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Article

Fuji-Kodak, the WTO, and the Death of Domestic Political Constituencies

Sara Dillon*

I. MAKING SENSE OF THE *FUJI-KODAK* CASE

On March 31, 1998, a World Trade Organization (WTO) Panel presented its Report in the *Fuji-Kodak* case.¹ The Panel's decision ostensibly represented a stunning blow for U.S. commercial interests, especially in light of the fact that many of the issues raised in the case were extensions of U.S. preoccupations during the so-called "Structural Impediments Initiative" of the early 1990s.² The United States had long complained to Japan

* Law Faculty, University College Dublin

1. *Japan—Measures Affecting Consumer Photographic Film and Paper*, Report of the Panel, WTO Doc. WT/DS44/R (Apr. 3, 1997) <<http://www.wto.org/wto/dispute/distab.htm>> [hereinafter *Fuji-Kodak Panel Report*].

2. The Structural Impediments Initiative (hereinafter SII), a long series of intense bilateral negotiations aimed at convincing Japan to liberalize its internal economy, was initiated by the Bush Administration to increase U.S. market share in key Japanese sectors. See Jonathan D. Richards, *Japan Fair Trade Commission Guidelines Concerning Distribution Systems and Business Practices: An Illustration of Why Antitrust Law Is a Weak Solution to U.S. Trade Problems With Japan*, 1993 WIS. L. REV. 921, 930-31 (1993). Richards writes:

Working under the U.S. trade negotiators' assumptions and recognizing that the United States also has its own problems contributing to the trade imbalance with Japan, the Bush Administration, starting in July of 1989, engaged the Japanese government in a series of talks seeking agreements for fundamental reforms in each country to reduce the tension on their trade relations. That series of talks was called the Structural Impediments Initiative. From their inception, the SII talks had as much to do with politics as with erasing the trade deficit with Japan. . . . [T]he six areas that the Japanese delegation agreed to address under the SII talks were: Japanese savings and investment patterns, land policy, distribution systems, exclusionary business practices, keiretsu relationships, and pricing mechanisms.

Id. See also KENJI HIGUCHI, FIKUSHON TO SHITE NO SHOHISHA RIEKI (1991) (describing in detail the political background against which America attempted to persuade Japan to remove its protection for the small and medium retail sector during the SII).

about its failure to enforce competition law principles; the U.S. had also long demanded that Japan eliminate its law protecting small and medium retailers—the Large Scale Retail Stores Law, or *Daitenho*.³

The transformation from the General Agreement on Tariffs and Trade (GATT)⁴ to the WTO regime has been characterized by an enormous proliferation in causes of action and by greatly increased legalism in dispute resolution.⁵ Panel decisions under the new WTO undoubtedly led the U.S. to believe that it might succeed in *Fuji-Kodak* and thus further extend the reach of WTO law into domestic economies. The WTO's panel decisions thus far have been unabashedly expansionist; they have shown little concern for domestic regulation, regardless of the sensitivity of the local politics surrounding the regulation in question.

This trend perhaps encouraged the U.S. to raise novel arguments in the course of the *Fuji-Kodak* dispute. In the view of many commentators, the best U.S. argument in *Fuji-Kodak* challenged the WTO-legality of the Large Scale Retail Stores Law under the General Agreement on Trade in Services (GATS).⁶ This line of argument, though ultimately dropped,

3. See DAITENHO, 1973/10/1, Law No. 109 (Japan), as amended. Legislation was passed on May 27, 1998, repealing the Large Scale Retail Stores Law, effective April 2000. See United States Trade Representative (USTR), *Access to Japan's Photographic Film and Paper Market: Report on Japan's Implementation of its WTO Representations*, "Assessment of Japan's Implementation of Specific Representations It Made to the WTO," at 2 (on file with author).

4. General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-11, T.I.A.S. 1700, 55 U.N.T.S. 194 [hereinafter GATT].

5. See MICHAEL TREBILCOCK & ROBERT HOWSE, *THE REGULATION OF INTERNATIONAL TRADE* 38-39, 397-98 (1995). See generally David Palmeter & Petros C. Mavroidis, *The WTO Legal System: Sources of Law*, 92 AM. J. INT'L L. 398 (1998) (explaining the legal transition from the GATT system to the WTO).

6. In fact, the initial case involved three separate actions by the U.S. against Japan. See Charlene Barshevsky, Press Statement, in United States Trade Representative (USTR) (June 13, 1996) (on file with author). The USTR initially stated that the U.S. would "make three separate requests for consultations under WTO auspices on the broad range of market access barriers in the consumer photographic materials sector in Japan." *Id.* These were described as follows:

First, the U.S. is requesting consultations regarding violations of the General Agreement on Tariffs and Trade 1994 (GATT) and nullification and impairment of GATT benefits arising from the full panoply of liberalization countermeasures that the Government of Japan has put in place and maintained to thwart imports in this sector.

Second, the U.S. is requesting consultations regarding violations of the General Agreement on Trade in Services (GATS) arising from the requirements and operation of the Large Scale Retail Stores Law, which constitute a serious barrier to foreign service suppliers as well as imports of film and other consumer products.

produced its desired result. Under an agreement reached during preliminary *Fuji-Kodak* negotiations and outside the supposedly transparent legalities of the WTO, the U.S. obtained a Japanese commitment to abolish its Large Scale Retail Stores Law.⁷

One interpretation of such pre-panel concessions is that they have always been part of the negotiating process under the GATT/WTO dispute settlement system. Yet “negotiations” under the new WTO significantly differ from those under GATT: since a country adversely affected by a Panel decision can no longer prevent the decision’s adoption,⁸ a “defendant” member country now faces much higher stakes in the disputes process, and therefore a complainant party’s ability to threaten WTO action to force long-sought regulatory concessions has increased.

Third, the U.S. is requesting consultations under a GATT decision concerning consultations on restrictive business practices. Through this mechanism, the U.S. intends to discuss with the Government of Japan the significant evidence of anti-competitive activities that it has uncovered in this sector, and to ask the Government of Japan to take appropriate action.

Id.

In fact, the U.S. only proceeded to a panel on the issues relating to GATT. There was a feeling in Japan that it was possible the U.S. would prevail on the GATS argument. This would have had serious consequences for the Japanese retail sector because reform of this sector would have been extremely politicized and exposed to international scrutiny. This Article will demonstrate how the U.S. came to make a “deal” with Japan, which in turn led the U.S. to drop this aspect of the case. The third arm of the case, taken under the GATT decision on restrictive business practices, is currently “in abeyance.” The U.S. had originally asked for separate panels to deal with arguments under the respective agreements.

7. See United States Trade Representative, “Assessment of Japan’s Implementation of Specific Representations It Made to the WTO,” *supra* note 3, at 2.

On May 27, the Japanese government passed legislation repealing the Large Scale Retail Stores Law . . . effective April 2000. The U.S. Government welcomed the repeal of this law, which has been a major impediment to the establishment, operation, and expansion of large retail stores. Senior Japanese Government officials have acknowledged that this action was taken because of concern that a WTO panel would very likely find the Large Stores Law in violation of the General Agreement on Trade in Services (GATS).

Id.

8. See Matthew Schaefer, *National Review of WTO Dispute Settlement Report: In the Name of Sovereignty or Enhanced WTO Compliance*, 16 ST. JOHN’S J. LEGAL COMMENT. 307, 313 (1996) (noting that under the WTO system countries traded the power to block a decision for the mere right to appeal an adverse decision).

Such coercion occurs even when the defendant country has long-standing policy reasons to retain the challenged domestic law.⁹

If viewed conventionally, the *Fuji-Kodak* case that remained and went to the panel (based on GATT Article XXIII: 1(b), and GATT Articles III and XI) can be understood as an uncommon failure on the part of the U.S. to anticipate the Panel's likely reaction to its legal arguments. The U.S. legal position might be seen as uncharacteristically forced and convoluted, or as simply an ineffective argument. The U.S. decision not to appeal might serve as confirmation that the U.S. was aware of having miscalculated. The case thus appears to some commentators as simply an interesting oddity, notable only for the few arguments concerning competition law and market access that were ahead of their time.¹⁰

The case is unusual to the extent that the U.S. as complainant does not normally fail at the WTO. Since WTO panels have exhibited a willingness to interpret the already quite expansive Uruguay Round Agreements broadly, many trade experts expected the U.S. to prevail. In my view, however, the U.S. did not entirely lose *Fuji-Kodak*, because the US secured from Japan a long-sought concession—a “sell out” of small business interests in Japan by the Japanese bureaucracy which completely revised national laws protecting the small and medium retail sector.

A. THE WTO AND EFFECTS ON DOMESTIC REGULATION

Academic fatalism attends research on international trade law.¹¹ Unlike scholars in other legal fields, international trade scholars have avoided an empirical analysis of the *effects created* by the law which dominates their field of inquiry: GATT/WTO. Particularly in the post-1995 trading system, these experts assume that a legal hierarchy exists in which international trade rules trump domestic regulation.¹²

9. See John H. Jackson, *The Great 1994 Sovereignty Debate: United States Acceptance and Implementation of the Uruguay Round Agreements*, 36 COLUM. J. TRANSNAT'L L. 157, 171 (1997) (noting that the WTO may cause external influences on domestic policy).

10. See, e.g., Douglas E. Rosenthal, *Jurisdiction and Enforcement: Equipping the Multilateral Trading System With a Style and Principles to Increase Market Access*, 6 GEO. MASON L. REV. 543, 543 & 554 (1998) (discussing competition law and market access under the WTO).

11. See, e.g., Sara Dillon, *Trade and the Environment: A Challenge to the GATT/WTO Principle of "Ever Freer Trade"*, 11 ST. JOHN'S J. LEGAL COMMENT. 351 (1996) (noting the lack of public discussion).

12. See David Kennedy, *The International Style in Postwar Law and Policy: John Jackson and the Field of International Economic Law*, 10 AM. U. J.

Yet domestic regulation often protects vulnerable national sectors and reflects the culmination of political activity on behalf of these groups. In the jargon of international trade, these "special interests" are seeking "protectionist" measures by their governments.¹³ Such political activity, however, is a key component of democratic lawmaking and should not be so easily dismissed.¹⁴

The Large Scale Retail Stores Law aspect of the *Fuji-Kodak* case highlights the fundamental conflict between national democratic "inputs" and the external threat the WTO poses to them. In 1997, when the Japanese Ministry for International Trade and Industry (MITI) proposed a complete overhaul of the law protecting small retailers, reportedly not one of Japan's parliamentary representatives was in favor of changing the law.¹⁵ This is not to imply that there was no Japanese constituency in favor of change. A number of sectors in Japan had long hoped that external pressure would lead to revision of the Large Scale Retail Stores Law.¹⁶ No reformist group within Japan, however,

INT'L L. & POL'Y 671, 703 (1995). Kennedy discusses the rhetorical universe created by the eminent Professor John Jackson in his development of international trade law as an academic discipline: "Jackson presents national policy either as already part of international economic law . . . or as an unfortunate deviation. In Jackson's view, the choice is not between those areas of national public life which are part of 'domestic jurisdiction' and those which have come to be regulated internationally, but between areas that do and do not support liberal trade." *Id.* at 703.

13. There has been a good deal of comment on the problem of the democratic deficit in international trade law generally; however, most writing on the subject is not presented with a sense of crisis. See, e.g., Andrea Schneider, *Democracy and Dispute Resolution: Individual Rights in International Trade Organizations*, 19 U. PA. J. INT'L ECON. L. 587 (1998) (describing the doctrine that holds that democratic input by political constituents is really no more than "political capture by narrow interests" within the state). Schneider sees the solution in terms of individual ability to engage in and enforce the terms of the international organization. *Id.* See also Wolf Sauter, *The Economic Constitution of the European Union*, 4 COLUM. J. EUR. L. 27 (1998) (discussing a conceptually similar problem at the European level).

14. *Id.*

15. Interview with MITI official, in Tokyo, Japan (July 2, 1998).

16. See Frank K. Upham, *Privatized Regulation: Japanese Regulatory Style in Comparative and International Perspective*, 20 FORDHAM INT'L L.J. 396 (1996). Upham writes:

[D]espite retailers' general satisfaction with the Large Scale Retail Stores Law (LSRSL), some level of reform became inevitable in the late 1980s. Foreign pressure was a major impetus for reform, but domestic pressure was equally strong. Between 1988 and 1989, the Japanese media, the *Keidanren*, the Economic Planning Agency ("EPA"), the Fair Trade Commission ("FTC"), and the . . . Second Administrative Reform Commission all called for varying degrees of relaxation. . . . [A]s the direct target of small retailers' pressure to strengthen the LSRSL, only MITI resisted.

had been able to defeat the political power of the small and medium retail sector and achieve fundamental revision or repeal of the law. Significantly, the decision in 1997 by Japan's elite bureaucracy to repeal the law and set aside a central component in Japan's commercial culture did not derive from a domestic source.¹⁷ Rather, the final decision resulted primarily from the immensely imaginative grafting together by the U.S. of a Section 301 complaint submitted by the Kodak company to the United States Trade Representative (USTR).

The *Fuji-Kodak* case stands at the crossroads of an increasingly ambitious WTO and a long-held U.S. belief that market access to Japan is blocked by a mysterious cultural essence, an essence which can only be broken by a combination of relentless pressure on Japanese decision-makers and threats of exclusion from the U.S. market.¹⁸ The U.S. invoked such culturalist argu-

Id. at 420.

Regarding the larger Japanese retailers, Upham writes that "the fundamental consensus [among large retailers] is that the LSRSL should be applied in a way more advantageous to the superstores. Without mincing words, they would like a shift from restricted competition under the leadership of small retailers to managed competition under the leadership of superstores." *Id.* at 419.

Finally, Upham also shows that the Large Scale Retail Stores Law was meant to allow for the stable co-existence of small and medium retailers, with a certain predictable share of the total retail market for larger department stores, within competitive conditions controlled to some degree by MITI on the basis of these policy considerations. *Id.*

17. There is a distinct "modernizing" faction within MITI, although that faction would not have been able to convince politicians to accept drastic changes to the Large Scale Retail Stores Law without the justification provided by the prospective WTO case.

18. The "increasingly ambitious" WTO is a combination of proliferating causes of action via the Uruguay Round Agreements covering intellectual property, safeguards, and trade in services and investments, among others, and the newly stringent consequences of losing in the dispute settlement procedure. See Understanding on Rules and Procedures Governing the Settlement of Disputes, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex II, LEGAL INSTRUMENTS—RESULTS OF THE URUGUAY ROUND vol. 1, (1994), 33 I.L.M. 1125 (1994). See also David Broiles, *When Myths Collide: An Analysis of Conflicting US-Japan Views on Economics, Law, and Values*, 1 TEX. WESLEYAN L. REV. 109 (1994) (discussing the longstanding U.S. belief that Japan's market is kept closed though some mysterious cultural behavior—virtual cultural collusion). Broiles states that "Japanese successes and American failures in trade are often explained in highly emotive or moralistic terms. Japanese are said to be unfair, conspiratorial, unethical, guilty of imposing stringent quotas, manipulative of the market, engaging in collusive market practices, subsidizing industries, limiting access, biased against imports, and as unfairly limiting product promotion." *Id.* at 112 (citing EDWARD LINCOLN, AN AMERICAN POLICY AGENDA, JAPAN'S UNEQUAL TRADE 135-36 (1990)). Broiles' conclusion is that "Japan challenges America's myth about itself." *Id.*

ments to reinforce its position in *Fuji-Kodak*.¹⁹ Japan's response was unusually pointed: the U.S. had substituted prejudice for hard evidence.²⁰

This Article will explore *Fuji-Kodak* not as an anomaly in recent WTO history, but as a case highly symbolic of the manner in which social and cultural concerns at the national level are being extinguished by the greatly enhanced legalism of the WTO.²¹ By examining recent WTO cases and the effects of WTO actions *within* individual jurisdictions, this Article contends that the new post-1995 WTO has altered the relationship between national governments *as* WTO representatives and their political constituencies "back home."²² This Article concludes

19. See USTR, *supra* note 3. The USTR claimed that

[o]ur comprehensive investigation of the Japanese film market has shown that the Government of Japan built, supported, and tolerated a market structure that thwarts foreign competition, and in which exclusionary business practices are commonplace. . . . We see in this sector the same market barriers that are present in sector after sector in Japan. These are systemic structural barriers, such as closed distribution systems and excessive regulation, that we have been discussing with Japan for years. With the detailed evidence uncovered in this investigation, we now have a clear understanding of how these barriers have interacted to keep out competitive foreign products in a particular sector.

Id. at 1.

20. See *Japan—Measures Affecting Consumer Photographic Film and Paper*, First and Rebuttal Submissions of the Government of Japan (3 April 1997 and 20 May 1997), available in 1997 WL 295222. In these documents, Japan was adamant that the U.S. had substituted mischaracterization for fact. In MITI's executive summary of its First Submission, it stated that "[t]he United States accuses Japan of having masterminded and maintained for over 30 years a conspiracy with its domestic industry to block imported film and paper from the Japanese market." *Id.* at 2. MITI accused the U.S. of "gross inaccuracies" in describing Japanese behavior. *Id.* at 3. MITI also claimed that the U.S. approach was "factually inaccurate" and "legally baseless." *Id.* at 8, 10.

21. It does appear that the U.S. took the opportunity of Kodak's complaint concerning market access for film in Japan to push MITI into acting on its past commitments to abolish the Large Scale Retail Stores Law. It is probable that the U.S. dropped the most potent part of the overall case (the GATS arm) because it had already obtained what it most wanted—the imminent possibility of penetration of the Japanese retail market by mega-retailers from the U.S.

22. In a certain sense, the new legalism of the WTO offers a grand simplicity to the national negotiators. Unlike the convoluted world of pre-1995 trade diplomacy, the adversarial WTO system creates clear winners and losers. It offers an opportunity for national governments, which had been struggling with the resistance of traditional domestic constituencies to changes being brought about by trade principles, to justify a new departure in which "adjustment" replaces protection. A stunning example of this process is in the agricultural context. The WTO has provided a basis for the European Community to reduce economic support for the farming sector in a manner that would not otherwise have been politically feasible.

that the threatened *Fuji-Kodak* litigation made Japanese decision-makers aware that the new GATS Agreement had the potential to invalidate Japan's retail sector regulations, with unpredictable results. Rather than face such a legal bruising, MITI decided to alter the Japanese retail law, but in such a way as to confuse and pacify the endangered domestic constituency.²³

II. THE DEMOCRATIC FLAW IN THE WTO

There has been substantial academic discussion of the alleged usurpation of national sovereignty by the WTO and regional trade blocs, as if the most important change brought about in 1995 was that *nations* would no longer exercise full powers of external and internal decision making.²⁴ Yet sovereignty en-

Furthermore, no member country of the WTO is, as a national entity, either entirely advantaged or disadvantaged. The WTO system (in a more fully developed version of the old GATT) is in fact an interlocking web of national objectives. The troublesome point is not that the participant *nation* sometimes loses, but that now with striking regularity, certain national *sectors*—after having struggled to gain political protection—are being left unprotected by the working of WTO law. See generally Steve Charnovitz, *Free Trade, Fair Trade, Green Trade: Defogging the Debate*, 27 CORNELL INT'L L.J. 459 (1994) (highlighting the debate regarding trade and the environment); see also Robert F. Housman, *Democratizing International Trade Decision-Making*, 27 CORNELL INT'L L.J. 699 (1994) (advocating that internal trade rules should incorporate democratic principles).

A number of other recent, high-profile WTO cases have involved the invalidation of environmental and other forms of "protective" domestic regulation through the application of WTO rules. In those cases, the conflict between stark trade rules and the domestic impulse to regulate is clear and dramatic. In *Fuji-Kodak*, largely because the U.S. lost the case and because the most significant part of the overall case was dropped through a form of settlement agreement between Japan and the U.S., commentators have largely failed to grasp the significance of what has taken place *vis a vis* the world of Japan's small retailing sector. Some specialists in Japanese retailing believe that MITI's decision to push the political establishment towards the abolition of legislative protection for this sector will herald rapid and irreversible changes in Japanese domestic commercial relations. See KATSUHIKO NAMIKATA, DAITENHO HAISHI: EIKYO TO TAIO 112-56 (1998).

23. It must be noted that it was MITI's apparent wish to avoid the possibility of having Japan's retail sector discredited at the international level through an adverse panel ruling that led to the decision to move forward with abolishing the Large Scale Retail Stores Law. Yet MITI's new strategy—the creation of a set of alternative laws to replace the Large Scale Retail Stores Law—can in no way foster meaningful continued protection of the small and medium retail sector.

24. See, e.g., William Sprance, *The World Trade Organization and United States' Sovereignty: The Political and Procedural Realities of the System*, 13 AM. U. J. INT'L L. REV. 1225 (1998) (describing steps taken by the U.S. to protect its state sovereignty within the new WTO). See also George Bermann, *Constitu-*

compasses more than the rights of a nation to act independently among other nations. It also includes a nation's ongoing capacity to respond adequately to democratic "inputs," which serve as the proper building blocks of national legislation.²⁵

Democratic theory requires constituency input, legislative response, and judicial interpretation. The power of the new WTO to invalidate even the most hard-won domestic legislation should be generating heated debate, as opposed to an esoteric and sanitized one over the meaning of *state* sovereignty. The emphasis in academic circles on the rights and powers of the nation state, as opposed to the rights of persons living within those states, is highly misleading in that it suggests that the only issue is whether a state can legitimately waive its sovereignty.²⁶ Many experts justify the WTO system by noting that individual states have ratified the WTO Agreement.²⁷ Even so, the state cannot legitimately waive the democratic rights of its citizens to influence the content of national legislation.²⁸

Though characterized as more diplomatic than "legal," the GATT system from its inception in 1947 was nonetheless powerful to the extent that it could generate important international publicity for or against a country. Thus, even in its pre-1995 form, GATT exerted strong, even coercive, economic influence.²⁹

tional Implications of U.S. Participation in Regional Integration, 46 AM. J. COMP. L. 463 (1998) (exploring the hierarchy of laws as between international trade treaties and inconsistent national law).

25. See Jackson, *supra* note 9, at 157 (examining the nature of sovereignty).

26. *Id.*

27. See generally Housman, *supra* note 22 (noting the lack of democratic input in the development of international law).

28. The Uruguay Round Agreements in particular are extremely varied in subject matter and contain virtually endless bases upon which national regulation can be invalidated. It is impossible to imagine that citizens in the many countries in which these agreements were ratified had anything more than the most cursory understanding of either the content of the agreements or their implications for national legal regimes. There was no attempt to present the agreements as individual subjects of examination and political choice.

It should be recognized that the agreements that make up the WTO system are far more powerful than virtually any other treaties. No single-subject matter convention could induce compliance with the effectiveness of the multi-sectoral WTO regime. The possibility of economic retaliation outside the sector of the original dispute ensures that the consequences of non-compliance are, for any WTO member, extremely high.

29. Even in those cases where panel reports were blocked by adversely affected contracting parties, the domestic law found to be GATT-illegal tended to be revised, if not abolished, over time. Note, for example, changes to U.S. law after losses at the GATT in the *Domestic International Sales Corporations* case and *The Tuna - Dolphin* case. See *United States Tax Legislation (DISC)*, Report

Before 1995, however, the GATT system was not designed to impose an absolute will on participating states through orders and sanctions. States could block panel decisions unfavorable to themselves, thereby rendering the legal import of such decisions ambiguous, because panel reports only gained legal effect upon adoption by consensus of all participating GATT parties.³⁰

In addition to the decisive shift in 1995 away from a "diplomatic" approach to international trade rules and dispute resolution, the Uruguay Round created a number of significant agreements, encompassing areas not traditionally part of the international trade regime. These agreements increased the causes of action available to GATT/WTO plaintiffs.

This heady combination of greatly enhanced powers of genuine enforcement for WTO panel decisions, along with new and unexplored causes of action, meant that domestic constituencies were now far more vulnerable to the *diktats* of the WTO legal system. Previously, such constituencies were shielded from harsh trade rules by national governments that were to some degree responsive to democratic inputs. Indeed, as the WTO has increased its scope, so too has the scope of anti-democratic interference by the WTO in delicate domestic law regimes.

A. THE ASSUMPTION THAT WTO LAW TRUMPS: A FICTIONAL HIERARCHY OF LAWS

It is unclear how the WTO came to supersede domestic regulation in the hierarchy of laws. There has never been a global referendum on the subject.³¹ Many of the major disputes decided since 1995 can be seen as case studies on the following theme: WTO law is treated as fundamental and absolute, whereas national laws in such areas as public health, the environment, and economic protection for farmers or small business are treated as

of the Panel, Nov. 12, 1976, GATT B.I.S.D. (23rd Supp.) at 98 (1977); *United States—Restrictions on Imports of Tuna*, Aug. 16, 1991, GATT B.I.S.D. (39th Supp.) at 155 (1993).

30. See GATT, *supra* note 4, art. XXII.

31. While there has much critical comment in Europe concerning the democratic deficit in the EU, at least new areas of subject matter brought into the foundational Treaty requires referenda to be held in each of the participating members. See P. Raworth, *A Timid Step Forwards: Maastricht and the Democratisation of the European Community*, 19 EUR. L. REV. 16 (1994). See also William Wallace & Julie Smith, *Democracy or Technocracy? European Integration and the Problem of Popular Consent*, 18 W. EUR. POL. 137 (1995) (discussing the absence of democratic input in the EU).

contingent and optional, at least to the extent that these regulations can be undone by a WTO decision.³²

It is an open question why individual member countries do not resist adverse decisions more vocally. No WTO member country, however, is a political monolith. In some instances, national decision-makers may be happy to have the excuse of WTO fiat to undo the effects of long years of lobbying by interested citizens to pass protective legislation.³³ Prior to the Uruguay Round, national governments could not honestly inform domestic constituencies that they were being "forced" by the GATT to abandon protection of those constituencies' interests. In the post-Uruguay Round world, they can invoke international legal necessity, thus removing a great deal of direct internal political pressure.³⁴

The dull, technocratic language of WTO law serves to conceal its essential radicalism. A number of the principal cases recently decided at the WTO, however, demonstrate that the WTO is now capable of brusquely undoing the legislative will of national constituencies as expressed in domestic legislation. These constituencies lack a sufficient understanding of the WTO to know how to protest. Yet even if they did attempt organized protest, there is no responsive political mechanism at the WTO level. All such a constituency can do is exert pressure on the national government to alter its participation in the WTO. In response, the national authorities would undoubtedly counter

32. See, e.g., Jennifer Schultz, *The Demise of "Green" Protectionism: The WTO Decision on the US Gasoline Rule*, 25 DENV. J. INT'L L. & POL'Y 1 (1996) (discussing the WTO finding that the Environmental Protection Agency's regulation on imported gasoline was inconsistent with WTO obligations); Charnovitz, *supra* note 22 (discussing the impact of GATT rules on the environment).

33. This is especially true in difficult and financially draining areas such as agriculture. It is indisputable that the European Union has been able to shift responsibility for reform of the Common Agricultural Policy onto the WTO. Why and how the EU decided to include agricultural products within those products covered by free trade "discipline" is an issue that has not yet been fully explored. Farmers within the Member States of the EU itself also imperfectly understand this matter. See Al J. Daniel, Jr, *Agricultural Reform: The European Community, the Uruguay Round, and International Dispute Resolution*, 46 ARK. L. REV. 873 (1994) (describing some of the difficulties associated with bringing agricultural products into the GATT system). See also Miguel Antonio Figueroa, *The GATT and Agriculture: Past, Present, and Future*, 5 KAN. J.L. & PUB. POL'Y 93 (1995) (discussing the complexities of international agricultural law); Jeffrey Steinle, *The Problem Child of World Trade: Reform School for Agriculture*, 4 MINN. J. GLOBAL TRADE 333 (1995) (discussing the Uruguay Round Agreement on Agriculture).

34. See GATT, *supra* note 4, art. XX(b).

that the new WTO is an “all or nothing” proposition and that member nations must accept all of the agreements in their entirety, with little meaningful opportunity for national derogation.³⁵

In addition, WTO panel and appellate body reports are oddly restricted to the discourse of free trade principles. In this sense, the WTO is without equity; it is a set of legal rules without human context.³⁶ Disputes are settled according to one legal yardstick—namely, whether or not free trade principles have been breached through the operation of the national law being challenged. The discourse of the panel reports thus actually suppresses significant contextual issues surrounding the particular dispute.³⁷ Defendant nations are in effect precluded from arguing complex legislative motivations before the panels in an

35. Astonishingly, most academic commentators on the WTO praise the fact that, unlike its predecessor, the new WTO is an “all or nothing” proposition. Several extremely significant characteristics of the negotiation results should be noted. Perhaps foremost is the ‘single package’ idea, which the negotiators had embraced some years earlier and had resolved to make an important aspect of the negotiation. The idea was that there should be one complete elaborate text to which all those who wanted to become members of the new structure must adhere and accept. This would be in contrast to the Tokyo Round result which included specific individual agreements that were optional (“GATT a la carte”).

JOHN H. JACKSON, *THE WORLD TRADING SYSTEM: LAW AND POLICY OF INTERNATIONAL ECONOMIC RELATIONS* 47 (2d ed. 1998).

Given what was at stake for domestic political constituencies around the world, and in light of basic democratic theory, this is an extraordinary admission that the ultimate purpose of the WTO was, in effect, to remain isolated from even the indirect pressure that might have been exerted on the contents of the Uruguay Round by a system of weighted voting for adoption.

36. See Schneider, *supra* note 13 (discussing the school of thought that characterizes domestic political input as “special interest” influence and sees liberal/free trade rules as lofty and correct in direct proportion to their freedom from such influences). To articulate such a theory, however, is to beg the question, especially in the absence of an international referendum on its underlying premise.

37. See generally JOHN GRAY, *FALSE DAWN: THE DELUSIONS OF GLOBAL CAPITALISM* (1998)

Those who seek to design a free market on a worldwide scale have always insisted that the legal framework which defines and entrenches it must be placed beyond the reach of any democratic legislature. Sovereign states may sign up to membership of the World Trade Organisation; but it is that organisation, not the legislature of any sovereign state, which determines what is to count as free trade, and what a restraint of it. The rules of the game of the market must be elevated beyond any possibility of revision through democratic choice.

The role of a transnational organisation such as the WTO is to project free markets into the economic life of every society. It does so by trying to compel adherence to the rules which release free markets from the encumbered or embedded markets that exist in every society. Transna-

attempt to salvage their national regulations. Because of the “all or nothing” structure of the Uruguay Round acceptance procedure, member countries are presumed to have “agreed” to the entire content of the new agreements, and thus they have no legitimate defense based on extra-WTO considerations. “Inter-disciplinary” balancing of rights and interests, a commonplace judicial preoccupation in most jurisdictions, is virtually unknown at the WTO.

The startling power of WTO law over national regulation is most clearly in three important cases: The EC *Beef Hormones* case,³⁸ the *Indian Pharmaceuticals* case,³⁹ and the EC *Banana Regime* case.⁴⁰ In each dispute, important domestic values were reflected in the targeted legislation. The defending parties were essentially forced to remain silent about the underlying purposes behind the legislation, because justification for a domestic law’s existence would be irrelevant before the panel. GATT/WTO principles thus effectively trump other regulatory values, rendering countless important national laws legally precarious. Moreover, WTO member countries may be less willing to pass such protective legislation, fearing that the legislation could later face a WTO challenge.

tional organizations can get away with this only insofar as they are immune from the pressures of democratic political life.

Id. at 18.

In Gray’s terminology, “encumbered” or “embedded” markets are those tending towards social stability, as opposed to the profound instability of the “free” market. *Id.*

38. *EC—Measures Concerning Meat and Meat Products (Hormones)*, Complaint by the United States & Report of the Panel, WTO Doc. WT/DS26/R/USA (Aug. 18, 1997) <<http://wto.org/wto/dispute/distab.htm>> [hereinafter *Hormones Panel Report*]; *EC—Measures Concerning Meat and Meat Products (Hormones)*, Report of the Appellate Body, WTO Doc. WT/DS26/AB/R, WT/DS48/AB/R (Jan. 16, 1997) <<http://www.wto.org/wto/dispute/distab.htm>> [hereinafter *Hormones Appellate Report*].

39. *India—Patent Protection for Pharmaceutical and Agricultural Chemical Products*, Report of the Panel, WTO Doc. WT/DS50/R (Sept. 5, 1997) <<http://www.wto.org/wto/dispute/distab.htm>> [hereinafter *Patent Panel Report*]; *India—Patent Protection for Pharmaceutical and Agricultural Chemical Products*, Report of the Appellate Body, WTO Doc. WT/DS50/AB/R (Dec. 19, 1997) <<http://www.wto.org/wto/dispute/distab.htm>> [hereinafter *Patent Appellate Report*].

40. *European Communities—Regime for the Importation, Sale and Distribution of Bananas*, Complaint by Ecuador & Report of the Panel, WTO Doc. WT/DS27/R/ECU (May 22, 1997) <<http://www.wto.org/wto/dispute/distab.htm>> [hereinafter *Bananas Panel Report*]; *European Communities—Regime for the Importation, Sale and Distribution of Bananas*, Report of the Appellate Body, WTO Doc. WT/DS27/AB/R (Sept. 9, 1997) <<http://www.wto.org/wto/dispute/distab.htm>> [hereinafter *Bananas Appellate Report*].

1. *The Beef Hormones case*

In *Beef Hormones*, both the Panel and Appellate Body decisions held that the European Community ban on hormone-treated beef was unlawful under the Agreement on the Application of Sanitary and Phytosanitary Measures (SPS Agreement).⁴¹ The principal question in the case involved the degree of freedom a WTO member retains to institute a ban on food treated with a substance believed by the member to pose a health risk, when the relevant international organizations hold a different, less critical view or when there is no relevant international standard. The Panel found against the EC, declaring that an assessment of risk under the SPS Agreement must be "a scientific examination of data and factual studies; it is not a policy exercise involving social value judgments made by political bodies."⁴² The Panel then examined the scientific evidence, and concluded that the EC failed to present risk assessment techniques and scientific results that would permit the Panel to find the trade ban to be WTO-legal.⁴³

The EC raised many important issues on appeal, including the proper standard of review for WTO panels in such cases.⁴⁴ The EC challenged the Panel's lack of deference towards the EC's own conviction (even if derived from general studies of hor-

41. See Agreement on the Application of Sanitary and Phytosanitary Measures, Dec. 15, 1993, GATT Doc. MTN/FA II-AIA-4 [hereinafter SPS Agreement].

Briefly put, the SPS Agreement is aimed at national laws regulating food additives and contaminants as well as public health dangers posed by and to plants and animals. The obvious concern underlying the drafting of the SPS Agreement is that WTO members might use such measures as "protectionist" devices. There is, it must be noted, no corresponding requirement of minimum health or safety standards within the WTO. In essence, WTO members should base SPS measures on the findings of an enumerated list of international bodies; where the national standard is higher than these "recognized" standards, the members must show their standard to be based on scientific evidence, or on a demonstrable assessment of risk. Such a set of requirements has the effect of devaluing national sensitivities which may not be based on fact or risk assessment, but rather on deeply held beliefs not immediately susceptible to proof—such as a belief in the "limits to science," as argued by the EC in the *Beef Hormones* case. In addition, the requirements raise the overall cost of maintaining truly national regulation. See generally Layla Hughes, *Limiting the Jurisdiction of Dispute Settlement Panels: The WTO Appellate Body Beef Hormone Decision*, 10 GEO. INT'L ENVTL. L. REV. 915 (1998) (arguing that the SPS Agreement's requirement of scientific evidence lacks foundation in domestic and international law and fails to consider the multitude of reasons for the measures).

42. *Hormones Panel Report*, *supra* note 38, ¶ 8.94.

43. *Id.* ¶ 9.1.

44. *Hormones Appellate Report*, *supra* note 38, ¶ 16.

mones, rather than studies of hormones used specifically for growth promotion) that a total EC ban on the use of hormone growth promoters for domestic and imported beef was desirable.⁴⁵

The Appellate Body stated that while “[p]anel should recognize that members act from prudence and precaution where risks of irreversible damage to human health are concerned,” the precautionary principle does not by itself “and without a clear textual directive to that effect”⁴⁶ relieve the Panel from applying the normal principles of treaty interpretation.⁴⁷

The Appellate Body held the Panel to be in error where it had found that risk assessment under the Agreement could not include “matters not susceptible of quantitative analysis by . . . empirical laboratory methods.”⁴⁸ At the same time, the Appellate Body stated that the SPS Agreement requires “that the results of the risk assessment must sufficiently warrant—that is to say, reasonably support—the SPS measures at stake.”⁴⁹ Since the Appellate Body found that the EC did not offer enough studies to “rationally support” its prohibition, the Body upheld what it called the “ultimate conclusion” of the Panel.⁵⁰

While more intellectually sound than the Panel Report, the Appellate Body Report is problematic for proponents of precautionary public health regulations. While the Appellate Body may have soothed certain WTO critics by stating that it recognized the validity of the motivation behind the EC ban, it failed

45. *Id.* ¶ 15.

46. *Id.* ¶ 124.

47. *Id.* ¶ 165.

The Appellate Body denied that the international standards referred to in the SPS Agreement should be seen as having “obligatory force and effect,” even though such standards do enjoy a presumption of WTO-legality. Ominously though, while the Appellate Body upheld the “important right” of members to set their own individual standards, this right, the body continued, “is not an absolute or unqualified right.” *Id.* ¶ 173. The Appellate Body further stated: “The requirement of a risk assessment . . . as well as of ‘sufficient scientific evidence’ . . . are essential for the maintenance of the delicate and carefully negotiated balance in the SPS Agreement between the shared, but sometimes competing, interests of promoting international trade and of protecting the life and health of human beings.” *Id.* ¶ 177.

48. *Id.* ¶ 187.

49. *Id.* ¶ 193.

50. The Appellate Body explicitly refuted the Panel’s conclusion that the EC legislation was primarily motivated by a desire to exclude foreign beef; in stating that it accepted the contention that the main reason for the legislation was to protect human health, the Appellate Body seems to have left open the possibility of the EC providing more cogent evidence to support its ban. See *Hormones Appellate Report*, *supra* note 38, ¶¶ 238-244.

to acknowledge that the *raison d'être* for the SPS Agreement itself is in fact to prevent domestic regulation from acting as an impediment to trade. This underlying fact provides the rationale for subjecting members to this evidentiary burden regarding their own nationally-devised safety regulation.

Environmental regulation and trade principles inhabit two separate universes. No matter how sympathetic the Appellate Body may have been with the aims of the EC legislation, the SPS Agreement still has as its primary purpose not the maximum possible protection of public health, but a legal limitation on what constitutes valid national measures.

2. *The Indian Pharmaceuticals case*

The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Agreement) is quite properly named, because it deals primarily with the "trade related" aspects of intellectual property, addressing only tangentially social, economic, and developmental aspects.⁵¹ The TRIPS Agreement was not aimed at wealthy developed countries, because most of those countries already had credible regimes for the protection of intellectual property rights. Rather, the TRIPS Agreement was specifically aimed at the "newly industrialized countries" (NICs), which have the capacity to reproduce the industrial products of the developed world but lack the resources and the political will to pay for the privilege.⁵²

The TRIPS Agreement does not address its own effect on ordinary persons in NIC countries. The agreement will likely substantially increase the cost of essential goods. NICs are characterized by large segments of the population living in poverty, their condition somewhat ameliorated because intellectual property rights held by companies in the developed world have been ignored in industrial reproduction.⁵³

51. See Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1C, LEGAL INSTRUMENTS—RESULTS OF THE URUGUAY ROUND vol. 31, 11 I.L.M. 81 (1994) [hereinafter TRIPS Agreement].

52. A. Samule Oddi, *TRIPs - Natural Rights and a "Polite Form of Economic Imperialism,"* 29 VAND. J. TRANSNAT'L L. 415, 458 (1996).

53. See Martin Adelman & Sonia Baldia, *Prospects and Limits of the Patent Provision in the TRIPS Agreement: The Case of India*, 29 VAND. J. TRANSNAT'L L. 507 (1996) (arguing that Indian researchers, industry, and consumers will ultimately benefit when India extends patent protection to areas which had heretofore received no protection in that country). The authors concede that it will be necessary for the Indian government to subsidize the pharmaceutical needs of the poorest citizens when the system is implemented. *Id.* The authors

The TRIPS Agreement demands, however, that all WTO members bring their intellectual property protection up to an agreed international standard, in part by incorporating by reference the major international conventions on the subject.⁵⁴ The WTO has been more effective in establishing NIC protection for intellectual property rights than any uni-focus organization, including the World Intellectual Property Organization (WIPO), because it has the multi-dimensional ability to impose sanctions against non-complying countries in *other* areas of economic concern to them.⁵⁵

Although developed countries have only one year to bring their national laws into compliance, the TRIPS Agreement does allow developing countries five years and least developed countries ten years to comply. For developing countries now obliged to extend patent protection to areas not previously patentable under national laws, the transition could be extended to 2005 for those products. There are, however, significant and subtle subject matter limits to this leniency. Because of the importance placed on the sale of pharmaceutical products and agricultural inputs in the massive developing world markets, the Agreement states:

When a member does not make available as of the date of entry into force of the WTO Agreement patent protection for pharmaceutical and agricultural chemical products commensurate with its obligations under Article 27 (re patentable subject matter), that Member shall: (a) notwithstanding the provisions of Part VI (on transition periods for developing countries), provide as from the date of entry into force of the WTO Agreement a means by which applications for patents for such inventions can be filed; (b) apply to these applications, as of the date of application of this Agreement, the criteria for patentability as laid down in this Agreement as if those criteria were being applied on the date of filing in that Member, or, where priority is available and claimed, the priority date of the application; and (c) provide patent protection in accordance with this Agreement as from the grant of the pat-

do not make clear what should or will happen if the system is phased in, but without a system of pharmaceutical subsidy being created. *Id.*

54. For a general discussion, see Adrian Otten & Hannu Wager, *Compliance with TRIPS: The Emerging World View*, 29 VAND. J. TRANSNAT'L. L. 391 (1996). See also J.H. Reichman & David Lange, *Bargaining Around the TRIPS Agreement: The Case for Ongoing Public-Private Initiatives to Facilitate Worldwide Intellectual Property Transactions*, 9 DUKE J. COMP. & INT'L L. 11 (1998) (describing the special difficulties of developing countries in implementing TRIPs).

55. See TRIPS Agreement, *supra* note 51.

ent and for the remainder of the patent term, counted from the filing date.⁵⁶

The most sensitive and vital products, medicines and agricultural chemicals, are required to be included in this "mailbox" provision. These products are at the heart of the intellectual property debate, because they raise the issue of whether developing countries should be forced to pay for the intellectual property rights of products essential to the life and health of their poor citizens. Indeed, under existing Indian law (i.e., pre-TRIPS), patents for pharmaceutical products and agricultural chemicals were unlawful for these socio-economic reasons. When the price of essential medication rises in India, many people without the means to purchase it and without public health insurance will likely die. The developed world's system of subsidizing the cost of intellectual property rights through insurance and public health programs is often non-existent in NICs. Nevertheless, the NICs are bound by the new TRIPS rules.

The U.S. did not hesitate to challenge India's failure to create the mailbox system required by the TRIPS Agreement.⁵⁷ India's defense was largely technical; India did not attempt to argue that the Agreement imposes an unjust and unworkable obligation on its citizens. Rather, India hoped that the Panel would take a generous view of a developing country's rights to postpone compliance during the transition period.

Predictably, India failed to convince both the Panel and the Appellate Body. The Panel focused entirely on the rights of the prospective patent-holder under the TRIPS Agreement.⁵⁸ As in the *Beef Hormones* case, the Appellate Body reined in the

56. See *id.* art. 70(8). This article further states that where a product is the subject of a patent application in a Member state in accordance with paragraph 8(a), exclusive marketing rights shall be granted, notwithstanding the provisions of Part VI, for a period of five years after obtaining marketing approval in that Member or until a product patent is granted or rejected in that Member, whichever period is shorter, provided that, subsequent to the entry into force of the WTO Agreement, a patent application has been filed and a patent granted for that product in another Member and marketing approval obtained in such other Member. See *id.*

57. Appended to the Panel Report as "evidence" provided by the U.S. is a letter to the United States Trade Representative from a Senior Vice President of the Pharmaceutical Research and Manufacturers of America, in which he says: "As you know, PhRMA companies are experiencing great losses in India because of its failure to provide patent protection for pharmaceutical products. Unless India establishes a mechanism to ensure that mailbox applications can be filed and given legal status required by the TRIPS Agreement . . . they will continue to face enormous losses for decades to come." *Patent Panel Report*, *supra* note 39.

58. See generally *id.*

Panel's extraneous and expansive interpretation of the Agreement, but it nevertheless upheld the Panel's decision.⁵⁹

The real reasons for India's longstanding failure to allow patents in these areas were never even alluded to in the decisions nor apparently in the pleadings. Under the logic of the WTO, once the TRIPS Agreement had been agreed to and ratified, there was no further point in raising defenses that could only be meaningful in the absence of the Agreement itself. In other words, no amount of socio-economic evidence could help India's case. The discourse of social good and distributive justice thus disappears from the legal analysis, and WTO law triumphs over domestic law considerations. GATT/WTO law, while sometimes referred to as creating a "constitution," is in fact law entirely without constitutional context.

3. *The EC Banana Regime case*

Bananas were among the last products to be brought within the EC's Single Market program. How to organize the banana trade at the European level had long constituted an intractable problem with the European Commission, and its 1993 "solution" was a cumbersome compromise among sharply competing interests.⁶⁰

One set of interests was the African, Caribbean, and Pacific ("ACP") banana-producing countries, former colonies which remained bound to the European Member States through the Lome Convention.⁶¹ Some European states, notably France, Italy, and the UK, had created national banana quota systems which guaranteed a market to these former colonial territories.⁶² It is likely that ACP banana production would have disappeared had the European banana trade operated on purely "free market" principles, because the rival Latin American plantations reportedly could produce tastier bananas more cheaply.

Germany received a special "banana protocol" waiver from the EC in the 1950s, allowing it to import as many Latin American bananas on a duty-free basis as it wished.⁶³ Certain other EC states imported Latin American bananas at a standard rate

59. See generally *id.*

60. *Bananas Panel Report*, *supra* note 40, ¶ 3.4.

61. The Lome Convention is a trade and aid agreement dating back to the 1960s, when it was known as the Yaounde Convention. The current convention is Lome IV, ratified for a ten year period in 1990 by the EC and 70 ACP countries.

62. *Bananas Panel Report*, *supra* note 40, ¶ 3.5.

63. *Id.* ¶ 3.31.

of duty. Spain and Portugal heavily favored their own domestic producers, mainly based on territorial islands.⁶⁴

Although Germany fiercely contested the 1993 regime, the EC obtained legal clearance from the European Court of Justice to proceed with its new regulation governing the banana market.⁶⁵ The banana regime provided, through a licensing and tariff quota scheme, a certain proportion of the market to ACP banana producers, but on a Europe-wide basis.⁶⁶ The intention was to eliminate national Member State discrepancies in this area of trade and allow for limited expansion in imports of more efficiently produced Latin American bananas, while at the same time preventing the economic devastation of former colonies in ACP countries.

A number of Latin American producers, along with the United States, brought a massive and legally complex challenge to the EC regime.⁶⁷ The case involved issues of EC external sovereignty, historical affiliations, and international development policy, as well as the wishes of the EC Member States with regard to international economic alliances and, of course, the traditional interests of traders in bananas from particular sources. Yet even such weighty considerations could not stand up to the letter of WTO law.⁶⁸ Again, there was little room to argue the motivation for the regime. The EC could only contend that WTO law did not reach this far and that the EC had acted within its rights as a WTO member in establishing the EC-wide banana regime.⁶⁹

One of the many challenges raised by the U.S. against the EC regime was based on Articles II (Most Favored Nation) and XVII (National Treatment) of the GATS Agreement.⁷⁰ Europe

64. *Id.* ¶ 3.5.

65. Case C-280/93, Federal Republic of Germany v. Council of the European Union, 1994 ECR I-4973.

66. *Bananas Panel Report*, *supra* note 40, ¶ 3.6.

67. See *European Communities—Regime for the Importation, Sale and Distribution of Bananas*, First Submission of the United States of America, 1995 WL 397092 ¶¶ 7, 11 (July 9, 1996).

68. See generally Inger Österdahl, *Bananas and Treaty-Making Powers: Current Issues in the External Trade Law of the European Union*, 6 MINN. J. GLOBAL TRADE 473 (1997) (describing the impugned banana regime from a European legal perspective). See also Zsolt K. Bessko, *Going Bananas Over EEC Preferences? A Look at the Banana Trade War and the WTO's Understanding on Rules and Procedures Governing the Settlement of Disputes*, 28 CASE W. RES. J. INT'L. L. 265 (1996) (describing the legal basis for the banana dispute at WTO level).

69. *Bananas Panel Report*, *supra* note 40, ¶¶ 4.15-4.31.

70. *Id.* ¶¶ 4.600-7.39.

appeared not to have imagined that the terms of the GATS Agreement would be used in such an expansionary manner by the U.S. The EC insisted that the GATS Agreement is intended "to regulate trade in services as such and that it covers the supply of services as products in their own right."⁷¹ Further, the EC argued that "GATS is not concerned with the indirect effects of measures relating to trade in goods on the supply of services."⁷²

The EC *Banana Regime* case makes clear that the U.S. was prepared to comb the GATS Agreement for possible causes of action. The response of the Panel and the Appellate Body confirmed that GATS was a potent new weapon not limited to the concept of trade in services *qua* services, but instead was capable of being expanded to cover issues of non-discrimination against the *service providers* behind ordinary trade in goods.⁷³ After the *Banana Regime* case, the term "services" has been interpreted to include the service of providing tradeable goods. This creates the potential for a separate and much more probing level of inquiry grafted onto a first stage inquiry concerning free trade in goods. That second inquiry raises the question of the rights and interests of individuals who are dealing in the goods—i.e. "services."⁷⁴

In the *Banana Regime* case, the EC explicitly committed itself to free trade in "wholesale trade services" under GATS, leaving itself open to the Banana Panel's conclusion that it had failed to live up to its GATS obligations.⁷⁵ The EC's surprise at the Panel's expansionary treatment of its GATS commitments was apparently unfeigned. The Banana Panel wrote: "The scope of the GATS encompasses any measure of a Member to the extent it affects the supply of a service regardless of whether such measure directly governs the supply of a service or whether it

71. *Id.* ¶ 7.277.

72. *Id.*

73. *See id.* ¶¶ 73-86.

74. It is hardly surprising that U.S. trade policy makers would have seen an opportunity under GATS to attack the Japanese Large Scale Retail Stores Law with arguments relating to the rights of service providers. This is not to suggest that the U.S. would have been guaranteed a victory on this point. But it is of great significance that the Japanese believed that such an approach by the U.S. could succeed, with grave consequences for retaining any regulatory control in the retail sector. There is, it should be pointed out, an after-the-fact school of thought to the effect that Japan voluntarily conceded the loss of the Large Scale Retail Stores Law in order to hand the U.S. an easy victory. Regardless, it is clear that the Japanese could not have looked forward to a WTO panel examining their retail store regulation in the light of the GATS Agreement.

75. *Id.* ¶ 79.

regulates other matters but nevertheless affects trade in services."⁷⁶

If the EC expected any substantive reversal by the Appellate Body, they were again disappointed. The Appellate Body addressed the GATS issue by stating: "Whether a certain measure affecting the supply of a service related to a particular good is scrutinized under the GATT 1994 or the GATS, or both, is a matter that can only be determined on a case-by case basis."⁷⁷ The Appellate Body continued: "For these reasons, we agree with the Panel that the EC banana import licensing procedures are subject to both the GATT 1994 and the GATS, and that the GATT 1994 and the GATS may overlap in application to a particular measure."⁷⁸ The Appellate Body further supported the Panel's conclusions: "If Article II of the GATS (MFN) was not applicable to *de facto* discrimination, it would not be difficult—and indeed it would be a good deal easier in the case of trade in services than in trade in goods—to devise discriminatory measures aimed at circumventing the basic purpose of that Article."⁷⁹

Two things are clear in the wake of the EC Banana Regime case: first, the GATS Agreement has nearly unlimited potential to invalidate national regulations; second, a WTO member country must consider the prospect of a GATS challenge in evaluating its own domestic socio-economic law-making.

B. TREATY RATIFICATION V. THE SOVEREIGN POWER AND POLITICAL DUTY TO LEGISLATE

There is no clear reason for giving precedence to WTO trade principles over other complex sectors of law, sectors representing political compromises worked out through a process of incremental recognition by legislators of diverse and often competing socio-economic interests.

Mere ratification of the WTO Agreements is not sufficient justification to disregard these political compromises. Unlike other treaties, the WTO Agreement and related Uruguay Round Agreements are not static commitments, but ongoing, open-ended abdications of legislative power. Because of the disparate subject matter appearing in various WTO disputes, academic writers have largely failed to identify the conceptual thread which unites them. Yet, in each case discussed *supra*, the de-

76. *Id.* ¶ 7.285.

77. *Id.* ¶ 221.

78. *Id.* ¶ 222.

79. *Id.* ¶ 233.

feudant WTO member received a legal surprise as the WTO set out to abolish some aspect of the national regulatory regime.

It is in this context that the *Fuji-Kodak* case must be examined, with an awareness of one major distinguishing feature. In the *Fuji-Kodak* case, the most significant events involving MITI and the Large Scale Retail Stores Law took place and were settled by the parties before the panel process. Japan's willingness to settle before a GATS issue was raised can only be understood in light of the WTO's ability not only to invalidate national regulations in the abstract, but also to enforce that invalidation through a very direct power of authorizing proportional retaliation.

III. FUJI-KODAK, THE WTO COMPLAINT: WHAT WAS LEFT OF THE CASE THAT CAME BEFORE THE PANEL?

The *Fuji-Kodak* case has generally been viewed as a rather weak and premature attempt by the United States to bring competition law within the scope of the WTO.⁸⁰ In addition, the ill-considered emphasis by the United States on the GATT legal concept of "non-violation nullification or impairment," as found in Article XXIII(1)(b) has been widely discussed.⁸¹ The U.S. likely decided to feature the "non-violation" strategy because of the novelty of its arguments concerning Japan's alleged support for restrictive distribution industry arrangements and Japan's

80. See, e.g., Renee Hardt, *Kodak v Fuji: A Test Case for the Extraterritorial Application of the Sherman Act*, 15 B.U. INT'L L.J. 309 (1997) (discussing the antitrust implications). While Kodak could have considered legal action on competition law grounds against Fuji in the U.S. courts, it decided on a more "diplomatic" route through a Section 301 complaint to the USTR. See *id.* at 312.

While recognizing that the U.S. is to some degree conflicted as to whether it wishes to see global competition rules established through the WTO, most Japanese commentators seemed to believe that the U.S. had strategically introduced premature competition law arguments in the *Fuji-Kodak* case to suggest that market-access related competition matters should be on the WTO agenda. For a comparative discussion of U.S.-EC attitudes in this regard, see Eleanor M. Fox, *Toward World Antitrust and Market Access*, 91 AM. J. INT'L L. 1 (1997) (offering a compromise proposal for bringing competition matters into the WTO system). See also Rosenthal, *supra* note 10, at 543 (providing a summary of perspectives on how competition law principles might be brought into the WTO, and on dealing with cases such as *Fuji-Kodak*, where the market access complaint involves a mix of public and private conduct).

81. See Sung-joon Cho, *GATT Non-Violation Issues in the WTO Framework: Are They the Achilles' Heel of the Dispute Settlement Process?* 39 HARV. INT'L L.J. 311, 332 (1998).

alleged failure to enforce its own domestic competition law in a fair and impartial manner.

As a preliminary matter, it is important to analyze the actual contents of the Panel Report in the case—a decision so completely dismissive of U.S. arguments that readers may assume that the U.S. came away from the dispute with nothing. The U.S. prevailed, however, in that Japan agreed to overhaul its Large Scale Retail Stores Law. The knock-on effects of the case (occurring outside the litigation itself) are all the more dramatic when one considers the overall tentativeness of the issues raised before the Panel.

Though the line between corporate and governmental interests are increasingly blurred in the GATT/WTO legal system, a complainant party must find offending official governmental behavior. It is not sufficient to bring a complaint over private conduct; there must be a showing that a national government has engaged in conduct damaging to the trade interests of the complainant.⁸² The U.S. focused in *Fuji-Kodak* on three basic categories of Japanese government “measures”: (1) a set of official guidelines and reports, dating back to the 1960s and 1970s, which purportedly show the Japanese government attempting to instruct Japanese manufacturers how to exclude foreign competition through manipulating the internal product distribution system;⁸³ (2) restrictions on large retail stores (as noted previously, there had been an alternative and far more powerful argument in a parallel action that the Large Scale Retail Stores Law was in violation of the GATS Agreement);⁸⁴ and (3) so-called “Promotion Countermeasures,” or competition rules that

82. See *Fuji-Kodak Panel Report*, *supra* note 1, ¶¶ 6.87-6.132 and 10.28-10.60.

83. —1967 Cabinet Decision;
 —1967 (JFTC) Notification 17 on premiums to businesses;
 —1968 Sixth Interim Report on Distribution Modernization Outlook and Issues;
 —1969 Seventh Interim Report on Systemization of Distribution Activities;
 —1969 Survey Report regarding Transaction Terms;
 —1970 Guidelines for Rationalizing Terms of Trade for Photographic Film;
 —1971 Basic Plan for the Systemization of Distribution;
 —1975 Manual for Systemization of Distribution by Industry: Camera and Film

Id. ¶ 10.93.

84. —1974 Large Stores Law
 —1979 Amendments to Large Stores Law

Id. ¶ 10.23.

acted to hamper foreign companies in their marketing campaigns in Japan.⁸⁵

The Panel Report set out the main U.S. position.⁸⁶ The United States alleged that these “measures,” individually and collectively, nullified or impaired benefits accruing to the United States within the meaning of GATT Article XXIII:1(b), the “non-violation” provision.⁸⁷ It also alleged that the distribution measures were inconsistent with Article III:4 of GATT.⁸⁸ Finally, the U.S. alleged that unpublished enforcement actions by the Japan Fair Trade Commission (JFTC) under the Premiums Law and fair competition codes, combined with the unpublished guidance through which the Japanese authorities require applicants for large stores to coordinate their plans with local competitors before submitting a notification for government review, were inconsistent with GATT Article X(1).⁸⁹

THE NON-VIOLATION CLAIM

The Panel first addressed the comparatively obscure non-violation nullification or impairment claim by the U.S.⁹⁰ It

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- 85. —1967 JFTC Notification 17 on Premiums to Businesses;
 - 1967 Cabinet Decision on Liberalization of Inward Direct Investment;
 - 1977 JFTC Notification 5 on Premiums to Consumers;
 - 1981 JFTC Guidance on Dispatched Employees.
 - 1982 Self-Regulating Rules Concerning Fairness in Trade with Business;
 - 1982 Establishment of Fair Trade Promotion Council;
 - 1984 Self-Regulating Standards Concerning Display of Processing Fees for Colour Negative Film;
 - 1987 JFTC approval of the Retailers Fair Competition Code and its enforcement body, the Retailers Fair Trade Council

Id. ¶ 10.23.

86. *Id.* ¶ 10.24.

87. *Id.*

88. *Id.*

89. *Id.*

90. *Id.* ¶ 10.33.

The Panel cited as authority for its approach to the non-violation standard the *EEC-Oilseeds* case of 1986. It quoted that case as follows:

The idea underlying [the provisions of Article XXIII:1(b)] is that the improved competitive opportunities that can legitimately be expected from a tariff concession can be frustrated not only by measures proscribed by the General Agreement but also by measures consistent with that Agreement. In order to encourage contracting parties to make tariff concessions they must therefore be given a right of redress when a reciprocal concession is impaired by another contracting party as a result of the application of any measure, whether or not it conflicts with the General Agreement.

Id.

pointed out that although the non-violation provision had been “on the books” for almost 50 years, there had only been eight instances of panels considering the question of a non-violation nullification or impairment of benefit.⁹¹ With this in mind, the Panel stated that this remedy “should be approached with caution and treated as an exceptional concept.” This is for the obvious reason that “members negotiate the rules that they agree to follow and only exceptionally would expect to be challenged for actions not in contravention of those rules.”⁹²

It may be that the concept of “non-violation nullification or impairment of benefit” was best suited to GATT’s diplomatic roots in the 1940’s and 1950’s, rather than today’s more complex WTO law. During that fragile early period, GATT was only part law and primarily diplomacy.⁹³ There was an understanding that countries should be induced to continue negotiating within the GATT system. If GATT had been seen in the early days to create clear winners and losers, the likelihood of broad, ongoing international participation might have been reduced. The non-violation remedy has thus become conceptually obsolete, as evidenced by its infrequent use.⁹⁴

91. See *Fuji-Kodak Panel Report*, *supra* note 1, ¶ 10.36. These are: *Australian Subsidy on Ammonium Sulphate*, GATT B.I.S.D. (vol. II) at 188 (1952); *Treatment by Germany of Imports of Sardines*, GATT B.I.S.D. (1st Supp.) at 30 (1953); *Uruguayan Recourse*, GATT B.I.S.D. (11th Supp.) at 95; *EC—Tariff Treatment on Imports of Citrus Products From Certain Countries in the Mediterranean Region*, GATT Doc. L/5576; *EEC—Production Aids Granted on Canned Fruit*, GATT Doc. L/5778; *Japan—Semi-conductors*, GATT B.I.S.D. (35th Supp.) at 116; *EEC—Oilseeds*, GATT B.I.S.D. (37th Supp.) at 86; *US—Agricultural Waiver*, GATT B.I.S.D. (37th Supp.) at 228.

92. See *Fuji-Kodak Panel Report*, *supra* note 1, ¶ 10.36.

93. See generally Arie Reich, *From Diplomacy to Law: The Juridicization of International Trade Relations*, 17 J. INT’L L. & BUS. 775 (1996) (discussing the movement from the diplomacy of GATT’s early years to the current law-based regime).

94. “In GATT jurisprudence, most of the cases of non-violation nullification or impairment have dealt with situations where a GATT-consistent domestic subsidy for the producer has been introduced or modified following the grant of a tariff concession on that product.” *Fuji-Kodak Panel Report*, *supra* note 1, ¶ 10.38. The Panel went on to say:

we wish to make clear that we do not *a priori* consider it inappropriate to apply the Article XXIII:1(b) remedy to other governmental actions, such as those designed to strengthen the competitiveness of certain distribution or industrial sectors through non-financial assistance. . . . In the context of a Member’s distribution system, . . . it is conceivable that measures that do not infringe GATT rules could be implemented in a manner that effectively results in a disproportionate impact on market conditions for imported products.

Id.

The *Fuji-Kodak* Panel made clear that there are limits to the scope of non-violation claims. It stated that "tariff concessions have never been viewed as creating a guarantee of trade volumes, but rather . . . as creating expectations as to competitive relationships."⁹⁵ The Panel thus began with a note of caution: the U.S. could not guarantee market access levels through the novel approach of a non-violation claim relating to government measures of a type not normally challenged in this type of action.⁹⁶

From the Japanese point of view, the Panel's interpretation of the term "measure" was of crucial significance. The U.S. maintained that it had identified relevant government actions, even though these could only be described as informal and hortatory. The GATT system had encountered this question before.⁹⁷

The issue of the legal status of Japanese administrative guidance, when it arose with reference to Article XI of GATT, was resolved in general terms in the *Japan-Semiconductor* case.⁹⁸ The *Fuji-Kodak* Panel cited that case to the following effect: "Where administrative guidance creates incentives or disincentives largely dependent upon governmental action for private parties to act in a particular manner, it may be considered a governmental measure." The *Fuji-Kodak* Panel appropriated this statement from the *Semiconductor* case, holding that certain non-mandatory measures taken by governments could operate in a manner equivalent to mandatory requirements, where the difference between them "was only one of form and not of substance."

For purposes of its Article XXIII:1(b) analysis, however, the *Fuji-Kodak* Panel took a broader view of what constitutes a government measure.⁹⁹ The Panel apparently believed that the

95. *Id.*

96. *Id.*

97. The Panel continued:

The ordinary meaning of measure as it is used in Article XXIII:1(b) certainly encompasses a law or regulation enacted by a government. But in our view, it is broader than that and includes other governmental activities short of legally enforceable enactments. At the same time, it is also true that not every utterance by a government official or study prepared by a non-governmental body at the request of the government or with some degree of government support can be viewed as a measure of a Member government.

Id. ¶ 10.44.

98. See *Japan—Semi-conductors*, *supra* note 91, at 154-55.

99. The Panel went on:

objectives of Article XXIII:1(b)—namely, to preserve the balance of GATT concessions by giving redress for government action not otherwise regulated by GATT rules—required such an expansive reading of “measure.” The Panel was quick to caution that the U.S. would bear a considerable burden of proof in establishing that the administrative guidance of which it complained continued to exist and, assuming it did, that it was in fact responsible for the nullification or impairment of benefit raised in the complaint.¹⁰⁰

Had the U.S. succeeded in the non-violation argument, it is possible that Japan would not have been required as part of the remedy to alter the measures that gave rise to the complaint, although compensation for the complainant would have been necessary.¹⁰¹ Thus U.S. reliance on non-violation nullification or impairment is ironic in the context of the Large Scale Retail Stores Law, because Japan had already conceded the point.

1. *Non-Violation and Japan’s Distribution Measures* (“Countermeasures”)

The Panel examined the specific Japanese government measures raised by the U.S. and determined that “The U.S. case against distribution ‘measures’ may best be understood in the context of the general theme advanced by the United States to the effect there exists in Japan a unique relationship between government and industry.” The U.S. maintained that Japan re-

In our view, a government policy or action need not necessarily have a substantially binding or compulsory nature for it to entail a likelihood of compliance by private actors in a way so as to nullify or impair legitimately expected benefits within the purview of Article XXIII(1)(b). Indeed, it is clear that non-binding actions, which include sufficient incentives or disincentives for private parties to act in a particular manner, can potentially have adverse effects on competitive conditions of market access. . . . In cases where . . . there is substantial reliance on administrative guidance and other more informal forms of government-business cooperation, . . . even non-binding, hortatory wording in a government statement of policy could have a similar effect on private actors to a legally binding measure or what Japan refers to as regulatory administrative guidance.

Fuji-Kodak Panel Report, supra note 1, ¶ 10.49.

100. As to the nature of the benefits which are alleged to have been nullified or impaired, the Panel turned to the seminal *Australian Subsidy* case. *See Australian Subsidy, supra* note 91, at 188. This case established that non-violation nullification or impairment of benefit occurs if the action in question upsets the competitive relationship between the two countries and could not have been reasonably anticipated by the complaining party, given all the circumstances and the terms of the General Agreement, at the time the tariff concession was negotiated. *Id.*

101. *See Fuji-Kodak Panel Report, supra* note 1, ¶¶ 6.39-6.42.

lied to an unusually high degree on various forms of semi-governmental entities, including study groups and committees, which in turn constituted a version of peer pressure on industry.

The U.S. contended that in the face of increased international competition in the 1960s and 1970s, resulting from the general lowering of tariffs and other common forms of market protection, Japan worked stealthily to adjust the domestic distribution system in order to enhance the future market share of national producers.¹⁰² The Japanese government and major domestic manufacturers allegedly colluded to pressure the distribution sector: either Japanese wholesalers and retailers would deal in domestic goods or they would pay a long-term economic price.

Since the U.S. narrative was an economic conspiracy tale and the character of the government measures complained of were so amorphous, the U.S. was forced to make the difficult case that it was the invisible as much as the visible behavior of the Japanese government which should be examined by the Panel. This in turn led the Japanese to argue that the U.S. was merely playing on prejudice concerning Japan's supposedly "unique" commercial culture. Japan alleged that the US was attempting to substitute pre-conceived ideas about Japan for solid proof of Japanese government behavior which might have led to the loss of an expected GATT benefit.¹⁰³

The U.S. may have been motivated to highlight competition law issues as a way of demonstrating that competition law rules should be included in the WTO. The U.S. raised these issues knowing that questions of competition law were premature for the WTO. In this sense, the non-violation setting was convenient for the floating of an argument which would have been unlikely to succeed in the violation context. Since there is no

102. The Panel stated:

The United States argues that when the liberalization of international trading conditions became imminent, MITI and Japanese industry recognized the superiority of foreign firms which could create serious competition for Japanese manufacturers and their products. MITI and Japanese manufacturers, it is argued, consequently devised a plan to streamline Japan's distribution system in order to bring it under the control of domestic producers. The basic US position is that MITI sought to strengthen vertical distribution channels that would handle the products of a particular domestic manufacturer exclusively.

Id. ¶ 10.92.

103. See *Japan—Measures Affecting Consumer Photographic Film and Paper*, First Submission of the Government of Japan, *supra* note 20, at 6.

GATT/WTO competition law as such, it was unlikely that there would be a violation found on a competition-based complaint.¹⁰⁴

The Panel first confronted the U.S. complaint regarding "Distribution Measures," those measures that correspond to alleged Japanese government policy responses in the face of imminent competition from foreign firms within the Japanese market in the 1960s and 1970s. Japan termed its general program a "modernization" of its distribution sector. However, according to the U.S., Japan was engaged in an effort to substitute one form of protection for another less overt form.¹⁰⁵

The Panel meticulously analyzed each "measure" and in each case failed to find the necessary legal link between the policy or guidance articulated by the Japanese government and the loss of benefit complained of by the U.S. The Panel obviously placed a high legal priority on requiring the U.S. to establish an indisputable connection between the government measure and the impairment of benefit because it was not dealing with a violation of GATT. The U.S. did not meet the relevant standard of proof with respect to the measures it had identified.

The U.S. attempted to create an impression that it had unearthed a large amount of damning material. It attempted to substantiate this impression with official reports and guidelines for the improvement of domestic industry, which the U.S. claimed contained a subtext of intentional exclusion of outsiders from domestic markets. The U.S. appeared to be offended by the Japanese government's conscious economic planning, an approach which is anathema to *laissez faire* capitalism. It is

104. It is possible that an argument relating to a field of law not yet included as subject matter in the GATT/WTO could succeed in establishing a GATT Article III violation. One example of this would be the dispute raised by the U.S. against Canada in the *FIRA* case, in which parts of a Canadian law to screen foreign direct investment was found to violate Article III, even though there is no specific mention of investment as a separate subject matter within GATT itself. See *Canada—Administration of the Foreign Investment Review Act*, Feb. 7, 1984, GATT B.I.S.D. (30th Supp.) at 140 (1984).

105. See Frank Schweitzer, *Flash of the Titans: A Picture of Section 301 in the Dispute Between Kodak and Fuji and a View Toward Dismantling Anti-competitive Practices in the Japanese Distribution System*, 11 AM. U.J. INT'L L. & POL'Y 847, 864-65 (1996). Schweitzer writes:

While Kodak alleges a host of violations and unlawful practices, the essence of Kodak's petition focuses on the alleged exclusionary film market in Japan, which Fuji has fashioned by way of its distribution system. . . . Kodak alleges the foundation of Fuji's market structure is four primary wholesalers (tokuyakuten) who distribute a single brand while colluding with Fuji to perpetuate an exclusionary structure on lower levels of the sales chain, all the way down to the retail level.

Id.

doubtful whether advising one's domestic industries to think strategically is a nullification of one's trading partners' benefits. The U.S. tried to read disingenuousness into MITI's assertions of the need to "meet the challenges" of increased international competition. The Panel, however, concluded that the U.S. did not establish its non-violation case with regard to distribution measures.¹⁰⁶

2. *Non-Violation and the Large Scale Retail Stores Law*

The Panel then turned to the issue of the Large Scale Retail Stores Law¹⁰⁷ and the United States' non-violation nullification or impairment claim. The US disliked the Japanese retail store

106. The Panel wrote:

The essence of the U.S. claim in respect of distribution "countermeasures" is that Japan created vertical integration and single-brand distribution in the Japanese film and paper market. In the U.S. view, this was done through standardization of transaction terms, systemization and limitations on premiums to businesses. As we have found above, the United States has not been able to show that the various "measures" it cites have upset competitive relationships between domestic and U.S. film and paper in Japan, principally because single-brand distribution appears to have occurred before and independently of those "measures," but also because the United States has not demonstrated that these "measures" are directed at promoting vertical integration or single-brand distribution. . . . Equally, the United States has not explained why the vertically integrated, single-brand distribution structure of the film sector in Japan—a state of affairs that the evidence suggests is similar to that occurring elsewhere in the world (including in the United States)—would have broken down in the absence of continuing government intervention.

Fuji-Kodak Panel Report, supra note 1, ¶ 10.204. See also William Barringer, Competition Policy and Cross Border Dispute Resolution: Lessons Learned from the U.S.-Japan Film Dispute, 6 Geo. Mason L. Rev. 459, 466-67 (1998) (comparing the distribution systems for film in both the U.S. and Japan); Jonathan Gowdy, Exposing Kodak: A Critique of the Toleration of Anticompetitive Practice Provision of Section 301 of the Trade Act of 1974, 47 FLA. L. REV. 459 (1995) (criticizing the inconsistencies in the Kodak position).

107. The Large Scale Retail Stores Law was passed by the Japanese Diet on October 1, 1973, with an effective date of March 1, 1974. The law established notification procedures to regulate the opening of large store structures (where more than one retailer may operate) and the opening and operation of retail stores operating in such structures. As originally enacted, the law regulated stores with floor space in excess of 1500 square meters. The 1979 amendment effected two main changes: (1) the threshold for stores covered by the law was lowered from 1500 square meters to 500 square meters; and (2) large stores were divided into two classes—Class I stores (1500 square meters and above) under MITI's jurisdiction, and Class II stores (500 to 1500 square meters) under the jurisdiction of local prefectural governors. The law permits the regulation of a store's size, opening date, operating hours, and closing days ("store holidays"). See generally Upham, *supra* note 16 (discussing in detail the Large Scale Retail Stores Law). The Panel confirmed,

size regulation quite apart from the Kodak complaint, and this case provided an opportunity to bring the issue to the WTO.

The U.S. argued that even after the Japanese government set about to reorganize domestic wholesale operations in the photographic materials sector, large retail stores remained what the U.S. called "one potentially significant alternative distribution channel in Japan for foreign film manufacturers." There was nothing special about film as a product; larger stores would simply be more likely to carry foreign products, and U.S. film is one of those products. The U.S. theory was that larger stores were "less susceptible to pressure by domestic manufacturers." The U.S. went so far as to assert that "if such stores were permitted to proliferate across Japan, . . . wholesalers would become less significant and foreign manufacturers could circumvent the bottle-necked distribution system." Indeed, the U.S. argued, it was the prospect of that very threat that first led to the enactment of the Large Scale Retail Stores Law.¹⁰⁸

Even in this truncated version (i.e., minus the GATS arguments) of the U.S. attack on the Large Scale Retail Stores Law, the fundamental contrast between U.S. and Japanese interpretation of the law is readily apparent. Japan contended that the Large Scale Retail Stores Law "reflects long-standing Japanese policy, dating back to the enactment of the Department Store Law in 1956, of regulating large stores to preserve a diversity of small, medium and large retailing competitors, a policy found in other countries as well." Japan further argued that "the law does not concern products generally, or film in particular. The law does not regulate which products large retailers can carry, nor does it take into account which products a retailer sells when determining whether and what adjustments are neces-

Article 3 of the law requires that a party intending to build or open a large-scale retail store must submit, to MITI or the appropriate prefecture, an initial notification including the proposed floor area and planned opening date at least 12 months before the planned opening date. If the store is deemed to be subject to the law's procedures, the plans for the store must be explained to the appropriate authority, local retailers and consumers. Following this, the authority may recommend a reduction in the size of the store and/or a delay in the opening date and/or a change in its opening hours and store holidays. In 1982, MITI instituted, through Directive No. 36, a "prior explanation" requirement to precede the initial notification required by Article 3. This directive was revoked in 1992. Also in 1992, the minimum floor space requirement for Class I stores was raised from 1500 square meters to 3000 square meters (and to 6000 square meters in cities designated by ordinance).

Fuji-Kodak Panel Report, *supra* note 1, ¶¶ 10.210-10.211.

108. See *id.* ¶ 10.212.

sary." Japan asked the Panel to conclude from this that "the Large Stores Law is incapable of adversely modifying competitive conditions for any imported products, including film," and that there is "no correlation between store size and the likelihood of carrying foreign film brands."¹⁰⁹

Given the extreme limitations on discourse in a WTO action, it was appropriate for Japan to argue that the U.S. could not prove cause and effect between the Large Scale Retail Stores Law and U.S. market access. In light of the retail law's legislative history, it would have been gratuitous for Japan to argue that the law represented valuable socio-economic policy and that *therefore* the Panel should accept it. As indicated with respect to other WTO disputes, there is no mechanism for invoking reasons of social need or cultural preference in defending a nation's legal regime against a WTO challenge, except in extremely limited circumstances as defined by the terms of GATT/WTO law itself. Social need and cultural preference have no independent power to influence the outcome of a WTO dispute.

In the context of the non-violation complaint, Japan's long-standing legislative policy of protecting small retailers might help determine whether the United States could have reasonably anticipated that Japan would pass successive measures for the protection of small retailers.¹¹⁰ The Japanese also described the policy behind the law to discredit speculative U.S. arguments as to the law's supposedly discriminatory purpose, the alleged effects of which the U.S. was unable to prove by credible evidence.

The difficult problem for the U.S., in light of the "product-neutral" characteristics of the Large Scale Retail Stores Law, was to demonstrate precisely how the law nullified or impaired an anticipated GATT/WTO benefit. Japan strongly denied that

109. *Id.* ¶ 10.213.

110. The Panel stated:

In analyzing the issue of reasonable anticipation at the conclusion of the Kennedy Round, we take note of Japan's argument that Japanese policy of regulating the mix of larger and smaller stores dates back to the Department Store Law of 1956 and that, therefore, the United States should have anticipated that such a policy would continue and would evolve to take account of changes in store types.

Id. ¶ 10.217.

However, the Panel rejected the idea that a general policy implies knowledge of future, more specific manifestations of that policy in the form of new legislative acts. The Panel then analyzed at length precisely which amendments the U.S. should be deemed to have had knowledge of, in light of the tariff concessions received by the U.S. from Japan on photographic materials at the relevant point in time. *Id.* ¶ 10.221.

the law was capable of altering, even indirectly, the competitive conditions between domestic and imported products—a crucial element necessary to prove non-violation nullification or impairment.

The Panel mentioned its awareness that the rationale behind the legislation was to protect smaller retailers and agreed with Japan that neither the law on its face nor its implementation bore any relation to product origin. “It is possible, however,” the Panel asserted, “that a measure that is formally neutral as to the origin of products may be shown to be applied in a manner that results in upsetting the competitive relationship between domestic and imported products to the detriment of imports.”¹¹¹ The U.S. argued that large stores were more likely to carry imported film, and the Japanese responded that the U.S. data showed only that high-volume sellers were more likely to carry imported film, regardless of store size.

The Panel expressed its “unease” with the U.S. logic here,¹¹² commenting that if the U.S. argument is accepted, then any regulation on a store more likely to carry a foreign product may give rise to a claim under Article XXIII:1(b).¹¹³ The Panel noted that the European Court of Justice faced similar arguments with regard to Sunday trading laws and rejected them.¹¹⁴

The Panel was also concerned that the U.S. argument was based on the concept of legitimate expectations of *evolving* market access—as if Japan should be expected to allow an ongoing increase in large stores, which would in turn facilitate U.S. access to the Japanese film market. But the Panel pointed out that “normally, for competitive relationships to be upset, we would expect an adverse change in the situation existing at the time of the tariff concessions. In the case of subsidies, for example, a Member reasonably expects that subsidies will not be increased, not that they will be decreased.”¹¹⁵

The United States failed to provide the Panel with sufficient evidence of nullification or impairment of expected benefit. Since the Panel focused on impairment of the complainant’s benefit, and not on any violation of GATT/WTO law, it placed a particularly heavy burden on the complainant to establish the

111. *Id.* ¶ 10.226.

112. *Id.* ¶ 10.227.

113. *Id.*

114. *Id.* The Panel cited to the following European cases: *Torfaen Borough Council v. B & Q Plc* [1990] 3CMLR31; *Keck & Mithouard* [1993] ECR I-6097; *Punta Casa SpA v Sindaco del Comune di Capena* [1994] ECR I-2355.

115. *Fuji-Kodak Panel Report*, *supra* note 1, ¶ 10.232.

factual validity of its expectations. In addition, it insisted that the causal link be firmly established between the non-violative behavior of the defending country and the loss of benefit by the complainant.

3. *Non-Violation and Japan's Promotion Measures*

The final line of argument put forth by the U.S. under the non-violation nullification or impairment of benefit arm of its complaint concerned "Promotion Measures," measures dealing with the regulation of economic inducements and aggressive advertising. The U.S. argued that even with the disadvantage it suffered from access problems in the distribution system, its marketing techniques could have compensated for the disadvantage, but they were consistently prohibited from doing so by official measures designed to prevent foreign firms from displaying their competitive advantage in this area.

The U.S. complained that its ability to "use certain discounts, gifts, coupons, and other inducements, or to rely upon innovative advertising campaigns, particularly where price comparisons are discussed," had been severely constrained. These measures had been implemented through the Premiums Law and also issued as regulations by the Japan Fair Trade Commission (JFTC) through its authority under the Anti-Monopoly Act. The U.S. conceded that this framework applied equally to domestic and foreign firms but insisted that "Japan has imposed them with the intention of striking against international competition by foreign imports following trade liberalization, i.e., the ability of foreign manufacturers to convert their strong capitalization and cost competitiveness into potent marketing strategies and aggressive promotional competition."¹¹⁶

Japan set out cogent, WTO-neutral reasons for its laws and demonstrated that the regulations in question fell with exact equality on foreign and domestic manufacturing companies. Japan rebutted the U.S. claim with the argument that the Premiums Law was "designed to deal effectively with unfair trade practices and encourage manufacturers to compete principally on the basis of price and quality, not unfair inducements or deceptive and misleading representations." Ordinary price and promotional competition was not hindered. There was no limit on advertising spending if deceptive statements were not made.

116. *Id.* ¶ 10.235.

Lotteries and prize giveaways were controlled to protect the consumer in a manner found in most other countries.

The U.S. identified a large number of "measures," many of them guidance documents published by the JFTC, that were of a similar semi-formal nature to those described in the distribution industries context. Included in the complaint were codes designed for self-regulation by the retail industry in relation to promotional premiums and approved by the JFTC. As before, in each instance the U.S. failed to convince the Panel that any GATT/WTO benefit had been nullified or impaired. The Panel refused to accept overbroad arguments, such as that the measures created a "chilling effect," as a substitute for the clear demonstration of a loss of anticipated benefit.

Finally, the U.S. attempted to construct a doctrine of "combined effects," claiming that the distribution countermeasures, the Large Scale Retail Stores Law, and the promotion countermeasures, when taken together, nullified or impaired benefits within the meaning of Article XXIII(1)(b). The U.S. argued that the distribution measures work together "as an organic whole."¹¹⁷

The Panel noted that it was theoretically possible for such an argument to be valid; however, the U.S. would still have had to find specific instances to support this novel approach. The U.S., the Panel stated, would have to "provide this Panel with a detailed showing of how these alleged 'measures' interact with one another in their implementation so as to cause effects different from, and additional to, those effects which are alleged to be caused by each 'measure' acting individually."¹¹⁸ The United States' appeal to a general sentiment reflected in Japanese business practices failed to resonate with the Panel.

The Panel remained firm in its adherence to the terms of the GATT/WTO rules. Of its own role, the Panel stated: "In the

117. *Id.* ¶ 10.351. The Panel continued:

The United States claims that MITI expected government and industry to work together to set targets for industrial restructuring, and for businesses to make efforts to achieve these targets, supported by government fiscal and other incentives. According to the United States, leading scholars in Japan agree that one way that administrative guidance is made effective is by a continuing process of studying, surveying, cajoling, and targeting the use of fiscal incentives that keeps the private sector focused on the goals set by the government, assesses their achievement of those goals, and builds peer pressure on those who are falling behind on their achievement.

Id.

118. *Id.* ¶ 10.353.

final analysis, it is not incumbent upon this Panel to engage in its own extensive, unaided investigation into the potential applicability in this case of the U.S. theory of combined effects. Rather, it is for the United States, as the complaining party, to make a detailed showing of the relevance of this theory to the matter at hand. We consider that the United States has failed to make such a showing here.”¹¹⁹ The U.S. appeared to be relying on an unprovable belief that Japanese commercial and cultural structures were inherently exclusionary and impenetrable.¹²⁰ The WTO Panel, a radically literal-minded judicial body, could hardly be expected to accept this as a legal doctrine.¹²¹

4. Reflections on the Outcome of the Dispute

The U.S. invested enormous resources in pursuit of this complaint, and yet the U.S. arguments were legally unconvincing. It must be asked why the U.S. did not appeal the panel decision. What was the full nature of the “understanding” between the U.S. and Japan which led the U.S. to drop the GATS arm as it related to the Large Scale Retail Stores Law and led

119. *Id.* ¶ 10.367.

120. See *Japan—Measures Affecting Consumer Photographic Film and Paper*, Rebuttal Submission of the Government of Japan, *supra* note 20, at 65. The rebuttal document stated:

Consider the implausibility of the U.S. claims of conscious Japanese subterfuge of GATT legal norms. The United States repeatedly implies that Japan was consciously trying to hide the true effect of its policies, and thus trying to fool others into believing Japan was complying with its GATT obligations. This claim is baseless; everything being done was published and widely publicized. . . . In reality, the U.S. case relies on a claim about protectionist intent. The U.S. selectively quotes from various documents to show the alleged protectionist intent. It is no accident that the U.S. statement to the panel focused on this alleged intent, with its section, “Why Japan Imposed these Measures,” and did not focus on the challenged government actions and policies themselves. . . . The U.S. relies so heavily on this legally dubious approach because it has little else to say. This panel could simply follow the guidance of earlier panels that wisely decided to ignore ambiguous, subjective, and indeterminate claims about government intent, and instead focus on clear, objective, determinative terms of specific government actions. . . . Of course, the Government of Japan was aware of the challenges being imposed by capital liberalization. The U.S., however, improperly takes every acknowledgement of this concern and spins a tale of conspiracies to block imports.

Id.

121. As for the “GATT-violation” arguments put forward to challenge the Japanese measures, the U.S. fared just as poorly. On each successive issue, the Panel was brief and to the point: the U.S. failed to show GATT-illegal behavior on Japan’s part. See generally *Fuji-Kodak Panel Report*, *supra* note 1, ¶¶ 10.368-10.401.

Japan to agree to abolish that law? Is it proper that the WTO panel process should be used in this way, as a vehicle of international pressure, to achieve diplomatic aims which the complainant party has been unable to achieve in more conventional ways? A WTO action is especially problematic when the subject matter of the underlying dispute and that of the "concession"—in this case, to abolish the Large Scale Retail Stores Law—are only tenuously linked.

The Japanese bureaucracy has warmly embraced the new post-1995 WTO structures, including the more legalistic dispute resolution procedures, because the advent of the WTO has in its view relieved Japan of intense bilateral pressures from the U.S. and Europe.¹²² The new WTO purports to render certain extra-GATT/WTO bilateral agreements unlawful. For example, Voluntary Export Restraints (VERs) have been outlawed under the new Safeguards Agreement.¹²³ This appears to have given Japan some confidence that the free-floating accusations, cultural and otherwise, common to the Structural Impediments Initiative period will disappear. It is significant that Japan hotly resisted the U.S. attempt to rely on commercial stereotypes and prejudice in its framing of the *Fuji-Kodak* complaint.

Despite the new "legalism" and the attempt to prevent countries from resorting to bilateral agreements under pressure *outside* the WTO, there is a danger that the enhanced power of WTO law will itself become a source of diplomatic intimidation. The awkward combination of the basic Kodak market access complaint and the Large Scale Retail Stores Law issue raises the question of whether Japan was induced to capitulate on a longstanding trade matter which should have been resolved in a more conventional setting, such as in long-term trade discussions.

IV. THE INCALCULABLE POWER OF GATS: WHAT HAPPENED WHEN THE U.S. INCLUDED, THEN DISCARDED, THE GATS ARM OF *FUJI-KODAK*

The WTO system has no mechanism for entertaining the significance to a domestic constituency of a national law protect-

122. See generally MICHIKO IKEDA, *GATTO KARA WTO E: BOEKI MASATSU NO GENDAISHI* (1996) (providing a historical exposition of Japanese psychological relief at the end of bilateral trade pressures and the creation of a more legalistic, rules-based WTO).

123. Agreement on Safeguards, GATT Doc. MTN/FA II-AIA-14 (Dec. 15, 1993), art. 11(1)(b).

ing it. The degree to which non-GATT/WTO or "equitable" considerations can be taken into account by a reviewing panel is set within the relevant WTO Agreement. In essence, a WTO panel is limited to considering member country arguments regarding whether the challenged national law does or does not violate some GATT/WTO principle or rule.

From the WTO's perspective, the defendant national jurisdiction must decide how it will defend its domestic legal regime during the panel and Appellate Body procedures under the terms of the relevant GATT/WTO agreement and then, if necessary, change that regime in accordance with WTO *diktat*. The consequences of invalidating the national law are not of any apparent concern to the WTO.

GATT/WTO law and domestic regulation, including protective laws for the environment, labor, and small businesses, derive from fundamentally different sources and sets of political considerations. In the case of Japan's Large Scale Retail Stores Law, the domestic constituency for protecting small and medium retailers lost out to an alliance of multinational, mainly U.S.-based mega-retailers who exerted external pressure, with the assistance of a few very large Japanese retailers. These large retailers would likely never have succeeded in undoing the Large Scale Retail Stores Law in the absence of the external pressure.

As indicated *supra*, there reportedly was not a single politician in Japan who initially favored abolishing the Large Scale Retail Stores Law. MITI bureaucrats were required to negotiate intensively over a long period to convince politicians to support a change in the law which would have the effect of hastening the decline and even disappearance of the small retailer in Japan. MITI relied on the argument that eliminating the law would raise Japan's international profile as a country willing to liberalize its internal economy, even at the expense of a politically strong yet economically vulnerable constituency. More ominously, MITI contended that if the U.S. persisted and prevailed with its GATS argument, Japan's international reputation for maintaining an open domestic market would suffer.

Japan's Large Scale Retail Stores Law was passed to protect Japan's vulnerable small retail sector from domination and defeat by the much larger and more powerful chain stores.¹²⁴ It is highly significant that Japan, as a member country being

124. For a concise discussion of this legislative intent issue, see NAMIKATA, *supra* note 22, at 20-22. Namikata is interested in the paradigm shift repre-

threatened with a WTO challenge, was induced to drop its national policy of protecting a segment of its own society. This shift is the logical extension of post-1995 GATT/WTO law under which the domestic democratic process itself becomes "illegal."¹²⁵

Most academic articles on WTO law end with a discussion of what occurs in the WTO-level litigation itself. International trade law scholars must examine the empirical effects of WTO law within actual jurisdictions, such as what will likely happen to the traditional retailing sector in Japan post-*Fuji-Kodak*.

It is inadequately understood outside Japan that economic policy encompasses social and cultural policy.¹²⁶ Japanese economic policy is more than a simple reflection of a cultural ethos; rather, economic policy for Japan in the modern period has enabled it to prosper without sacrificing cultural bonds. While the Japanese bureaucracy appears to feel liberated from bilateral pressure in the new WTO era, its pre-WTO socio-economic compact and its highly selective internationalization and modernization may fall as a result of the WTO's more stringent rules and far more absolutist dispute settlement system.

It is frequently pointed out that by the time Japan promised to abolish the Large Scale Retail Stores Law in 1997, the law had virtually ceased to be stringently applied in any case.¹²⁷ Because of relentless U.S. pressure during the Structural Impediments Initiative phase as well as policy confusion in Japan, the law was frequently ignored.¹²⁸ What is striking about the effect

sented by the abolition of the old Large Scale Retail Stores Law and the creation of three substitute laws with different—more acceptable—stated "intents."

125. See Rajesh Swaminathan, *Regulating Development: Structural Adjustment and the Case for National Enforcement of Economic and Social Rights*, 37 COLUM. J. TRANSNAT'L L. 161, 186-89 (1998) (making the point that national governments are more responsive to the demands of the IMF and World Bank than to their own domestic constituencies). See generally John Gray, *supra* note 37 (exploring the destabilizing effects of modern international trade rules).

126. Interview with MITI official, in Tokyo, Japan (July 15, 1998).

127. See NAMIKATA, *supra* note 22, at 21; Kenji Higuchi, *Kisei Kanwa to Daikibo Kouritenpoho no Ronri*, CHUSHO KOKO GEPPU, Dec. 1997, at 28-33. Higuchi explains that from the time of the early Structural Impediments Initiative talks, Japan began to relax its application of the Large Scale Retail Stores Law. *Id.*

128. Namikata makes clear that during the Structural Impediments Initiative, the U.S. wanted nothing short of abolition of the Large Scale Retail Stores Law. NAMIKATA, *supra* note 22, at 22-23. The U.S. logic was that one of the methods of reducing the U.S. trade deficit with Japan was to allow for stores big and powerful enough to carry U.S. goods, and to build new shopping centers that would serve to enhance consumer demand. See *id.*

of the GATS arm of the *Fuji-Kodak* case is that it appears to have pushed Japan to take a firm decision on abolishing its Large Scale Retail Stores Law. Under U.S. and European pressure, Japan had for years been discussing plans to end protection for certain vulnerable domestic sectors, including small retailers, yet it also avoided taking decisive action which would constitute abrupt abandonment of those sectors. Before the *Fuji-Kodak* case, the political fate of the small- and medium-scale retail sector was highly uncertain. The possibility of a high-profile WTO challenge to Japan's retail regulatory system provided the final impetus for the Japanese bureaucracy to bring an end to that uncertainty.¹²⁹

A. MITI'S TASK IN ABOLISHING THE LARGE SCALE RETAIL STORES LAW

MITI was in the unenviable position of having to abolish the Large Scale Retail Stores Law to comply with its commitment to the U.S.; create a substitute law which would resemble retail-regulating laws in other industrialized countries in order to insulate the new law from further WTO actions; and, finally, man-

129. There is obviously a difference of opinion whether the Large Scale Retail Stores Law has continued to have much effect, especially in the mid-nineties. A Japan Economic Institute of America Report states that

[a]lthough procedural changes set in motion by the July 1990 Structural Impediments Initiative agreement have expedited government action on retailers' plans to build stores with sales areas of 500 square meters (5,400 square feet) or more and given stores considerable leeway on operational issues, . . . major retailers are still forced almost as often as not to revise their expansion plans because of opposition from smaller counterparts. In FY 1996, for instance, the Ministry of International Trade and Industry's Large Scale Retail Stores Council reportedly ordered alterations in 44.7 percent of the 2,416 applications filed to open new outlets. The changes included cuts, frequently drastic, in the proposed sizes of the buildings, earlier closing hours and more non-business days.

Susan MacKnight, *Japan to Replace Large Retail Store Law*, Japan Economic Institute of America Report, Mar. 20, 1998.

In short, while legal academics and others involved in the cause of small and medium retailers would say that the law had failed miserably to protect the sector, and while more neutral commentators would say that not even the Large Scale Retail Stores Law could save this sector against market forces, the U.S. maintained throughout that the law acted as a draconian restriction on the development of the large scale retail sector in Japan. It is unclear to what extent the U.S. position was influenced by the wish to see more large scale Japanese retail outlets capable of selling more foreign product—or, by contrast, to what degree the U.S. was hoping for a retail “big bang” which would see U.S. retailers (such as Wal-mart or OfficeMax) enter Japan for the purpose of bypassing the existing distribution system altogether, thereby selling more U.S. goods. The difference in emphasis is worth exploring.

age to pacify the small and medium scale retailers with the content of the new law without excessively aggravating trade friction with the U.S. MITI accomplished all of this with extraordinary political skill. While the U.S. would have preferred a completely free market approach, it was apparent that the new set of laws would not be nearly as effective at blocking the introduction of large-scale retail outlets. The constituency most likely to resist these legislative changes, the small and medium retailers, was unclear about the likely effectiveness of the new laws and therefore was reduced to a wait-and-see attitude. The third pillar of the new set of laws, that which appropriates funds for the regeneration of traditional town centers, was intended as a sweetener.

B. THE "THREE PILLARS" OF THE NEW RETAIL STORE LAWS

The three new laws that will replace the Large Scale Retail Stores Law in the year 2000 might appear to resemble the old law in spirit. Both systems are outwardly based upon procedurally loose consultation and adjustment-oriented instruments. The principal difference between the two systems is that under the old law MITI could order compliance if a prospective retailer did not follow the official guidelines.¹³⁰ While the new laws also

130. While smaller retailers were unwilling to see this potent (albeit very sporadically applied) legal device abandoned, even the most ardent defender of small shops in the traditional town center (the *shotengai*) believed that the law was not working as originally intended. Japan had developed, courtesy of MITI, an internally contradictory attitude towards the protection of the endangered smaller retail sector. See Upham, *supra* note 16, at 404. Upham explains under "The History and Structure of the LSRSL" that the original roots of the law go back to the 1930s. He writes that the law protected small and medium stores against excessive competition from bigger stores, but also helped to guarantee the territorial shares of department stores by restricting new entrants. Upham states:

Passage of the LSRSL can best be explained as a political compromise among department stores, small and medium retailers, and super-stores, but official MITI commentaries on the LSRSL invariably cited strengthened consumer protection and industry rationalization as statutory goals. Besides guaranteeing small merchants an "enterprise opportunity," Articles 1 and 11 of the LSRSL specifically require due consideration to the interests of consumers and to the well-being of the retail industry as a whole. . . . While these goals were potentially contradictory, legal commentators contemplated the bureaucratic creation of a set of criteria that would balance these varied interests on a case by case approach.

Id. at 406.

Under the Large Scale Retail Stores Law, when a store was being planned, the developer was required to notify its plan to MITI at least 12 months before the planned opening. A public briefing was also required to be held, with infor-

involve public consultation followed by official suggestions or recommendations, MITI cannot order a retailer to comply.¹³¹ A

mation on the plan to be presented to the relevant local government, the chamber of commerce, the local association of small and medium retailers, and consumers resident in the area. The MITI Minister would then ask the Large Scale Retail Store Council to review the evidence and assess the case, taking into account the opinions of all interested parties. The Council would then present its opinion to the MITI Minister. Local governors were also entitled to express their view on the proposed store.

Upham writes: "A [MITI] recommendation had no legal force and a retailer could violate its terms without incurring legal liability or being subject to MITI sanctions. If a retailer did violate the terms of a recommendation, however, MITI had the power to issue a *meirei*, or order, which was compulsory." *Id.* at 407.

The crucial element was that the MITI Minister (or the prefectural governor, in the case of Type II large stores), based on all these local inputs, would issue a series of recommendations to the prospective store developer. The Minister might suggest, for example, that the store size be reduced (and mandatory reductions were often very significant) or the hours of opening altered. While the official recommendation on its own was not legally binding, the store developer was nevertheless not free, as he or she will be under the new regime, to ignore it.

131. The new laws involve public consultation without the same *commercial* consultation, followed by official suggestions emanating from the local government level without a decision-making role for national government authorities. The three new laws which are to replace the Large Scale Retail Stores Law are as follows: The Large Scale Retail Stores Location Law, or *Daiten Ritchi Ho* (an essentially environmental assessment law); the Revised Town Planning Law, or *Kaisei Toshi Keikaku Ho* (an amendment to existing town planning law, to allow for zoning by local government of certain areas so as to limit these to small and medium shops); and the Town Center Revitalization Law, or *Chushin Shigaichi Kasseika Ho* (an urban renewal law, creating funds and tax incentives for the regeneration of traditional town centers). For a full description of each of the new laws, see NAMIKATA, *supra* note 22, chs. 3-5.

The most significant of these laws is the first, since it contains the central process by which any proposed large-scale retail outlet will be reviewed. The structural weaknesses of the Large Scale Retail Stores Location Law would indicate an inevitable lowering of the future standard of protection provided for the small and medium retail sector, a sector that has acted as one of the mainstays of Japanese socio-cultural traditions.

Commentators also point out that it has historically been the responsibility of small shopkeepers in the *shotengai* to plan and direct local festivals, or *omatsuri*, events which are essential to the continuation of traditional culture. It must also be borne in mind that in the latter years of the Large Scale Retail Stores Law, where "non-implementation" or quasi-implementation had been the norm, a certain momentum in favor of mega-retailing had been generated. Especially in some Japanese provincial towns and cities, the traditional *shotengai* is not so much under threat as nearly extinct. As is the case in the United States, the mega-retailers of Japan (both domestic and foreign) are essentially creating alternative towns out-of-town. See Takayoshi Igarashi, *Kogai Ten Kara Machi wo Mamoru*, YAMAGATA SHINBUN, May 26, 1998. Professor Igarashi writes that not only do the new mega-retailers stock traditional food, clothing, and household goods, but increasingly have also added cinemas, bow-

local government can oppose the new store, but in the absence of zoning or other clear factors militating against its construction, the store developer can proceed and ignore official guidance. The process is also now more expeditious.¹³²

From the U.S. point of view, its timely pressure on Japan in the highly public forum of the WTO caused Japan to capitulate and to agree effectively to eliminate the Large Scale Retail Stores Law.¹³³ Neither supporters nor detractors of the old law are now satisfied because of the ambiguous nature of the substitute laws and the unpredictability concerning the stringency with which they will be applied after 2000. While outwardly honoring its commitment to the U.S. to repeal the Large Scale Retail Stores Law, MITI had adroitly fashioned the new three-part Japanese law on established European regulatory models.¹³⁴ While pleased at the repeal of the Large Scale Retail Stores Law, the USTR is already expressing public skepticism concerning Japan's motives in devising the new legal regime.¹³⁵

ling, and other sports facilities—virtually creating a city within itself. *Id.* Against such pressures, he concludes, the traditional *shotengai* cannot begin to compete. *Id.*

132. The former regime could take up to eight years before a store would be allowed to proceed. The new system is firmly time bound, with the expectation that store developers will receive final word within a year of lodging the application.

133. Interview with U.S. Embassy official, in Tokyo, Japan (June 15, 1998).

134. See *Large Scale Retail Store Law Today*, MITI, May 1997. MITI is at pains to compare the regime in Japan with those in five European countries, the U.S., and Korea. *Id.*

135. Note the tone of impatience in the USTR:

Along with repealing the Large Stores Law, the Japanese Government enacted a new Large Scale Retail Stores Location Law, . . . which eliminates the use of supply/demand adjustment mechanisms. The new law gives local governments authority over the establishment and expansion of large stores. The new regime will require local governments to apply transparent criteria that are limited to environmental factors (e.g., traffic and noise) set out in guidelines issued by the central government.

The U.S. Government has expressed strong concerns to the Japanese Government regarding the new Large Stores Location Law, in particular with regard to allowing interested parties to review and comment on the draft guidelines, the need for close monitoring by the central government of implementation of the new law by local governments, and the need to facilitate the resolution of complaints from retailers seeking the establishment or expansion of a large store.

The U.S. Government also is very concerned that local governments will use new zoning authority granted to them by recent amendments of the City Planning Law to block large retail stores. The amended City Planning Law allows local governments to create new types of "special-use zones," such as "small-to-medium-sized retail

MITI emphasises the fact that the new laws are made up of elements that are common to the "retail regimes" in other developed countries. This selectivity was probably to protect the substitute regime from any future WTO action by the U.S., since the U.S. would hardly attack a regime comparable to those found in Europe.

The MITI-led legal changes go beyond a *pro forma* shift of emphasis from protecting an organized, traditional political constituency to safeguarding the environment and quality of life for residents and consumers. The new laws are unlikely to hinder large retail developments, as the USTR speculated. MITI consciously drafted the laws in a manner that enables the individual large retailer to choose whether or not to comply with official recommendations. MITI is aware of this weakness in its new legal regime and is concerned that it will become a source of domestic political criticism.¹³⁶

The new legal regime is in fact more generous towards large retailers than similar regimes in most European countries, where definitive permit systems and clear lines of enforcement tend to prevail. It must be asked why the Japanese government went *beyond* the degree of liberalization necessary to bring its retail regime in line with those in certain EU countries. A system which allows the relevant authority either to reject on policy grounds or impose strict, enforceable conditions is now, for all practical purposes, dead in Japan.

It is important to understand the general political context in which these changes have occurred. Japan is experiencing a strong movement towards "decentralization" (*bunken*) and a move away from the old-style clientalist politics. Ironically, this has served to make the new retail regime appear more benign than it otherwise might have. The three new laws replacing the Large Scale Retail Stores Law may appear to be part of a larger

store zones," which could be restricted to small and medium sized retailers.

The U.S. Government strongly urges the Japanese Government to ensure that local governments do not use the new measures to create an environment for large stores that is similar to (or worse than) that arising under the current Large Stores Law, to impose unreasonable restrictions on large retail stores, or to favor small and medium-sized retail stores over large stores. The U.S. Government will continue to monitor this issue closely.

USTR, *supra* note 3, at 2.

136. Interviews with MITI officials, in Toyko, Japan (June-July 1998).

trend, one driven by the popular democratic/decentralization sentiment currently prevalent in Japan.¹³⁷

C. FOCUS ON THE POLITICAL DISCOURSE OF "PILLAR ONE" OF THE NEW LEGAL REGIME: THE LARGE SCALE RETAIL STORES LOCATION LAW (*DAITEN RITCHI HO*)

The purpose of the new Large Scale Retail Stores Location Law is not in any overt sense to oppose the creation of mega-shopping malls. Rather, in accepting the "necessity" for these stores, it attempts to find a way to prevent the deterioration of the surrounding environment.¹³⁸ Under the new procedure, the proposed large store owner will issue a public notice of his intent to develop any store larger than 1,000 square meters. Within a strict time limit, potential environmental problems will be identified and the interested public and local government authorities will be permitted to comment. The owner/developer of the proposed store will respond to these comments by announcing measures to address the problems and issues raised. Ultimately, the local government authority will make a recommendation, either positive or negative.

A stunning weakness in the system is that the recommendation is not binding and it cannot be backed up with an official order to comply. In the absence of a zoning prohibition or some other bar, the store owner/developer may ignore the recommendation and proceed, even in the event of a very negative assessment by the local government authority. MITI does not view this as a serious weakness, since no businessperson in Japan would ignore the recommendation of such a body with impunity.

137. See Sukehiro Hosono, *Tenpo Chosei, Shichoson Reberu De*, NIHON KEIZAI SHINBUN, Jan. 20, 1998. While recognizing problems and weaknesses in the new legal regime, Professor Hosono describes the old Large Scale Retail Stores Law as a relative failure. He agrees that the legislative changes are in line with the general shift towards decentralization of government and with administrative reform, and sees the new legal regime as reflecting a change from "economic constraints" to "social constraints," in that consumer behavior will play a more decisive role.

138. See Takayoshi Igarashi, *Toshi Wa Doko Ni Yuku No Ka? ZOKEI*, No. 15, June 1998, 22-30. Contrast this evaluation of the new law with Professor Upham's description of the old Large Scale Retail Stores Law, *supra* note 130, where he points out that the LRSRL was also a compromise among competing retail interests, and not meant to prevent all large store developments. The major difference between the old and the new regimes, however, is that the old LRSRL, insofar as it involved a slow and cumbersome process of review—often lasting years—and included a binding order of compliance with conditions, had far greater power to keep out certain types of mega-retail development indefinitely.

MITI overlooks the fact that foreign retailers would not feel particularly restricted by social pressures from the local business community or local residents. It is in fact highly likely that only a multinational retailer, without any significant ties to the locality or indeed to Japan, *would be* in a position to ignore a negative recommendation with such impunity. Ironically, MITI is invoking a concept of informal social and peer pressure that is virtually irrelevant for the largest international retail operators.¹³⁹

The new "environmental" discourse of retailing, as found in the Large Scale Retail Stores Location Law, taps into emerging trends of political thought in Japan mentioned *supra*, especially decentralization (*bunken*), consumer power, and the end of clientalist politics. As so often happens during times of political reform, popular dissatisfaction with the immediate political past is being exploited by major business interests in a sleight-of-hand that is quite invisible to the public at large.¹⁴⁰ Interest-

139. The two laws related to the main Large Scale Retail Store Location Law have been treated with skepticism by Japanese commentators. See *supra* notes 129-30 and accompanying text. One allows special zoning to exclude large stores, and the other deals with incentives to revitalize traditional town centers. See NAMIKATA, *supra* note 22, chs. 4 & 5.

Critics dismiss the town planning law amendment on several grounds: first, because it relies on zoning, which is quite weak in Japan compared to other developed countries; second, because it only encompasses a very small part of Japan's total land; and third, because it lacks the added weight of a complementary national land use directive on the subject of large stores. See Igarashi, *supra* note 131, at 24. Its effectiveness will also depend upon the vigilance of local governments, which in turn depends upon the ability of local politicians to resist the temptation to compete for scarce commercial activity in the form of new mega-malls. The urban renewal incentive scheme, like all such schemes, will depend upon the level of consistent funding provided. *Id.* at 24-25. It is difficult to imagine how such a scheme will form the basis for smaller town center shops to compete with out-of-town shopping centers; experience in the United States and some parts of Europe indicates that urban renewal schemes cannot halt the decline of older shopping areas confronted with the lure of malls. For a vivid description of this process at work in the United States, see JAMES KUNSTLER, *THE GEOGRAPHY OF NOWHERE: THE RISE AND DECLINE OF AMERICA'S MAN-MADE LANDSCAPE* (1994). Instead, it is highly likely that the network of "mom and pop" stores in traditional town centers in Japan will be replaced by niche shops that do not purport to serve general needs, especially after business hours.

140. See NAMIKATA, *supra* note 22, at 24. Namikata declares that the change from the old law to the new represents a shift in Japan from extreme protectionism of the small and medium business sector to an emphasis on markets and *seikatsusha*—a concept that encompasses both consumers and people generally, as they make their way in the world. The new law, he explains, is not an instrument of protection, but rather one to ensure that the environment is not destroyed by the advent of mega-retailing. Namikata states that this, in

ingly, just as WTO law lacks any articulation of "equity" and remains a hermetically sealed set of principles operating in isolation from non-market considerations, so too the discourse surrounding the abolition of the Large Scale Retail Stores Law and the creation of the Large Scale Retail Stores Location Law fails to reflect the inevitable loss of social and cultural cohesion that the dying away of *shotengai* will certainly bring in its wake.

Under cover of *bunken*, the highly popular slogan indicating a movement toward decentralization and a limited devolution of government power onto local governments throughout Japan, MITI has assisted the central government in abdicating its role as protector of the small business sector. The national government could have retained in the legislation a set of land use guidelines creating a strong presumption against larger out-of-town retailing. It is unclear whether MITI believed that such an addition to the law would have been indefensible in WTO terms. The new law could be described as fatalistic and accepting of the drastic impending changes in the retail sector. The more startling implications of the new regime are sugar-coated with references to environmental adjustments, the quality of life of residents and consumers, and urban regeneration.¹⁴¹

It is also unclear what is meant by the often-invoked "world standard" when it comes to retail-related law.¹⁴² MITI undoubtedly studied European and American retail development law in an attempt to create a WTO-proof regime. However, it is common in Europe to have an environmentally-focused retail law which provides either local or national authorities the power to refuse permission to the out-of-town developer or owner. In the wake of disastrous planning in the 1980s, the UK has recently gone so far as effectively to ban large out-of-town shopping de-

turn, emphasizes the needs of *seikatsusha*. This sort of discussion is now common in Japan, as younger intellectuals blur the distinction between Japan's internal need for a loosening of the reins of power held by the old guard of politicians and the desire of multinational corporations and the larger Japanese corporations to exploit this sentiment in favor of economic liberalization and open markets.

141. See Deborah Weitsman, *Mega-malls Becoming Major Players in Japan*, JAPAN ECON. NEWSWIRE, Aug. 6, 1997, at 1. Weitsman reports: "We're transferring the U.S. system (of malls) to Japan," said Kunihiro Ueta, president of MGS Japan Co., a Japan-U.S. joint venture that plans to build 15 megamalls in this country [Japan] within 10 years. Up until now, megamall developers say, they have faced many visible and invisible barriers unique to the Japanese market." *Id.* It would seem that these developers have no doubt about what the impending changes to the law actually mean.

142. See Kenji Higuchi, *Sekai ni Okureru Ogata Tenpo Kisei*, NIKKEI RYUTSU SHINBUN, July 28, 1998.

velopments. Since the UK planning guidelines come from the central government, local authorities essentially have no power to grant permission for such developments.¹⁴³

On its own terms, the new Large Scale Retail Stores Location Law has little legal coherence. The principal areas of concern permitted to be taken into account under the new regime are traffic congestion, parking issues, noise, and waste. There is no mention in the law of the need to protect existing businesses, the traditional shopping cores of towns, the landscape, or other "cultural" features of the locality.¹⁴⁴ All socio-economically "protective" language was avoided. The new law is unlikely on its own to assist the preservation of town centers in any meaningful way.¹⁴⁵ For an "environmental" law of this type to serve complex and multiple purposes, the definition of "environment" must be broad. Here, it is narrow, but despite this commentators and advocates insist that its purpose is to protect the entire "environment" and quality of life in which residents and consumers live, work, and shop.

V. FUJI-KODAK IN ITS PROPER CONTEXT

The *Fuji-Kodak* case is an example of the struggle between domestic political constituencies, who were accustomed over years of democratic development to think that they had a right to influence the content of national legislation, and global pressures to "streamline" domestic legal regimes in order to facilitate the free flow of goods, capital, and supposed consumer choice. The *Fuji-Kodak* case, while apparently part of a particular trade history involving the U.S. and Japan, is in fact one of a series of WTO cases wherein important domestic regulations have been eliminated by the application of free trade principles.

143. See STUART BELL, *BELL AND BALL ON ENVIRONMENTAL LAW* 225 (4th ed. 1997).

144. It is, of course, possible to accommodate a broad notion of environment in a legal instrument. Note the concept of environment used in the EC's environmental impact assessment directive, which includes cultural heritage as part of the environment. See Council Directive 85/337 on the Assessment of the Effects of Certain Public and Private Projects on the Environment.

145. It should be noted that even this level of retained control was resented in some quarters in the U.S. diplomatic community. One official in the U.S. Embassy in Tokyo indicated to the author that the Japanese were using the environment as a "pretext" for the continued protection of the smaller retail sector when, in this official's view, what Japanese consumers really wanted was to get in the car on weekends and drive to an American-style suburban megamall. Interview with U.S. Embassy official, in Tokyo, Japan (June 8, 1998).

It remains to be asked whether domestic constituencies understand the degree to which they have become sidelined in the WTO process. Since there is no natural political forum in which this essential questioning can occur, it is perhaps left to international trade law scholars to look beyond the technicalities of the subject and analyze the full implications for vulnerable groups of the harsh application of post-1995 international trade law. What happens to the valid non-GATT, non-WTO reasons for a domestic regulation when it is invalidated by the WTO system? Do these reasons disappear, even though the constituencies that brought them into being have not yet disappeared, and would under normal circumstances (in the absence of WTO pressures) survive at the domestic political level?

Now that the GATT/WTO system has begun functioning in the manner of a genuine legal system,¹⁴⁶ it must be subjected to a normal level of scrutiny by legal scholars. Similarly, political representatives must be held accountable for changes in domestic legal regimes which emanate from the WTO. Anything less would indicate that the WTO system has taken on legislative powers in the absence of democratic justification or accountability.

Mere ratification is not sufficient justification for this multifaceted legal changeover, which goes to the heart of democratic theories of government. If an international treaty such as the WTO sets up an autonomous, unpredictable, and open-ended system of alternative law, then it can no longer be classified with other, more limited and "static" treaties. Neither can a field of law be isolated from other, competing areas of law, or from general social consequences. Equity demands that fact and circumstance color our understanding of the letter of the law and that all law be applied according to a sense of due process and proportion. The very fact that GATT/WTO law is an isolated set of principles set up according to a theory of social good which has not in itself been ratified by voters world-wide means that panel law is simplistic and thus fails as law.

GATT/WTO law implicitly declares its lack of interest in the "legislative intent" behind any domestic regulation which stands opposed to free trade principles. A panel may be aware of this intent, but must not be influenced by non-GATT/WTO considerations in its decision-making. Since 1995, free trade principles have had the power to undo domestic laws and regulations, re-

146. Recall John H. Jackson's praise of the WTO system for having eliminated "GATT a la carte." See JACKSON, *supra* note 35, at 47.

ardless of the law's purpose and no matter how strongly it is supported by domestic constituencies. Some might suggest that citizens and consumers have been liberated from protectionist domestic regulation in favor of the far preferable free trade principles of GATT/WTO. We have, however, no political measure of this "preferability."

The *Fuji-Kodak* case ought not to be seen as a minor, rather eccentric case—one in which the U.S. "lost its touch" with the WTO panel and failed to produce sufficient evidence. Rather, it was a case in which the U.S. grafted its long-time wish that Japan would cease protecting its small and medium retailers onto a case ostensibly about the difficulties of distributing film in Japan, with devastating results for the Japanese small retail sector. Stereotypic academic interpretations of WTO disputes have exacerbated the Western tendency to see all Japanese domestic regulation through the prism of U.S. and European attempts to open Japanese markets.

Although the WTO has advertised as one of its virtues that it is newly transparent and has eliminated special deals between member countries outside the WTO, the *Fuji-Kodak* case initially involved the threat of a powerful GATS challenge, which caused Japan to move quickly with its long-delayed overhaul of the Large Scale Retail Stores Law. It is the Japanese small and medium business sector which has lost its influence, while domestic politicians upon whom that sector has traditionally relied can claim helplessness in the face of external pressure.

It is significant that this pressure goes beyond the familiar bilateral pressure emanating from the USTR. This time, there was the prospect of having a WTO panel make sweeping negative statements about the deep structure of Japanese retailing, including presumably to the effect that it systematically "discriminates" against large retail service providers. MITI decided to "settle" in *Fuji-Kodak* and managed to persuade the entire Japanese political order that removing the Large Scale Retail Stores Law was a necessary step. Ultimately, it was the fate of the traditional *shotengai* that was finally "settled."

Had each of the Uruguay Round Agreements been put to the voters in member nations for referendum, many, if not most, would have failed to pass. To those who say that such democratic input would render the system too tentative and unwieldy, the only intellectually defensible response is that the WTO dispute settlement process has obviously overreached in

taking on the trappings of a judicial system. Modern judicial systems must, under any democratic theory, rest on a basis of complex legislation derived from competing social inputs. Since the WTO lacks such a basis, it is at best a partial, and at worst a fraudulent, judicial system. Without addressing this central issue, the WTO nevertheless continues to move forward on an ambitious route towards global economic integration. It is a matter for urgent academic consideration that no mechanism exists for measuring the desirability among national voters of this newly strengthened global legal system.