When I was Director for Japanese Affairs at the Office of the U.S. Trade Representative, my colleagues and I often wondered whether there was a better way to resolve our trade disputes with Japan than acrimonious and exhausting negotiating sessions such as last summer’s auto talks. Although I am now in the private practice of law, having left the USTR late in 1994, I still find myself struggling with the same question. One reason is that despite the lip service being paid in Japan to “early warning” and quick action to avoid confrontation on trade matters with the United States, the Japanese Government refuses to address legitimate American concerns. Kodak’s recent complaint against the Government of Japan, which is being handled by the firm where I work, is an example. Kodak’s story provides an excellent case study of why many Americans continue to feel frustrated about U.S. trade relations with Japan and why there are still many issues that require actions by the governments in both countries.

A Barrier Called “Liberalization Countermeasures”

When Kodak formally requested that the U.S. government enter into negotiations concerning market access problems in Japan, the case was dismissed by some Japanese as yet another “American company raising a groundless trade complaint.” But Kodak’s complaint raises fundamental questions regarding the nature of the Japanese market, especially the role of the Ministry of International Trade and Industry (MITI) and of the Japanese government as a whole. Did the government of Japan introduce non-transparent measures in the 1970s and 80s designed to create a market structure for the purpose of impeding foreign access? And is this market structure still being maintained today?

During the 1970s, as Fuji Photo Film Co., Ltd. (Fuji) sought to develop international competitiveness, the Japanese photographic materials market was still protected by high tariffs (40%), quotas, and a prohibition on direct foreign investment, including investment in distributors and photo processing facilities. These restrictions were progressively dismantled between 1971 and 1976, under pressure from Japan’s trading partners, the Organization for Economic Cooperation and Development, and domestic groups within Japan. With liberalization looming, MITI worked with the Japanese photographic industry to devise a strategy to prevent Kodak from achieving significant market gains in Japan. In effect, the Japanese government simply “privatized” protection. These “liberalization countermeasures” (jiyuka taisaku), as they were called by MITI itself, were aimed at,
among other things, the distribution system, and had as their purpose the creation of a marketing structure designed to resist foreign penetration.

During the liberalization countermeasures period, Fuji moved, with assistance and guidance from MITI, to establish firm control over the distribution routes for photographic film and paper. For example, almost all Fuji film destined for the domestic market is sold through four primary wholesalers (tokuyakuten). These four are specialized photographic supply distribution wholesalers that handle Fuji film exclusively. They in turn sell Fuji film directly to some large retailers and photo processing laboratories, as well as to roughly 300 secondary wholesalers, which resell the film to retail outlets. It is said that there are over 250,000 retail outlets in Japan; thus it is almost impossible for a manufacturer to sell directly to all of these stores.

Over time, Fuji, backed by government guidance, has reduced its four tokuyakuten from their original position as powerful, independent photographic supply houses to a state of utter financial and operational subservience. One observer described the relationship in terms of an old Japanese saying regarding feudal landlords and tenant farmers: “they don’t let them starve, but they also don’t let them live.”

**MITI Supported Managed Prices**

MITI assisted Fuji’s consolidation of its grip on distribution channels by issuing the “Distribution Guidelines for the Photosensitive Materials Sector.” These guidelines dealt with payment terms and distribution methods and “recommended” the reorganization of the vertical relationship between the manufacturer, wholesalers, and retail stores. MITI also helped Fuji overcome distributors’ resistance, helping frustrate Kodak’s market entry. Moreover, when “managed prices” (kanri kakaku) by Fuji and Konica were revealed by Japan’s Fair Trade Commission (FTC), MITI defended the practice by saying “the power of Kodak is very strong, and even if small manufacturers challenge it, they cannot stand up to it. Consequently, ‘managed prices’ by the two film manufacturers are unavoidable,” and undertook efforts to ensure that stable prices would be maintained at the wholesale and retail level. [“Tariff Reduction and the Promotion of International Competition: Examination of Print Price, MITI Investigated Film Price Trends,” Zenren Tsuho, December 1970, pp. 17-20.]

The U.S. government trade negotiators were not aware of the liberalization countermeasures, and in the late 1970s they continued to press Japan vigorously for further tariff cuts in consumer photographic film on the assumption that as tariffs fell, U.S. market opportunities would increase. When Japan finally agreed to offer tariff cuts on film in 1979, the results were hailed as “valuable concessions for America which would open significant export opportunities.”[Report By Industry Sector Advisory Committee 21 on Photographic Equipment and Supplies to the Office of the U.S. Trade Representative and the U.S. Department of Commerce, 19 May 1979, p. 444.]

As a result of Fuji’s tight and highly disciplined control over Japan’s photographic goods distribution network, however, Fuji has consistently held approximately a 70 percent share
of Japan’s market for consumer photographic film and a 56 percent share of the market for consumer photographic paper. Fuji’s control over the distribution routes for both film and paper renders its market position largely impervious to significant challenge by foreign competitors (Kodak and Agfa) and even by its Japanese rivals, Konica (film and paper) and Mitsubishi and Oriental (paper only). Moreover, Japanese Government data show that prices for photographic film and paper in Japan are 1.5 to 4 times higher than other major markets and in many cases have not fluctuated at all for several years. Such high, stable prices suggest the lack of a freely operating market in Japan.

What is the basis for Fuji’s control over not only its affiliated laboratories but its wholesalers and retailers as well? Our firm’s research team has uncovered the following methods:

(1) **Rebates and sales-promotion payments.** Fuji operates a complex, clandestine system of cash payments to financially-strapped wholesalers and retailers which enables it to exert great power—in some cases that of life or death—over an enterprise. Fuji uses this “carrot and stick” approach to monitor the loyalty of wholesalers and retailers, to maintain retail prices, and to exclude outsiders.

(2) **Horizontal “market stabilization measures.”** Retail outlets affiliated with Fuji work together to limit price discounting by discussing “problems” caused from discounting by outsiders and seeking “resolution” through discussions with manufacturers and wholesalers.

(3) **Retail price maintenance.** Fuji also exerts pressure through the tokuyakuten and its family laboratories on retailers to refrain from discounting the retail price of Fuji film and prints, a function which is reinforced by trade associations that punish discounters and report individual cases of discounting to Fuji.

(4) **The tokuyakuten “distribution bottleneck.”** The four major tokuyakuten not only control the distribution of Fuji film but also dominate distribution within Japan of cameras and a wide range of photographic accessories. As a result, a photographic retailer that breaks away from the tokuyakuten may not only lose access to its supply of Fuji film, but to all photographic products.

(5) **Anticompetitive institutional arrangements.** Fuji’s market stabilization efforts are reinforced by close coordination between wholesale and retail trade associations mutually committed to price stability and the prevention of “excessive” competition.

(6) **Monitoring and discipline.** Fuji has developed a multifaceted and meticulous system for monitoring the sales activities by all of its affiliated wholesalers and retailers, with the result that it is virtually impossible to reduce prices or turn to a competitor without Fuji’s knowledge.
Why Government-to-Government Consultations?

Why hasn’t Japan’s FTC taken action against such practices? There are some who contend that the FTC lacks power. However, I do not accept this explanation. Rather, it is more likely that the FTC was aware of Fujis anticompetitive practices but has tolerated them because of the nation’s overriding industrial policy goals. There are several bases to support this conclusion. First, anticompetitive practices (such as discussion for purposes of resale price maintenance) are openly and commonly reported in the press and trade association journals. Second, the FTC has taken limited enforcement actions against small sub-segments of the Fuji system (the FTC found Fuji’s 100-percent-subsidiary Fuji X-Ray in violation of Article 19 for resale price maintenance and territorial restrictions). These actions should have provided the agency with plenty of additional evidence, but only limited enforcement actions were taken against the entire Fuji system. Third, the FTC has in fact placed the sectors involved in this case on its special “watch list.” Fourth, various FTC study group reports state that this industry should be “strictly monitored” because it is an oligopolistic industry.

With respect to the role of MITI, one of the more remarkable notions being advanced in response to Kodak’s complaint is that this case involves purely private business matters and, as such, falls under the sole jurisdiction of the FTC. The proponents of this notion contend that MITI no longer has the authority to address issues involved in Kodak’s case. All that is required to reject the validity of this statement is a cursory review of a book entitled Tsusho Sangyo Roppo, which is a 2,202-pages-long compilation of trade and industry related laws and regulations published by MITI. MITI clearly has enormous legal powers. More important, as far as the Japanese government is concerned, there is no artificial division between industrial and competition policy measures because MITI continues to implement industrial policy measures that directly affect the enforcement of the Antimonopoly Law.

When the issues are understood in this context, it becomes clear that they cannot be resolved at the private sector level. MITI’s liberalization countermeasures exist in the background and involve violations of a series of commitments and pledges made by the Government of Japan to the United States in trade talks. Therefore, Kodak’s decision to seek the assistance of the U.S. government becomes quite reasonable. No private company can single-handedly resolve bilateral trade issues when these involve government industrial and competition policy. Fuji is not a principal in this case, nor, for that matter, is Kodak. That role is shared by two governments, and the issues presented in Kodak’s complaint must ultimately be resolved by the governments, not by exchanges between private firms. This case is not about trying to achieve certain market shares but about obtaining market access and trade liberalization—a request made repeatedly over the last three-and-a-half decades by Japan’s trading partners.

Charles Lake is a lawyer with the firm Dewey Ballantine, and is one of the attorneys working on the Kodak case. Portions of this article appeared in Japanese in Gendai, October 1995, pp. 132-40.
JPRI members interested in obtaining the three main documents filed with the U.S. government in support of Kodak, entitled *Privatizing Protection, Response to Fuji’s Rewriting History Volume I*, and *Response to Fuji’s Rewriting History Volume II: Evidentiary Appendix* should write directly to Dewey Ballantine, 1775 Pennsylvania Avenue, N.W., Suite 200, Washington, D.C. 20006.