs that exist in the Asia Pacific-region;
- an agreement that addresses trade challenges that are emerging in the 21st century, for example, cloud computing and SOEs, that have not been addressed in previous FTAs nor not fully in the World Trade Organization (WTO) because they did not exist or were considered not as important; and
- a “living agreement” that will not restrict its membership to the 11 countries but will be open to other countries acceding to it as long as they are willing to commit to its provisions and will take on new issues as they arise.

The leaders of the nine TPP countries instructed their negotiators to develop a completed legal text as soon as possible. The complexity of the issues at hand, the diversity of the membership, and the possibility of new members, such as, Japan, and newly invited Canada and Mexico, suggest challenges ahead for the negotiators.

U.S.-Japan Economic Ties

A brief overview of U.S.-Japan economic ties can provide context for understanding U.S. and Japanese interests in the TPP and the potential implications from various perspectives. It could also shed light on opportunities and challenges presented by an FTA that includes the United States and Japan. A U.S.-Japan FTA is not a new idea, but it is a policy option that has failed to take hold in the past because of some fundamental issues which have been seemingly intractable.

U.S.-Japan Trade Trends

The United States and Japan are the world’s first and third largest economic powers. Together they account for over 30% of gross world product.⁶ The two countries remain very important economic partners, accounting for large shares of each other’s foreign trade and investment, even though their relative economic significance to one another has declined over the last few years. In 1999, Japan slipped from being the second largest U.S. trading partner to the third largest. In 2004, it slipped to number 4, where it has remained. Until 2007, the United States was Japan’s largest trading partner, but it slipped to number 2 since 2007.⁷

The global financial crisis and economic downturn added another dimension to the relationship as the two countries have grappled with the severe impact of the crisis on their respective economies, while working with their partners in the G-20 to coordinate a multilateral response.⁸ The impact of the March 11, 2011 earthquake and subsequent tsunami and nuclear accidents in northeast Japan also affected trade, although not as much as originally anticipated.

⁶ CRS calculation based on data in CIA, *World Factbook*, <http://www.CIA.gov>.

⁷ Global Trade Atlas.

⁸ The G-20 countries are: Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, the United Kingdom, the United States, and the European Union.

U.S.-Japanese bilateral trade in goods and services declined significantly in 2009 over 2008 levels because of the global economic downturn but picked up in 2010 and 2011. (See **Table 1** and **Table 2**.)

Table 1. U.S.-Japan Merchandise Trade, 2004-2011

(\$ billions)

Year	U.S. Exports	U.S. Imports	Total Trade	U.S. Trade Balances
2004	54.4	129.6	184.0	-75.2
2005	55.4	138.1	193.5	-82.7
2006	59.6	148.2	207.8	-88.6
2007	62.7	145.5	208.2	-82.8
2008	66.6	139.2	205.8	-72.3
2009	51.2	95.9	147.1	-44.8
2010	60.5	120.3	180.8	-59.8
2011	66.2	128.8	195.0	-62.2

Source: U.S. Department of Commerce, U.S. Census Bureau.

Table 2. U.S.-Japan Trade in Services, 2004-2011

(\$ billions)

Year	U.S. Exports	U.S. Imports	Total Trade	U.S. Trade Balances
2004	36.0	21.3	57.3	14.8
2005	42.5	23.8	66.3	18.7
2006	42.0	25.5	67.5	16.5
2007	41.2	26.2	67.4	15.0
2008	42.3	25.7	68.0	16.6
2009	41.4	22.9	64.3	18.5
2010	45.1	25.9	71.0	19.2
2011*	47.6	27.3	74.9	20.3

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

Notes: * Preliminary

Raw trade data likely underestimate Japan's importance because they do not readily measure Japan's role in the East Asian supply and production networks that produce goods exported to the United States. The two countries are also economically tied through investment flows. For example, Japanese investors are the second largest group (next to China) of foreign holders of U.S. treasury securities and, therefore, U.S. government debt and of direct investments in the U.S. economy.

In the 1980s and 1990s, the bilateral economic relationship was the centerpiece of U.S. and Japanese foreign economic agendas. Persistent and increasing U.S. merchandise trade deficits

with Japan, sharp increases in Japanese exports to the United States of high-value manufactured products, such as cars, and large volumes of Japanese investments in the United States (including purchases of high-profile properties, such as the Empire State Building) stoked fears in the United States of Japan as an economic threat to the United States. Many scholarly and popular books and journal articles were written on the subject.⁹

However, since the mid-1990s, the trade relationship with Japan has been a lower priority for U.S. officials. One reason for the shift may be the rise of China as a global trade and economic power, and source of challenges and opportunities to U.S. trade policymakers. Symbolic of this rise are the relative merchandise trade balances with Japan and China. While U.S. merchandise trade deficits with Japan have remained relatively constant in recent years, the U.S. deficits with China have risen significantly. In 2011, the U.S. trade deficit with Japan was \$62.2 billion, while the trade deficit with China was \$295.4 billion.¹⁰

Another reason may have been that Japan's economic problems over the last two decades have made it seem less of a competitive "threat."¹¹ In addition, the level of Japanese foreign direct investments in the United States has declined. Furthermore, security issues, such as North Korea's nuclear program (the United States and Japan are parties to talks on North Korea's fledgling nuclear program) and the relocation of U.S. troops in Japan, have overshadowed bilateral trade relations as a priority.¹² Nevertheless, trade-related tensions remained, albeit below the surface.

Managing the Trade Relationship

Over the years, U.S.-Japan economic relations have experienced degrees of friction, sometimes to the point of threatening the stability of the alliance. The United States dominated the economic relationship with Japan for many years after World War II. The United States was by far the largest economy in the world, and Japan was dependent on the United States for national security. The United States set the agenda, and the issues on the agenda were driven by the U.S. demands for Japan to curb exports to the United States and/or to remove barriers to U.S. exports and investments.

In the 1960s and 1970s, the primary issues were Japan's perceived protectionist economic policies that it implemented through high tariffs and other border restrictions. As Japan's economy became more developed and competitive and as it negotiated reductions in its tariffs with other members of the General Agreement on Tariffs and Trade (GATT)—now the World Trade Organization (WTO)—the United States focused on non-tariff barriers, including "behind the border" measures, such as government regulations that, while not ostensibly protectionist, may be applied in a way that restricts trade. Certain measures are not covered by WTO agreements and are currently not readily addressed in trade negotiations since they serve non-trade functions. Examples of such measures include:

⁹ For example, Clyde V. Prestowitz, *Trading Places: How We Allowed Japan to Take the Lead*, New York: Basic Books, 1988.

¹⁰ For more information on the rise of China in U.S. economic relations, see CRS Report RL33536, *China-U.S. Trade Issues*, by Wayne M. Morrison.

¹¹ For more information on Japan's economic problems, see archived CRS Report RL30176, *Japan's "Economic Miracle": What Happened?*, by William H. Cooper.

¹² For more information on the overall U.S.-Japan relationship, see CRS Report RL33436, *Japan-U.S. Relations: Issues for Congress*, coordinated by Emma Chanlett-Avery.

- domestic taxes on car purchases and other regulations said to discriminate against sales of imported vehicles;
- a government contract bidding system that favors certain domestic providers of construction services;
- zoning regulations that discourage the establishment of large retail stores that are more likely to sell imported products than the smaller stores the regulations are designed to protect;
- government health insurance reimbursement regulations that discourage the purchase of newer, leading-edge pharmaceuticals and medical devices, many of which are imported; and
- government subsidies for the production of semiconductors.

To address these non-tariff barriers Japan and the United States employed, largely at the latter's instigation, special bilateral frameworks and agreements to conduct their government-to-government economic relations. These arrangements included:

- the Market-Oriented Sector-Specific (MOSS) talks started in 1985;
- the Structural Impediments Initiative (SII), begun in March 1989;
- the United States-Japan Framework for a New Economic Partnership, begun in 1993;
- the Enhanced Initiative on Deregulation and Competition Policy (the Enhanced Initiative), begun in 1997;
- the U.S.-Japan Economic Partnership for Growth (The Economic Partnership) begun in 2001; and
- the United States-Japan Economic Harmonization Initiative, launched in 2010, which now operates as the primary bilateral forum for bilateral discussions.

The two countries also concluded bilateral agreements or memoranda of understanding (MOUs), whereby Japan agreed to address U.S. concerns about its trading practices for specific products, including autos and semiconductors.

These arrangements varied in their approaches. However, they shared some basic characteristics: they were bilateral; were designed to remedy U.S.-Japan trade problems by focusing on regulations and other fundamental barriers; and were typically initiated by the United States. However, these arrangements were only of limited success, judging by the fact that many of the issues they were supposed to address remain.

Pending Challenges and the TPP

Many of that issues that have continually irritated the U.S.-Japan economic relationship could be addressed within the TPP. U.S. policymakers and other stakeholders have identified three issues that, if resolved, would be considered "confidence-building measures" that could boost U.S. support of Japan's inclusion in the TPP. The issues relate to: Japanese restrictions on imports of

U.S. beef; market access in Japan for cars made by Detroit-based U.S. manufacturers; and preferential treatment for insurance and express delivery subsidiaries of state-owned Japan Post.¹³

Market Access for U.S. Beef

In December 2003, Japan, along with a number of other countries, imposed a ban on imported U.S. beef in response to the discovery of the first U.S. case of bovine spongiform encephalopathy (BSE or “mad cow disease”) in Washington State. In 2006, after numerous negotiations, Japan loosened the restrictions to allow beef from cattle 20 months or younger. (Some other countries, such as South Korea and Taiwan, have allowed imports of U.S. beef from cattle 30 months or younger.) U.S. beef producers and some Members of Congress have argued that international monitoring agencies have declared U.S. beef to be safe no matter the age of the cattle, and that Japan should lift the restrictions entirely. Negotiations between U.S. and Japanese officials failed to resolve the issue.

During a November 12, 2011 meeting with President Obama prior to the meeting of leaders of the APEC forum in Honolulu, Hawaii, Prime Minister Noda indicated efforts underway to review Japan’s beef import restrictions and expand market access for U.S. beef. According to the White House, “The President welcomed these initial measures, and noted the importance of resolving this longstanding issue based on science. We are encouraged by the quick steps being taken by Prime Minister Noda and look forward to working closely with him on these initiatives.”¹⁴ During a November 17-18, 2011 meeting with Japanese officials in Tokyo, Deputy U.S. Trade Representative (USTR) Demetrios Marantis raised the issue of lifting the restrictions on U.S. beef.¹⁵ In December 2011, Japan announced that it was reassessing its BSE-related restrictions with the objective to raise the maximum age of cattle from 20 to 30 months for U.S. beef exported to Japan.

U.S. Department of Agriculture (USDA) inspectors discovered on April 24, 2012, a case of BSE in a cow that was sampled for the disease at a rendering facility in central California. USDA said that the cow “at no time presented a risk to the food supply, or to human health,” because it was not intended for slaughter for human consumption.¹⁶ Japanese officials have said that the recent BSE discovery has not changed its policy on shipments of U.S. beef.¹⁷

Market Access for U.S.-Made Autos

Auto and auto-parts-related trade and investment have been a very sensitive set of issues in the U.S.-Japan economic relationship. The issue has its roots in the late 1970s and early 1980s, when U.S. imports of Japanese-made vehicles surged as a result of the increase in U.S. consumer

¹³ Office of the USTR, *U.S., Japan Hold High-Level Discussions on the Trans-Pacific Partnership*, <http://www.ustr.gov/about-us/press-office/press-releases/2012/february/us-japan-hold-high-level-consultation-trans-pacif>.

¹⁴ The White House, Office of the Press Secretary, Readout by the Press Secretary of the President’s Meeting with Prime Minister Noda of Japan, November 12, 2011.

¹⁵ *World Trade Online*, November 25, 2011.

¹⁶ USDA Press Release, “Update from APHIS Regarding a Detection of Bovine Spongiform Encephalopathy (BSE) in the United States,” May 2, 2012.

¹⁷ *International Trade Reporter*, May 3, 2012.

demand for smaller vehicles, largely in response to the rapid increase in gasoline prices, while demand for U.S.–manufactured cars plummeted. Facing pressure from the U.S. auto industry and pressure from Congress in the form of limits on imports of Japanese made cars, the Reagan Administration persuaded Japan to agree in 1981 to voluntary export restraints. Japanese manufacturers responded to the restraints by establishing manufacturing facilities in the United States and exporting high-valued, passenger cars. U.S. manufacturers asserted that Japan employed various measures to restrict sales of foreign-made cars in Japan and the use of U.S.-made parts in Japanese cars manufactured in the United States. These issues were the subject of bilateral negotiations and agreements through the 1990s. The agreements were mostly in the form of Japanese government pledges to ensure that government regulations did not impede the sale of U.S.-made cars in Japan and voluntary efforts on the part of Japanese manufacturers to increase the use of U.S.-made autoparts in cars made in the United States. The U.S. government pledged to implement programs to promote the export of U.S.-made cars in Japan.

The three Detroit-based car manufacturers—Chrysler, Ford, and General Motors—have responded to the possibility of Japan joining the TPP by charging that Japanese government regulations continue to prevent them from obtaining their fair share of Japanese domestic vehicle sales. They cite the traditionally small share of total cars sales in Japan that consist of imported cars—around 5%. In contrast, imports accounted for 26% of U.S. sales of light vehicles in 2010.¹⁸ U.S. manufacturers also point to the small share of total sales accounted for by U.S. origin cars—0.2% in 2010.

Among other things, U.S. car manufacturers claim that safety and certification rules and the lack of transparency in their development and implementation discourage imports of U.S. made vehicles. U.S. automakers also cite the barriers to establishing dealerships in Japan that would sell their vehicles.¹⁹ The Japanese industry argues that U.S. manufacturers are not producing a sufficient number of small-engine cars that are in demand in Japan. In contrast, European manufacturers produce more of that type of model and their share of the Japanese domestic sales stood at 2.9% in 2010.²⁰

Insurance, Express Delivery, and Japan Post

Japan is the world's second largest insurance market, next to the United States. U.S.-based insurance providers have found it difficult to enter the market, especially in life and annuity insurance. They have been concerned about favorable regulatory treatment that the government gives to the insurance subsidiary Japan Post Insurance of Japan Post, the national postal system, which holds a large share of the Japanese domestic insurance market. Japan Post subsidizes the insurance operations from revenues from its other operations. Also, Japan Post Insurance is not subject to the same regulations as other, privately-owned insurance providers, both domestic and foreign-owned. Similarly, U.S. express delivery providers have charged that Japan Post's express delivery company obtains subsidies from the government-owned parent agency that gives it an unfair competitive advantage.

¹⁸ Automotive News, Databank.

¹⁹ 2012 National Trade Estimate Report on Foreign Trade Barriers (NTE), March 2012, p. 221.

²⁰ Japan Automobile Manufacturers Association, <http://www.jama.org/pdf/MVS2011.pdf>.

On October 1, 2007, the Japanese government of then-Prime Minister Junichiro Koizumi introduced reforms to privatize Japan Post and a major objective of his administration. The Bush Administration and many U.S. companies, particularly insurance companies, supported these reforms. However, successor governments led by the Democratic Party of Japan (DPJ) have taken steps to roll back the reforms. On March 12, 2012, the government introduced, and on April 27, 2012, Japan's legislature passed, a bill into law to loosen regulatory requirements. According to industry reports and other commentaries, the bill reverses the reforms that the Koizumi government introduced.²¹ The bill is reportedly a compromise package by the lawmakers from the ruling DPJ and the two largest opposition parties, the Liberal Democratic Party (LDP) and the New Komeito Party.²²

Overall U.S. Objectives

Japan's possible entry into the TPP touches on a range of U.S. trade and foreign policy objectives. The United States greeted positively Prime Minister Noda's November 2011 statement of pursuing the possibility of participation in the TPP. However, USTR Ron Kirk stipulated:

To join the negotiations, Japan must be prepared to meet the TPP's high standards for liberalizing trade and to address specific issues of concern to the United States regarding barriers to agriculture, services, and manufacturing trade, including non-tariff measures. Japan's interest in the TPP demonstrates the economic and strategic importance of this initiative to the region.²³

Market Access

Japan's entry into TPP negotiations could likely expand U.S. trade and investment opportunities in Japan. The target for the United States would be to get Japan to liberalize non-tariff measures, such as certain government regulations, which have been a more significant irritant than tariffs in U.S.-Japan trade relations. The TPP, as envisioned and being negotiated by the current set of nine countries, would cover at least some of these non-tariff measures that Japan maintains. If Japan enters the TPP negotiations, the United States and Japan would have a framework within which to address these long-standing market access issues.

Rules-based Trade Framework and Impartial Dispute Settlement

One drawback of bilateral frameworks that the United States and Japan have used in the past is that they have had no formal dispute settlement mechanism. For example, a number of trade disputes in the 1980s and 1990s—including on market access for U.S.-made autos and autoparts in Japan, Japanese trade practices in semiconductors, and access to Japanese markets for construction services—became highly politicized with threats of U.S. unilateral action,

²¹ Coalition of Service Industries, *Proposed Japanese Legislation Complicates Entry in to the TPP*, press release, April 6, 2012. Also, Parker, David A. and Matthew P. Goodman, *Japan Post Reform: Return to Sender*, commentary from Center for Strategic and International Studies, May 30, 2012.

²² World Trade Online, April 5, 2012.

²³ Office of the USTR, *Statement by U.S. Trade Representative Ron Kirk on Japan's Announcement Regarding the Trans-Pacific Partnership*, November 11, 2011.

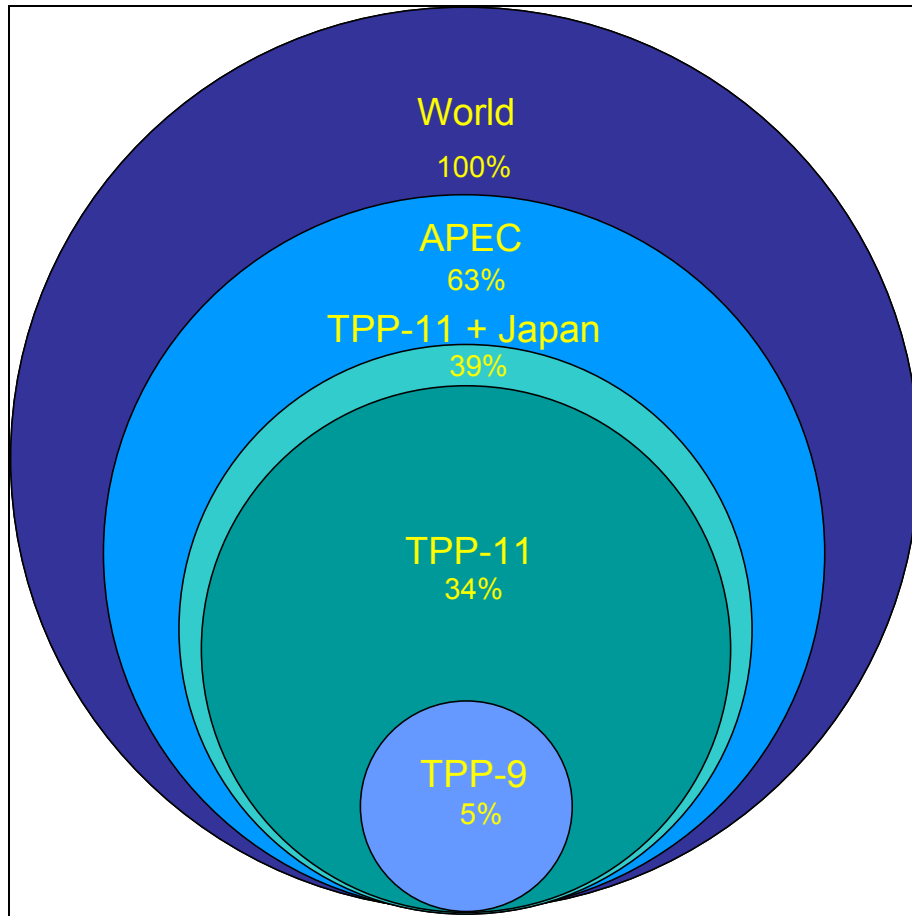
potentially undermining the overall relationship. Disputes usually were resolved through brinkmanship but often did not produce meaningful changes in Japan's trade practices or a significant increase of U.S. exports of the products in question. The TPP would provide a set of mutually agreed-upon rules that go beyond the WTO but would likely use an impartial, multi-party dispute settlement mechanism like that used in the WTO that would reduce the role of one-on-one confrontations in resolving issues.

Enhanced TPP

Japan would increase the economic importance of the TPP from the U.S. perspective. It would increase the amount of U.S merchandise trade that the TPP (the original 9 countries plus Canada and Mexico) would cover, from 34% to 39% based on 2011 data and would also increase trade in services and foreign investment activity within the TPP. (See **Figure 1.**) Japan would increase the share of the world economy accounted for by TPP countries (including Canada and Mexico), from around about 30% to about 38%.²⁴

²⁴ CRS calculations based on data in nominal dollars contained in the CIA *World Factbook* at <http://www.cia.gov> and in CRS Report R42344, *Trans-Pacific Partnership (TPP) Countries: Comparative Trade and Economic Analysis*, by Brock R. Williams.

Figure 1. U.S. Merchandise Trade with Various Countries and Trading Blocs
(shares of total, 2011)



Source: Analysis by CRS. See CRS Report R42344, *Trans-Pacific Partnership (TPP) Countries: Comparative Trade and Economic Analysis*, by Brock R. Williams, Data from U.S. ITC.

Japan's participation might strengthen the U.S. position on many issues within the TPP. The United States and Japan share some common objectives, including: strong intellectual property rights protection; protection of foreign investment; clear rules of origin to facilitate trade; and market access for services.

Foreign Policy Interests

In addition to trade and investment interests, Japan's participation in the TPP could affect U.S. political and foreign policy interests. The U.S. entry into the TPP negotiations is part of the Obama Administration's foreign policy and military "rebalancing" to the Asia-Pacific—often referred to as the "pivot" to the Pacific—announced in 2011.²⁵ The pivot refers to a series of diplomatic, military, and economic measures that the United States has taken or plans to initiate to influence the evolving rules and norms of the Asia-Pacific region. Many policymakers and

²⁵ For more analysis of the "pivot," see CRS Report R42448, *Pivot to the Pacific? The Obama Administration's "Rebalancing" Toward Asia*, coordinated by Mark E. Manyin.

analysts believe that China's pursuit of its own bilateral and multilateral economic arrangements has produced a competition of sorts over the shape of Asia's future economic architecture, in which the United States and several other countries in the Pacific are pushing for a deeper set of regional economic rules and expectations than Chinese leaders prefer.²⁶ The potential inclusion of Japan, as the second largest economy—and richest economy on a per capita basis—in East Asia could transform this struggle between alternative visions of regional trade rules. Additionally, U.S. and Japanese participation in the same free trade agreement could arguably be viewed as a means to reaffirm their alliance. The long-running bilateral relationship at times over the years has been overshadowed by U.S. and Japanese interests and concerns elsewhere in Asia, e.g., China and the Korean Peninsula, and in other parts of the world.

Japan's Objectives

Underlying the arguments for Japan to join the TPP talks is a growing feeling among many Japanese that, after two decades of relatively sluggish growth, Japan's economic and political influence is waning in comparison with China and with middle powers such as South Korea. The rapid aging and gradual shrinking of Japan's population has added to a sense among many in Japan that the country needs to develop new sources of growth to maintain, if not increase, the country's living standards. Japanese proponents of TPP have called for joining the talks for a number of overlapping reasons, some defensive in nature, others more proactive:

- **A desire to promote Japanese growth and prevent the hollowing out of Japan**—i.e., the relocation of Japanese companies to other countries—by expanding Japanese exports, especially to the fast-growing Asia-Pacific region. The decade-long stalemate in the WTO's "Doha Round" of trade talks, plus the explosion in bilateral and multilateral FTAs over the past decade, has led Japan to cautiously pursue its own FTAs.²⁷ As noted earlier, Japan is an important link in the Asia's global supply chains, and the TPP could facilitate operations within the supply chain. Conversely, greater trans-Pacific economic integration could potentially erode Japan's place in these manufacturing and export networks.²⁸
- **A feeling that Japan is being left behind in negotiating FTAs.** Although Japan has signed 13 FTAs—what it calls Economic Partnership Agreements (EPAs)—it has none with a major economic power, with the possible exception of the 2011 Japan-India EPA, and many of them exclude agricultural trade. (See **Table 3**.) In contrast, South Korea, the country many Japanese now compare themselves to, has signed FTAs with the United States, the European Union (EU), and in 2012 opened negotiations with China. If Japan is left behind in the FTA race, the feeling runs, its companies will be left at a competitive disadvantage.²⁹ Japan has

²⁶ August 2012 conversation with Takeshi Terada, Professor, Doshisha University.

²⁷ For historical background on Japan's FTA strategy, see archived CRS Report RL33044, *Japan's Free Trade Agreement Program*, by Raymond J. Ahearn.

²⁸ For more information on supply chains, CRS Report R40167, *Globalized Supply Chains and U.S. Policy*, by Dick K. Nanto.

²⁹ For instance, in his opening statement at a November 2011 press conference to discuss Japan's decision to explore joining the TPP talks, Prime Minister Noda said, "as a trading nation, in order to pass down the affluence we have cultivated to our future generations and to develop our society into one with vigor, we must incorporate the economic growth of the Asia-Pacific region." Japanese Prime Minister's Office, "Press Conference by Prime Minister Yoshihiko (continued...)"

belatedly tried to make up for the gap by discussing whether to open FTA negotiations with the EU and agreeing to begin negotiations on a trilateral FTA with China and South Korea. Indeed, some Japanese see these two sets of talks—particularly the “CJK” (China-Japan-South Korea) FTA negotiations—as alternatives to joining the TPP.

Table 3. Japan's Free Trade Agreements

In Force	Negotiating	Under Discussion
Japan—ASEAN ^a	Japan—Australia	Japan—European Union
Japan—Brunei	ASEAN+3	Japan—Canada
Japan—Cambodia	ASEAN+6	Japan—China—South Korea (negotiations to begin in 2012)
Japan—Chile		Japan—Mongolia
Japan—India		Japan—South Korea
Japan—Indonesia		TPP
Japan—Malaysia		
Japan—Mexico		
Japan—Peru		
Japan—Philippines		
Japan—Singapore		
Japan—Switzerland		
Japan—Thailand		
Japan - Vietnam		

Source: Japanese Ministry of Foreign Affairs, <http://www.mofa.go.jp/policy/economy/fta/index.html>.

a. ASEAN stands for the Association of Southeast Asian Nations, which consists of Brunei Darussalam, Burma (Myanmar), Cambodia, Indonesia, Laos, Malaysia, the Philippines, Singapore, Thailand, and Vietnam.

- **A belief that entering the TPP will help promote economic reforms inside Japan.** Over the years, many experts and government officials have argued that Japan needs structural reform to spur its economy. A number of Japanese commentators and officials believe that one way to overcome resistance to reform from vested interests is through negotiating a comprehensive, high-standard FTA such as the TPP, which will help reform-minded groups and individuals by giving them political cover. Also, negotiating the TPP could potentially enable Japan to gain benefits by trading structural reforms for concessions from negotiating partners.
- **A hope that entering the TPP will help Japan's strategic situation in Asia.** Joining the TPP would complement Japan's moves in recent years to augment the U.S.-Japan alliance by strengthening Tokyo's relationships with middle powers in

(...continued)

Noda," Friday, November 11, 2011.

and around the Asian region. Behind this push is a concern that China's rise is diminishing Japan's influence and eventually could jeopardize its security and economic interests.

At this preliminary point in the negotiations over whether Japan will join the TPP talks, it does not appear that the Japanese government has made any requests for concessions from the United States. There are some items that the United States presumably could offer Japan to make it politically easier for Japan to enter the negotiations. The most significant of these would be an understanding that some exceptions—such as rice—would be allowed in the final deal. Although such a promise would violate the TPP's operating premise that all items would be “on the table,” many believe that ultimately a final agreement will allow at least small number of “sacred cows” to continue.

Japanese Politics and the TPP

The question of whether Japan should join the TPP negotiations has often been front-page news in Japan and has generated enormous political controversy since serious discussion of the possibility began in 2009 and 2010. Both the ruling Democratic Party of Japan (DPJ) and the largest opposition party, the Liberal Democratic Party (LDP) are split over the TPP issue. The frequent turnover among Japanese prime ministers—Japan is being governed by the sixth premier in as many years—has failed to produce the leadership that might unify the pro-TPP camps across the two parties. These political weaknesses have exacerbated the traditional institutional limitations of the prime minister's powers, making it more likely that motivated interests can effectively veto government action. As a result, Japanese leaders have neither decisively stated they intend to join the negotiations, nor demonstrated they have the political clout to overcome opposition to the changes that acceding to TPP would entail.³⁰

Most observers believe that Prime Minister Noda wishes to bring Japan into the TPP talks. However, since the beginning of his tenure in September 2011, the longevity of Noda's time in office has almost continuously been called into question, making it difficult for him to go on the offensive on the TPP issue. Additionally, Noda has placed other items higher on his list of priorities, including passing a consumption tax measure, pushing for economic reconstruction and reform in the aftermath of the March 11, 2011 earthquake and tsunami, and dealing with Japan's new energy supply landscape.

For much of 2012, Noda's strategy appears to have been to try to resolve most if not all of these issues before attempting to marshal the support that would be needed for Japan to join the TPP talks. Pushing forward on TPP could lead to defections from Noda's Democratic Party of Japan, depriving it of its majority in the parliament's Lower House, which chooses the prime minister. The prospects for entering TPP in 2012 were further set back in August 2012, when the LDP and its allies forced Noda to promise to hold Lower House elections "at an early date" in

³⁰ As noted earlier, Prime Minister Noda stated in November 2011 that he would begin the process of *consulting* with countries that are negotiating the TPP: “We will start consultations with the countries concerned, make efforts to gather further information as to what each country would expect from Japan, and, through sufficient national debate, reach a conclusion on the TPP faithfully from the viewpoint of our national interests.” On the eve of Noda's announcement, a DPJ study team issued a recommendation that neither endorsed nor opposed TPP participation, a sign that the group was unable to bridge its differences. The LDP's own ambivalence is reflected in its formal position that it is opposed to unconditional entry into the TPP.

exchange for their support for passing Noda's initiative to raise Japan's consumption tax. Most analysts expect the elections to be held by early 2013. The DPJ is widely expected to do poorly and perhaps lose the premiership. For its part, the LDP has formally opposed entering the agreement if it does not allow for some exemptions.³¹

Japan's powerful agricultural institutions, most notably the nationwide agricultural cooperative organization (JA), have been the most vocal opponents of joining the TPP, as has been true of virtually all trade liberalization agreements that Japan has pursued for the past 40-50 years. Japan's farm sector has taken advantage of the fact that Japan's rural areas are over-represented in the Diet. As a result, farm lobbies have significant sway in both the ruling DPJ and the LDP and have supported an array of policies that benefit the agricultural sector. For example, many farm products remain protected behind high tariff barriers. (See Table 4.) Additionally, a range of other policies ensure that Japanese farming remains small scale, performed increasingly by aging and part-time farmers, and generally unproductive compared to farms in most other countries. The Japanese government provides around ¥1 trillion (about \$12 billion) annually in direct income to farming households.³² In an effort designed in part to ease opposition to joining the TPP, the Noda government in the fall of 2011 unveiled an agricultural reform plan which, according to Japanese farm policy expert Aurelia George Mulgan, has not been advanced beyond a few tentative measures.³³

Table 4. Comparative Japanese and U.S. Tariff Rates on Select Agricultural Products
(Average applied ad valorem MFN rates)

Category	Japan	United States
Animal Products	18.9	2.3
Dairy Products	93.3	20.3
Fruits & Vegetables	10.6	4.9
Coffee & Tea	15.3	3.2
Cereals & Preparations	42.0	3.5
Oilseeds, Fats & Oils	9.0	4.6
Sugars and Confectionary	27.2	10.3
Beverages & Tobacco	14.6	15.6

Source: WTO Tariff Profiles.

JA has allied with a variety of other powerful interest groups to mount an aggressive campaign against entering the TPP. The most significant of these other groups may be the Japan Medical Association, which argues that TPP will erode if not eliminate Japan's universal healthcare

³¹ The LDP also has wanted to protect Japan's food safety standards, has objected to some investor-state dispute settlement requirements that might be agreed to in the TPP, and has argued that government procurement and financial services must have their basis in Japan's 'special characteristics.' Aurelia George-Mulgan, forthcoming article, *Current History* and July 2012 conversation with Aurelia George-Mulgan, Professor, University of New South Wales Canberra.

³² Aurelia George Mulgan, "Japan's New Agricultural Policy Plan Neglects Trade Liberalisation," East Asia Forum blog, November 2, 2011, <http://www.eastasiaforum.org>.

³³ Laura Araki, "An Interview with Aurelia George Mulgan. Japanese Agricultural Reform and the Trans-Pacific Partnership," *National Bureau of Asian Research Policy Q & A*, June 21, 2012. The Noda government plan is called the Basic Policy and Action Plan for the Revitalization of Our Country's Food and Agriculture, Forestry and Fisheries.

insurance system because it will be forced to pay higher prices for medicines and medical equipment. Many experts argue that Japan's traditional agriculture interests, medical lobby, and other TPP opponents have successfully controlled the debate about TPP inside Japan. They have gained the support of scores of lawmakers, including a group of around 100 DPJ Diet members who belong to the "association to think carefully about the TPP." Among the arguments that many of the TPP opponents make is that the United States is compelling the Noda government to consider entering the negotiations.

The Views of U.S. Stakeholders

In a December 7, 2011 *Federal Register* notice, the Office of the USTR solicited the views of private sector stakeholders on whether Japan should be included in the TPP. USTR received over 100 responses. Around 40% of the responses were from agricultural firms, another 25% came from manufacturing firms, 15% from services providers and the remainder from various non-government organizations (NGOs) and business associations. Some of the responses came from Japanese companies or associations representing Japanese companies.

In a few cases, the respondents expressed outright opposition to Japan's participation. One of the most notable members of this group is the American Automotive Policy Council (AAPC).³⁴ The AAPC represents the three Detroit-based auto manufacturers—Chrysler, Ford and General Motors. In its statement, the AAPC said:

The AAPC opposes Japan joining the Trans-Pacific Partnership negotiations at this time... Japan's trade barriers in the auto sector cannot be addressed easily or quickly, and will needlessly slow down the negotiations. To date Japan has not indicated a willingness to change its decades-long practice of maintaining a closed automotive market. Given the systemic trade imbalance and lack of willingness to reform, a U.S. free trade agreement with Japan would only lock-in the already one-way trade relationship that Japan's closed auto market has created, and significantly delay, if not prevent proceeding with a high quality TPP trade agreement with other more compatible trade partners in the important and rapidly growing Pan-Pacific region.

The AFL-CIO also opposes Japan's participation in the TPP, having stated:

Given the numerous unknowns about the yet unfinished Trans-Pacific FTA, it is difficult to provide significant technical advice or even formulate well-grounded opinion with respect to the possible impacts on working families of Japan's accession to the Trans-Pacific FTA.

As such, the AFL-CIO has serious concerns regarding the premature expansion of the Trans-Pacific FTA negotiations to include Japan or any other nation before US negotiators first demonstrate an ability to successfully negotiate an agreement that will produce genuine benefits for American workers and increase domestic production.

[Japan's] markets are notoriously closed to foreign goods, and this is not the result of high tariff barriers.... To gain significant and substantial market access to Japan, the United States Trade Representative (USTR) would have to adopt a new and revolutionary approach.... If USTR is not willing to 'think outside the box' and abandon its currently slavish approach to

³⁴ AAPC, The American Automotive Policy Council's (AAPC) Views Regarding Japan's Expression of Interest in the Trans-Pacific Partnership (TPP) Trade Negotiations, January 13, 2012.

free trade, it is difficult to see how Japan's accession to the Trans-Pacific FTA can benefit American working families.³⁵

In some cases, respondents expressed strong support for Japan's inclusion in the TPP. For example, Caterpillar, Inc. argues that the TPP would be the vehicle for addressing Japan's remaining non-tariff barriers.³⁶ The U.S. Chamber of Commerce and the U.S.-Japan Business Council, in separate submissions, also expressed support for Japan's participation in the TPP negotiations. However, each group asserted that Japan would have to address issues that have plagued relations with member companies, including regulatory barriers, favored treatment of insurance and express delivery subsidiaries of Japan Post, and government procurement, among others.³⁷

Some Members of Congress have weighed in on the issue. For example, in a November 8, 2011, bipartisan letter to USTR Ron Kirk, the Chairmen and Ranking Members of the House Ways and Means Committee and the Senate Finance Committee stated that Japan's participation "would represent an opportunity for much needed change in Japan's approach to international trade." They assert that, while Japan is a long-time U.S. ally and friend in Asia,

...paramount considerations in evaluating a request relating to a trade agreement must be whether Japan is willing and able to meet the high standard commitments inherent in U.S. free trade agreements and whether inclusion would truly open this historically-closed market to the benefit of our companies, workers, and farmers.

These comments and others from stakeholders suggest that the debate within the United States and negotiations with Japan on the TPP will be difficult and complex. The legacies of a sometimes contentious bilateral economic relationship have carried over into the TPP negotiations.

Outlook, Possible Outcomes, and Consequences

Japan's negotiations with the United States, as well as its negotiations with Australia and New Zealand, continue with no publically announced deadline or timeframe. The Obama Administration has stated that it wants to take as much time as necessary but would not let these negotiations interfere with the pace of the negotiations among the current TPP countries. The June 2012 invitations to Canada and Mexico to join the TPP may place a stronger spotlight on Japan, at least politically, as the remaining outstanding country of the three that has expressed interest in joining.

If Japan enters the TPP, it could represent a major change in the shape and dynamic of the U.S.-Japan economic relationship. Over the years, trade policymakers, business representatives, and regional specialists in both countries have floated the concept of a U.S.-Japan FTA. Until the TPP talks began in earnest, the idea had not gained traction because the hurdles—Japanese agricultural

³⁵ AFL-CIO, Comments in Response to "Request for Comments on Japan's Expression of Interest in the Proposed Trans-Pacific Partnership Trade Agreement."

³⁶ Caterpillar's Views Regarding Expanding Trans-Pacific Partnership Negotiations to Include Japan, Mexico, and Canada, January 11, 2012, Submission to the Office of the USTR.

³⁷ U.S. Chamber of Commerce January 13, 2012 letter to o USTR and U.S.-Japan Business Council, Public Comment, *Japan's Expression of Interest in the Proposed Trans-Pacific Partnership Negotiations*.

policy, problems in auto trade, government regulations and practices—have been too high to overcome. These same hurdles would need to be overcome if Japan and the United States are able to work successfully in the TPP.

The outlook for Japan's entry into the TPP negotiations remains unclear at this time and depends on a number of factors. Perhaps the most critical factor is whether Japanese political leaders can reach a political consensus on whether to proceed with the negotiations and then whether Japan can reach agreement with the TPP partners on conditions of its entry. The timing of Japan's decision on whether to proceed has likely been delayed by domestic politics. Recently, in return for the LDP and the New Komeito Party agreeing to a vote on the consumption tax, Prime Minister Noda promised to dissolve the Lower House "at an early date." As a result, new elections for the lower house would be called, possibly resulting in changes in control of the legislature. Therefore the decision on TPP will likely not be before this December at the earliest but most likely later. Japan expert Ed Lincoln has suggested the decision will likely be pushed even farther out.³⁸

The outcome of this issue could have implications for the U.S.-Japan bilateral trade relationship, the overall alliance, and the TPP. The TPP issue presents opportunities and challenges for the United States and Japan. On the one hand, if successful, it could reinvigorate an economic relationship that has remained steady but stagnant, by forcing the two countries to address long-standing, difficult issues, and allowing them to raise their relationship to a higher level. On the other hand, failure to do so could indicate that the underlying problems are too fundamental to overcome and could set back the relationship. It could signify the failure of the United States and/or Japan to deal with domestic opposition to a more open trade relationship.

The implications for the overall U.S.-Japanese alliance are less certain. While the TPP would likely be viewed as strengthening the alliance, and failure of the negotiations could be considered a setback, the alliance is also built on common national security concerns, such as North Korea's nuclear program and the economic and military advancement of China, which could well trump trade problems.

Furthermore, Japan's possible entry into the TPP is largely viewed, on the one hand, as an important step in forming a wider Asia-Pacific regional trade arrangement. On the other hand, the absence of Japan could undermine the credibility of the TPP as a viable regional trade arrangement and a setback for Asia-Pacific economic integration.

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³⁸ *World Trade Online*, August 9, 2012.