Policy Approaches to Economic Deregulation and Regulatory Reform

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Policy Approaches to Economic Deregulation and Regulatory Reform

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ABSTRACT

This paper is divided into three parts. Part I contains a brief discussion of traditional theories for, and the actual methods of, economic regulation. It also examines factors that have influenced global trends toward deregulation--e.g.,regulatory failure, poor performance, labor market problems and budgetary concerns. Part II examines some of the U.S. academic literature that has analyzed the political economy of economic deregulation in the United States and the factors that drove deregulation. Chief among these factors includes: the convergence of elite opinion in support of reform and the important contribution of economic analysis in the reform process; the proactive exercise of leadership by policymakers; the role of independent regulatory agencies and courts which allowed for considerable deregulation to occur without Congressional action; and the role of Congress. Drawing on the structural features identified in part II, Part III of the paper examines the political economy of economic deregulation in Japan, both historically and at the current time. This paper argues that over the postwar period Japan has experienced a considerable degree of regulatory reform and economic deregulation. This has been driven by the interplay of four factors: the pluralization of interests within Japanese society; the emergence of domestic and international market-based pressures for change; external political pressures for change; and the perceived fiscal necessity to reduce public expenditures. Each of these factors is discussed in some detail. The paper also examines the current deregulation debate in Japan and identifies groups supportive and opposed to deregulation and regulatory reform. The paper argues that domestic and international market and technological factors have converged to necessitate on-going reforms. The costs to the Japanese economy of failing to continue the process seem to be sufficiently great that further reforms are expected. However, the paper discusses the role played by Japanese regulatory agencies, courts, policy makers and interest groups and argues that the institutional mechanisms that exist elsewhere to drive reform, or tolerate it, are less than robust in the Japanese setting.

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Introduction

Over the last 20 years, a number of once heavily regulated sectors of OECD economies have been the focus of considerable economic deregulation and regulatory reform. The sectors chosen for deregulation, the approaches employed by policymakers, and the interplay of political, social and economic factors, have varied from nation to nation.

There is no single or simple definition of deregulation and the term itself is not self-defining. A now classic definition of economic deregulation was advanced by George Stigler: namely, the state's withdrawal of its legal powers to direct the economic conduct of nongovernmental bodies[1]. Dr. Stigler's definition can encompass a very broad range of actions including the removal or reform of regulations on market entry and exit, output, services and prices. However, it may not fully encompass the use of other policy instruments that have been used in tandem with deregulation in some countries--e.g., the withdrawal or modification of exemptions from competition laws so as to extend such laws to encompass sectors of the economy previously immunized from enforcement of competition policy. Dr. Stigler's definition also does not automatically bring to mind privatizations or other restructurings of state-owned enterprises, that have been an

[1] George Stigler, "The Theory of Economic Regulation," Bell J. Econ., Spring 1971.

important recent development in Europe and, to some extent, in Japan.

This paper uses the terminology economic deregulation and regulatory reform. Although admittedly over-broad, this terminology combines economic deregulation in the Stiglerian sense with other reform efforts inclusive of privatization, restructuring and the use of economy-wide measures such as competition policy.

Since only in a few instances has economic deregulation resulted in the elimination of regulatory oversight of a previously regulated industry, deregulation has been a continuum in many countries. Typically, it is also a protracted and selective process. Economic deregulation has triggered debate in many countries as to the responsiveness, or lack of it, of economic regulations and deregulatory measures to social policy concerns such as health, safety, pollution control, employment, quality of life, etc.

Many discussions of economic deregulation and regulatory reform to which I have been a party have ultimately turned on whether the discussant believes that an efficiency-based rationale for economic deregulation applies in a given instance, and if so, if it is sufficiently sensitive to broader social policy concerns. Although that assessment is important, this paper does not attempt to assess the costs and benefits of economic deregulation on a sectoral or national basis. Rather, it identifies some of the contours of the

policy environments that can influence approaches to economic deregulation and regulatory reform.

Specifically, this paper is organized in the following manner:

Section I begins with a very brief discussion of the traditional theories for, and the actual methods of, economic regulation. Since the current interest in economic deregulation stems in part from dissatisfaction with traditional approaches to and rationales for economic regulation, Section I will offer a context within which approaches to economic deregulation and regulatory reform can be examined. Many important details will only become evident when we examine specific sectoral experiences, which is not undertaken in a detailed fashion in this paper but shall be the focus of this conference.

Section II will identify a wide array of political and economic factors influencing the nature and focus of economic deregulation in the United States, and thus provides a grounds for comparison with Japanese experiences with economic deregulation. It should be understood that U.S. experiences with economic deregulation are not being advanced as a template for economic deregulation and regulatory reform elsewhere. This paper makes no claims about the extent to which lessons arising out of the U.S. policy experience (which is looked at only in a general fashion) can be applied abroad. However, for the purpose of this discussion, we posit that

the extensive degree of economic deregulation and regulatory reform in the United States, the abundant U.S. academic literature on this subject, and perhaps even the demonstration effect of U.S. experiences, allows the U.S. experience to be a useful starting point for considering a range of political and institutional factors that can usefully be examined in the Japanese context.

Section III briefly examines approaches to economic deregulation in the Japanese context.

I. Regulation and the Move Toward Deregulation

A. Rationales

Traditional theory of economic regulation argues that regulation serves the public interest by correcting some form of market failure. An often-cited example of market failure are natural monopolies, where it was assumed that consumer welfare would not be maximized by allowing firms to pursue profit-maximizing strategies in markets that were not structurally competitive.[2] A traditional assumption has been that the market cannot efficiently support more than one firm.

Regulation may also be seen as justified under circumstances where competitive solutions exist but are seen as inefficient because of

[2] Technological change, market based pressures, and the evolution of regulatory schemes have all come to challenge traditional notions of natural monopolies.

externalities (e.g., air or water pollution), inadequate information (e.g., a safety problem in a consumer product), public goods (e.g., a lighthouse) or the problem of the commons (e.g., over-use of shared natural resources). In each of such cases the production or consumption of the product has effects that go beyond those entities that are directly involved in the production or consumption of the product.[3]

Broadly put, regulation traditionally has been viewed as necessary to remedy the types of market failure we have alluded to above. A general rationale for regulation has been that it "provides protection for consumers or workers".[4]

Observers of U.S. business history argue that New Deal regulations in the U.S. transportation (railroad, trucking, airlines), communication (telephone and telegraph), energy (electric and gas) and financial sectors were all designed to in some sense stabilize

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[3] See, OECD, Regulatory Reform, Privatisation and Competition Policy (Paris:OECD 1992) at 12.

[4] Paul W. MacAvoy, Industry Regulation and the Performance of the American Economy (New York: W.W. Norton & Company, 1992) at 1. Paul MacAvoy argues that in trucking rates and airline fares, for example, regulation was seen as necessary because rates varied widely from monopolistic to competitive levels. And in regulating retail gas, electricity and telephone companies, state and federal legislatures argued that cost based prices were necessary so that local monopolies could not set high and discriminatory prices. The underlying assessments of business conditions, of course varied. In airlines, for example, the early justification for regulation stemmed from arguments about "excess competition". In communications, in contrast, the underlying argument was often "natural monopoly".

competition through government control of price, profitability, entry, and restructuring.[5] Such control was believed to be necessary to keep a tight lid on monopolies such as utilities and to deal with complex competitive problems (as in the case of railroads) for the public good. Much of the economic regulation introduced in the first quarter of the century in the United States was designed to curb the market power of firms and to protect consumers from monopoly power. A customary way of doing this was to create a regulatory agency endowed with wide powers to establish price ceilings in line with the costs of production and distribution[6].

New Deal legislation gave federal agencies far greater powers than earlier legislation.[7] The main objectives of economic regulation in these industries included high quality, wide availability of service, secure contractual arrangements, and stable prices.

Legislators also wished to ensure that all consumers could obtain services, even if this meant that certain customer prices are set low to ensure service, subsidized by customers who pay more. The oversight agencies then had to protect the regulated firms from

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[5] Richard H.K. Vietor, Contrived Competition: Economic Regulation and Deregulation, 1920s-1980s", Business History, Vol 36 October 1994 Number 4 at 1.

[6] P. MacAvoy, supra note 4.

[7] Examples include the passage of the Civil Aeronautics Act and the Natural Gas Act in 1938.

competitive entry that might erode the higher prices charged to other consumers in order to provide returns to cover the below-cost pricing to high-end customers.[8]

Professor MacAvoy argues that much U.S. regulation was put in place to have stabilizing effects along these lines. He argues that the implication of stability was as follows:

> ...companies licensed for service would offer prices that on average over a decade would be no more than sufficient to cover the average total (variable and capital) costs of service for all classes of consumers. With both averaging over time and over classes, regulation would then have one of two effects. It would either reduce monopolistic prices or require that excess revenues from continued monopolistic prices to some customers in some periods be used to subsidize services at prices below costs to other customers at other periods. [9]

B. Methods

OECD studies have identified a number of generic methods of regulation. Regulation can encompass what it calls "structural regulation", i.e., a regulatory authority determines both entry and exit.

Other forms of regulation may be aimed at "conduct". An example would be when governments attempt to direct the behavior of monopolies by placing limits on profits. A form of conduct regulation has been the approach taken by U.S. regulators in the telephone, electricity, gas, and airline industries, where ceilings were placed on the cost-of-service ratemaking. This system

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[8] P. MacAvoy, supra note 4 at 12.

[9] Id. at 12.

reflects an administrative effort to apply a pricing formula through a statutory scheme that obliges the regulated firm to file tariffs containing proposed rates. The agency then has the right to suspend any new filing for a specified period, during which time it holds hearings and investigates the reasonableness of the charge.[10] Ordinarily the goals of such ratemaking systems include: preventing excess profits; holding prices down to costs; avoiding economic allocative waste; eliminating inefficient production methods; and assuring administrative ease.[11]

A further form of regulation that has been extensive in Europe is government ownership. Public enterprises have run the gamut from entities associated directly with ministries to publicly traded joint stock companies in which the government holds a majority share but is largely a passive shareholder[12].

There is great variety in how these methods are implemented. By way of example, it is worth reviewing several instruments used by U.S. agencies to control prices and production. Agencies developed case-by-case procedures for analyzing whether or not individual

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[10] See, Stephen Breyer, Regulation and its Reform, (Cambridge: Harvard University Press,1982) at 37.

[11] Id. at 37.

[12] A classic rationale for public ownership is that public ownership permits or entities to pursue a mix of profit and other factors that maximize social as opposed to private benefits that would not otherwise be achieved under private ownership. See, OECD, supra note 3.

pricing schedules were "just and reasonable" or whether production occurs in ways that "protect the health of persons."[13] Regulatory schemes have been developed and embodied in statute that seek to bring uniformity of results across industries. For example, Professor MacAvoy argues that "state and national statues establishing agencies to control prices for electricity, gas and telephone services all contain requirements for preventing high, unstable and discriminatory prices."[14]

Another factor that has significantly shaped the regulatory process in the U.S. is the Administrative Procedures Act (APA). In its early days, a main feature of the APA was its requirement that regulated companies have recourse to due process through judicial review of agency action.[15] Over time the scope of this review has broadened to examine whether agency decisions are reasonable in light of the goals of the statute. In the 1970s, the APA came to be used by activists as a sword to ensure that their interests in "agency decision making were given fair representation."[16] And in the 1980s, the APA was used to challenge the elimination of entire programs of agencies.[17]

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[13] P. MacAvoy, supra note 4 at 21.

[14] Id. at 21.

[15] Id. at 22.

[16] Patricia M. Wald, "The Realpolitik of Judicial Review in a Deregulation Era", Journal of Policy Analysis and Management, Vol 5, No. 3 (1986) at 535.

[17] Id.

The OECD also identifies competition policy enforcement as an economy-wide method of regulation. Competition (or antitrust) enforcement can be used in tandem with economic deregulation and regulatory reform and for this reason is properly an area heavily emphasized by the OECD. Yet, to characterize it as simply another form of regulation is to misconstrue the fundamental goals and instruments of competition policy enforcement.

Competition enforcement seeks to create or maintain a competitive marketplace rather than to replicate the results of competition and correct for defects in competitive markets. Antitrust laws, therefore, act "negatively, through a few highly general provisions prohibiting certain forms of conduct. They do not affirmatively order firms to behave in specified ways; for the most part they tell private firms what not to do... Only rarely do the antitrust enforcement agencies create the detailed web of affirmative legal obligations that characterizes classical regulation."[18]

Antitrust laws are premised on the assumption that competitive market environments will achieve more efficient allocation of resources, greater product efficiency, and increased innovation. It seeks to achieve these ends by removing private impediments to competition[19]. As Stephen Breyer argues,

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[18] S. Breyer, supra note 10 at 157.

[19] Id. at 158.

> where this assumption holds true, antitrust would ordinarily seem the appropriate form for government intervention to take. Where the assumption fails, one finds the demand for other modes of governmental intervention, such as classical regulation. Viewed in this way, regulation is an alternative to antitrust, necessary when antitrust cannot successfully maintain a workably competitive marketplace or when such a marketplace is inadequate due to some other serious defect.[20]

C. Factors Influencing Economic Deregulation and Regulatory Reform

A fairly recent report by the OECD issued upon completion of an extensive survey and analysis of regulatory reform and deregulation, identified five major factors as stimulating domestic reform efforts within member countries: regulatory failure; poor performance; labor market effects; budgetary considerations; and technological change.

With respect to regulatory failure, the OECD suggests that in many countries interventions, once intended to correct market failures, have produced adverse and often unintended consequences for the achievement of efficiency. Since regulation was designed to serve a variety of public interest concerns unrelated to economic efficiency, such regulation in numerous instances distorted the price mechanism and led to uneconomic activities and outcomes. Excessive costs, high prices, pricing rules that made administrative sense but not economic sense, excessive quality standards in relation to what consumers required and were willing to pay for, and a variety of other inefficiencies have all been identified as important motives for deregulation and regulatory

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[20] Id. at 158.

reform.[21]

Critics of regulation in the U.S. have argued that the growth of regulation in the U.S. has brought on a variety of ills such as "high cost; ineffectiveness and waste, procedural unfairness, complexity and delay; unresponsiveness to democratic control; and the inherent unpredictability of the end result."[22]

The OECD report does not try to sort out the domestic factors that can lead to such outcomes. Professor Paul MacAvoy identifies two main "culprits" as causing serious regulatory problems in the United States. The first of these, he argues, is the tendency of regulation through legislation to serve too many and too diverse interest groups, thereby producing distortions in the regulatory process and in pricing and structure. The second culprit is the limited managerial competence to be found in the regulatory agencies. He also notes that approaches to regulation that may have made sense under one set of market conditions often proved to make far less or no sense under different conditions.[23] Overall,

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[21] Regulation has been justified in the name of market failure, which is itself not a static concept. As the OECD points out, changes in technologies and market conditions have led to re-thinking of the nature and extent of market failure. See, OECD, supra note 3 at 20.

[22] S. Breyer, supra note 10 at 4.

[23] For example, Professor MacAvoy points to the use of ceilings on prices in line with previous period costs of service. He argues that" these worked well when industry demands increased and costs decreased each year from larger scale. But when inflation was accompanied by recession, so that costs increased

imperfect procedures probably have "prevented regulation from working in the interests of consumers, by reducing production across the regulated industries and thereby reducing the rate of growth of the economy." [24]

A second and related motivation for deregulation and reform, as noted by the OECD, is the perception that regulated sectors have performed poorly. Comparisons with deregulated sectors in other countries, or between regulated and deregulated regions within countries, have accentuated this recognition.

Regulation itself has been identified as contributing if not producing such poor performance--e.g., by skewing incentive structures through low salaries; allowing political interference in decision making; imposing constraints on diversification; and limiting public and regulated enterprises from introducing new technologies or management methods.

Third, the OECD notes that labor market problems have also had significant effects on the movement toward regulatory reform. The performance of public sector entities deteriorated as union pressures brought pay increases in excess of productivity

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rapidly, this same method had quite the opposite effect. Prices lagged behind costs so long as costs increased continuously. The operating practices of the agencies by themselves generated adverse price and production behavior". P. MacAvoy, supra note 4 at 4.

[24] Id. at 4.

improvements. In the U.K. for example, the OECD notes that support to public sector entities became a disguised employment subsidy with adverse consequences for the specific sector and the overall health of the economy as a whole.[25]

A fourth factor exerting a strong influence on deregulation and regulatory reform has been budgetary. Privatization can provide a direct cash infusion to public coffers, and other forms of regulatory reform can bring substantial cost savings. Both the United Kingdom and Japan are cited as countries where this motivation featured prominently in the privatization that took place. In the U.K. context, the instruments chosen to implement privatization have included transfer of share ownership from public to private sectors, subcontracting and curtailment of statutory monopoly powers.[26]

The OECD does not try to weigh the relative importance of any given factor in a country's decision to embark on a program of reform. Expert opinion often divides on this point.[27]

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[25] OECD, supra note 3.

[26] See, Colin Harbury, "Privatization: British Style", Journal of Behavioral Economics, Vol 18, No 4 , 1990 at 268.

[27] In the U.K., for example, Sir Alan Walters, former personal economic adviser to Prime Minister Thatcher, has argued that the two principal motives for economic deregulation and in particular the extensive privatization programs of the Thatcher government include: (1) the desire to reduce the politicization of economic decision making, particularly in state run companies, and (2) the
desire to increase net wealth through improvements in economic

II. Deregulation in the United States

Political scientists Martha Derthwick and Paul Quirk, in their extensive analysis of regulatory reform in the U.S. airline, trucking, and telecommunications industries, argue that five general factors made deregulation possible in the United States--albeit to varying degrees, and with a wide range of consequences for consumers, workers, and affected industries.[28] We shall briefly review their conclusions and then related them to deregulation in Japan.

First, the authors argue that elite opinion in the U.S. converged in support of reform. In particular, they suggest that deregulation would not have occurred in the United States had it not been for the theoretical and applied work of economists that provided compelling evidence that much economic regulation in fundamentally

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efficiency of enterprises. Professor's Vickers and Yarrow, on the other hand, argue that the momentum of privatization policies were initially influenced by dissatisfaction with the performance of publicly-owned industries, later by short-term budgetary considerations, and finally by share ownership and distributional objectives. The distributional objective--i.e., gaining political advantage by means of transfers of wealth-- was far more important in a latter period of privatization--e.g., between 1987-93. Sir Ian MacGregor, a key figure in privatization in the U.K., stresses that privatization was driven by ideological coupled with a growing recognition of privatization's collateral advantages--namely, the populist notion of widening share ownership. See, Privatization and State-Owned Enterprises, Paul MacAvoy, W.T. Stanbury, George Yarrow, Richard Zeckhauser, ed. (Boston: Kluwer Academic Publishers, 1989).

[28] See, Martha Derthwick & Paul J. Quirk, The Politics of Deregulation, (Washington D.C.: Brookings Institution, 1985).

competitive markets had large costs without the associated benefits.[29]

This academic literature is well known and need not be fully amplified here. Suffice it to say, however, that numerous sectoral and theoretical writings of what might be called private-interest theories all but superseded the public-interest theory of regulation that had dominated the thinking of earlier decades. Writings in this vein offered a far more negative view of regulation and regulators' behavior.[30] This literature challenged the public-interest theory by focusing on regulators' behavior, which not only showed the sources of inefficiency but other structural features that kept such inefficiencies in check.[31]

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[29] Where regulation was not anticompetitive (e.g., it did not restrict minimum prices of goods and services), Derthwick & Quirk argue that elite opinion did not similarly converge. They cite natural gas as one case in point. Id. at 238.

[30] See, for example, Harvey Verch and Leland Johnson, "Behavior of the Firm Under Regulatory Constraint," Amer. Econ. Rev.,. Dec. 1962, pp. 1052-69.

[31] See, George Stigler, supra note 1; Sam Peltzman "Toward a More General Theory of Regulation", J. Law Econ., August 1976, 19 (2); Clifford Winston, " Economic Deregulation: Days of Reckoning for Microeconomists" Journal of Econ. Lit. Vol XXXI, Sept 1993 at 1263-1289. Gary Becker, "A Theory of Competition Among Pressure Groups for Political Influence", Quarterly Journal of Economics, vol. 98 (August 1983). Peltzman argues, for example, that the lessons of this theoretical literature are that well organized groups, (frequently comprised of producers), tend to benefit more from regulation than broad diffuse groups (such as consumer groups) and that regulatory policy will strive to preserve a politically
optimal distribution of rents across this coalition of well-organized groups. But "because the political payoff to regulation arises from distributing wealth, the regulatory process is

These theoretical writings, argued that social welfare would be enhanced by deregulation because the gains to those who support deregulation and to the wider society were likely to be larger than the losses to those benefitting from regulation.[32]

Derthwick and Quirk go on to make the important point that the soundness of the empirical contributions of economist would not have been sufficient to propel the policy process toward reforms, had influential policy research institutions and government agencies not housed reform-oriented policymakers. This may be another way of saying that individuals and institutions in favor of regulatory reform were on hand and could be and were mobilized in support of it.

The concept of economic deregulation and regulatory reform has proved politically malleable and attractive to U.S. political leadership. Presidents Ford, Carter, and Reagan, in seeking to

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sensitive to deadweight losses. Policies that reduce the total wealth available for distribution will be avoided, because, other things being equal, they reduce the political payoff from regulation." See, Sam Peltzman, " The Economic Theory of Regulation After a Decade of Deregulation", in Brookings Papers on Economic Activity, Martin Baily and Clifford Winston, ed. (Washington D.C. Brookings Institution 1989) at 12.

[32] See C. Winston, Id. In this excellent survey article, Dr. Winston identifies the variety of economic inefficiencies created by regulation that economists predicted would be reduced or eliminated by deregulation. Sam Peltzman, in reviewing deregulation, argues that the U.S. deregulatory experience with railways is quite consistent with the theoretical predictions of economists. Trucking deregulation, however, was a "resounding defeat" Id.

address inflation and respond to public dissatisfaction with government intervention, embraced the policy prescriptions of experts and academics. In this sense, deregulation and procompetitive reform was a national rather than a partisan movement, it that found broad political appeal across the political spectrum.

Liberals supportive of deregulation and regulatory reform were able to stress the consumer gains to be achieved through lower prices and by putting an end to what could be characterized as government coddling of business interests. Conservatives could embrace reform in the name of reducing the excessive and intrusive burden of government regulation in private markets. These different elements of elite opinion converged in favor of reform.

A second important variable identified by Derthwick and Quirk was the proactive exercise of leadership by policymakers. The inference drawn is that leaders can in fact be mobilized to serve broad and often diffuse interests, instead of narrow and particular ones, if the issues are "ripe" and fit well with the leaders political agenda, if the benefits are perceived as greater than the risks, and if the steps that are taken prove popular or have a positive demonstration effect.

Third, Congress did not have to act in order for a considerable amount of deregulation to occur. This is owing to the independence

of existing regulatory commissions and the interplay between those commissions and the courts. The former are endowed with broad powers to act, and occasionally have had strong and independent leadership. Regulatory commissions have, on occasion, served as a spur to Congress. In addition, U.S. courts have provided a forum for review of agency actions and have, particularly through antitrust litigation obliged industry restructuring--e.g., in telecommunications.

A fourth variable emphasized by the authors is that in some instances Congress did take legislative measures and in several instances affected industries proven unable to effectively countervail the confluence of factors we have just identified.

In sum, areas that experienced extensive deregulation in the United States benefitted from a number of conditions: reform proposals were firmly rooted in empirical analysis; amenable to political manipulation; buttressed by institutional mechanisms that provided reformers with the requisite independence to take action independent of legislative action; and came up against interests that at times were badly organized or otherwise unable to mount an effective counter-offensive.

Airlines deregulation often is cited as one sectoral example where all of these factors together. Certainly this is a sector there was comprehensive deregulation and even the elimination of the

oversight agency. Specifically, in the late 1970s the CAB abandoned regulation by suspending scheduling and entry restrictions, and allowed fare flexibility between city pairings.[33] The passage of the Airline Deregulation Act eliminated the CAB. By that time, controls in the agency had effectively been abolished from within.[34]

How and why did this come about? Stephen Breyer, now a Justice on the U.S. Supreme Court, in his assessment of airline deregulation in the United States, places particular emphasis on the role played by Congressional hearings. These were able to mobilize the political support needed to implement those reforms long seen as desirable by economists. The following are the general conclusions Breyer draws from his experience with airline deregulation in the late 1970s.

First, in order for reform to be implemented, interested parties must possess detailed knowledge of the changes that are needed and desirable. Second, reformers must come up with a real-world alternative to existing forms of regulation as well as a practical transition plan. Third, they must organize and deal with political

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[33] P. MacAvoy, supra note 4 at 112.

[34] This had, in the view of some analysts, provided enough experimentation with the open market process "to establish that service would improve, so that congressmen voting for the elimination of the CAB would not later be blamed for market instability, monopoly or whatever". Id. at 112

factors.[35]

With respect to the last point, political leaders must be persuaded to devote the necessary time and effort to organizing a political coalition intent upon reform. Breyer argues that reform can be accomplished if the issue becomes visible politically. Congressional hearings are one means of making the issue "ripe" for political action. But as the issue becomes visible it must be characterized in such a fashion that it will strengthen the political alliance in its favor. Coalitions to implement reform must also be formed within the executive and the legislative branches,[36] as well as among outside interests. Advocates of reform must put forward a practical and fair plan that maps out the transition from the regulated regime to the new system.

In the context of airline deregulation, the Subcommittee on Administrative Practice and Procedure, chaired by Senator Kennedy, was the Congressional group that took the lead in pushing for airline deregulation. It did so, Justice Breyer argues, because political benefits would accrue to the Committee if it undertook an investigation and hearings in that area. Academics already had offered extensive evidence that the airline industry was an instance of regulatory failure, and that reform would lead to lower prices while maintaining service.

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[35] S. Breyer, supra note 10 at 318.

[36] Id. at 318-321.

For example, Breyer argues that there was ample evidence that the market defect that was the original justification for airline regulation (namely, excessive competition) did not exist. Instead, the markets were in fact "workably competitive".[37] Reformers were able to put forward strong arguments that the industry could support competition and that to the extent there were problems (e.g., excessive competition), other policy instruments or oversight agencies could address them. For instance, antitrust law could deal with predatory pricing, and the FAA could deal with safety related matters.

Politically, deregulation and regulatory reform gave the Kennedy Committee a specific mission but also a wider theme that permitted it to review other sectors and agencies. Through hearings the Committee could gain develop the expertise that would enable it to play a role in other economic regulatory areas.[38] Thus an ambitious committee chairman was able to gain considerable prominence as a policymaker by taking on this regulatory reform agenda.

Further, Justice Breyer argues that the Committee was effective because it did its homework in an exhaustive fashion. It went through a painstaking preparatory stage of identifying issues and substantive arguments. The Committee drew upon extensive existing academic studies showing that the Civil Aeronautics Board's

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[37] Id.

[38] Id. at 323.

regulation of prices and entry had led to high prices, overcapacity, and inefficiency.[39] The Committee then forged alliances within the executive branch and elsewhere, collected information and proposals, and scheduled extensive public hearings. These hearings then served the multiple functions of: obliging executive agencies and other interests to take a stand on issues and thereby serve as catalysts for change; marshaling existing arguments and information both in favor of and opposed to regulatory reform; and serving as excellent "theater" to propel the process of reform forward.[40]

Public hearings had the added benefit of showing up the inefficiencies of the existing regulatory scheme. They brought a number of government agencies to the table to speak up in favor of reform because they believed that the existing system was inefficient and "wrong".[41] This, Breyer claims, had a "powerful" effect in convincing Congress to act to change the system.[42] The coalition in support of reform consisted not only of those with an

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[39] Breyer argues that high fares was basically a problem of low load factors, which itself reflect excessive scheduling which in turn derived from CAB action that inhibited price competition. He also argues that regulation had closed the industry to newcomers; had guaranteed relatively stable market shares to incumbents; and had weakened drives to efficiency. CAB procedures also violated "accepted administrative norms of efficiency, fairness or propriety". Id.

[40] Id. at 327.

[41] Id.

[42] Id. at 321.

economic interest in any given outcome, but also groups holding ideological views that corresponded with the position on issues that had made the issue a politically visible one.

While Justice Breyer sees the exhaustive work of the Kennedy Committee as the central driver, others have placed relatively more emphasis on the role of executive and presidential action--even in the case of airline deregulation. James Miller, for example, argues that presidential sponsorship is crucial to deregulation given the basic political economy of economic regulation. Drawing on the traditional paradigm of the iron triangle, Miller has argued that typically

> an agency is captured by its industry and protects it from the ravages of competition. The agency is nurtured by the committees on Capital Hill who oversee its programs and its budget. The industry is very attentive to the Senators and Representatives on those critical committees...What Hill committee will say, 'we have been meddling needlessly where free markets would do better?'....Moreover, when technological change or an increase in the geographic expense of competition puts stress on a regulatory system, the agency's usual response is to expand its domain.[43]

Given this reality, Miller argues that the politics of regulation makes presidential initiative critical[44]. He does point to the

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[43] James C. Miller III, "The Administration's Role in Deregulation", 55 Antitrust L.J. 199 (1986)

[44] Miller cites some five ways that leadership can be exercised. First, by direct action--e.g., through an executive order which is the method employed by President Reagan in oil. Second, through proposed legislation. Third, through the power of appointment to regulatory agencies--which was the case in airlines. Fourth through legal intervention--e.g., a lawsuit--such as was the
case in telecommunications. Fifth, by providing the necessary

Congressional hearings on airline deregulation as being a "watershed event," but argues that absent the support of presidents Ford and Carter and certain appointees to the chairmanship of the CAB, deregulation would not have occurred.[45]

III. Deregulation in Japan

Thus far we have discussed various rationales for regulation and deregulation, identified basic factors driving deregulation, and reviewed the political economy of economic deregulation in the United States. We now turn to an examination of the political economy of economic deregulation in Japan context, historically and at the current time. Where useful, there will be comparisons made with the U.S. experience.

A. The Early Postwar Years: The Government's Visible Hand

It is worth recalling that an overriding goal of Japan's government officials in the early postwar years was to catch up to Western countries through policies that promoted high levels of savings and investment generally and high levels of investment in certain

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supporting analysis--e.g., the commissioning of studies on deregulation by President Ford. Id.

[45] Indeed, Miller quips that not only does deregulation require the cooperation and support of the President, but to assure success, you may need a whole host of them. Id.

specific sectors. In the immediate postwar years the government had powerful instruments available to it to help achieve these goals--e.g., direct administrative controls over foreign exchange transactions and considerable formal and informal influence over the direction of investment.

Two legal instruments that provided such direct controls over economic activity were the Foreign Exchange and Foreign Trade Control Law (FECL) and the Foreign Investment Law (FIL). Most laws in Japan have been written as to give wide latitude to bureaucratic discretion; these two laws are cases in point. In effect, government officials could and would make decisions on the basis of their own interpretations of national interest.[46] Protection from import competition, based on theories of infant industry protection, routinely was applied, and until the early 1970s, was either explicitly or implicitly tolerated by other advanced industrial countries. By the 1970's, many of the specific controls over economic activity had been weakened or eliminated, and others were under a variety of cross-pressures that led to further adjustment.

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[46] Thomas Pepper, Merit E. Janow and Jimmy Wheeler, The Competition: Dealing with Japan (New York: Praeger Publishers, 1985). Lawrence Krause and Sueo Sekiguchi describe MITI's role in those days in the following manner: "The MITI had to approve, on a case by case basis, any foreign trade transaction that was not to be based on the standard method of payment. Thus, the MITI became intimately involved in business decisions from the beginning and was able to evolve into a very powerful ministry". Lawrence B. Kraus and Sueo Sekiguchi, "Japan and the World Economy" in Asia's New Giant, ed. Hugh Patrick and Henry Rosovsky (Washington D.C.: Brookings Institution, 1976), at 411.

B. Forces for Change

To the extent that regulatory reform and economic deregulation has occurred in Japan, it has arguably been driven by the interplay of at least four factors. First, the pluralization of interests within Japanese society. Second, the emergence of domestic and international market-based pressures for regulatory change, notably the important role of technological advances. Third, external political pressures for change, and fourth, the perceived fiscal necessity to reduce public expenditures, which arose in part from the government's inability to win legislative approval for revenue generating tax reforms.[47]

Let me briefly examine each of these elements.

1. Pluralization of Interests

It is hardly surprising that economic growth and prosperity gradually reduced the dependence of commercial and industrial enterprises on economic bureaucracies. Earlier degrees of government control over economic activity became increasingly inappropriate (and unwelcome) given the level of prosperity attained. In some areas, regulatory adjustments were necessitated by Japan's signing on to international agreements and organizations

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[47] John Haley, "The Context and Content of Regulatory Change in Japan", in The Age of Regulatory Reform, Kenneth Button and Dennis Swamm, ed. (Oxford: Clarendon Press, 1989) at

such as the GATT and the OECD. In response, government agencies reduced some of their controls over capital flows and investment, and adjusted some of their industrial support measures. Phased liberalization, usually of a minimalist nature, gradually was introduced, and this was reflected in adjustments to the FECL and FIL and in other laws and regulations.

In addition, as per capita income increased, new domestic goals emerged alongside that of economic growth--e.g., protection of the environment, better health-care facilities for the aged, and increased leisure time. One need only recall the "kutabare GNP" ("Down with GNP") campaign, and the sarcastic slogan "Gross National Pollution" that became a catchword in the early 1970s to be reminded of the public criticism that arose in Japan over the government's perceived single-minded pursuit of industrial development objectives.

The 1980's witnessed a further proliferation of diverse economic interest groups, both inside and outside the government, competing for resources and calling for further modifications to various aspects of regulatory control. Developments in the telecommunications sector, which are discussed below, offer a good illustration of the growth of multiple and competing interests. However, tensions erupted in other sectors of the economy subject to regulatory control. For example, strains brought on by regulation were showing up in the petroleum refining and

petrochemical industries in the mid-1980's.

Under the Petroleum Industry Law (PIL), which was administered by MITI, domestic petrochemical industries were obliged to purchase naphtha from domestic petroleum firms. When domestic naphtha prices rose to levels substantially above those found in world markets, domestic petrochemical firms threatened to circumvent the existing regulatory scheme and purchase imported naphtha directly. Eventually, MITI and industry reached an accommodation whereby the petrochemical firms were permitted to purchase imported naphtha but were required to allow the petroleum firms to be the import agents. MITI's specialized agency responsible for administering the PIL retained the authority to regulate domestic prices but agreed to hold the price of naphtha down to the price of imported product.[48]

2. Market Pressures

In Japan as elsewhere, market-based pressures have been an important agent of regulatory change. Although regulatory reform generally has tended to lag behind market and technological change, regulatory adjustments have occurred. Let us examine telecommunications in somewhat more detail.

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[48] For more details on this case see: T. Pepper, M. Janow & J. Wheeler, supra note 46, and Frank K. Upham, "The Legal Framework of Japan's Declining Industries Policy:The Problem of Transparency in Administrative Processes", 27 Harv. Int'l L.J. 425 (1986).

After World War II, several public corporations were created--NTT, Japan National Railways (JNR) and the Japan Monopoly Corporation (JMC). NTT was established as a public corporation having a monopoly in domestic telecommunications. It was under the jurisdiction of the Ministry of Posts and Telecommunications (MPT) and MPT identified those areas of business within which NTT could operate, but did not regulate its activities as strictly as did the FCC in the United States. Much of NTT's top management came from MPT. As was the case in Europe and elsewhere, this was seen as a natural monopoly.[49]

The early mission of NTT was to establish a national system and install telephones. Telephone subscribers, both business and residential, were required to pay a substantial one-time fee in the form of "telephone bonds" to establish service; sale of these bonds was used then to finance the expansion of the system. Installation charges were set at a higher rate for residences than for businesses on the grounds that a home telephone was a luxury, whereas calls from the office contributed more to overall economic

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[49] This is in contrast to JNR, which had a nationwide network but faced competition from other modes of transport such as road transportation, private railways and airlines. Although we do not discuss privatization of JNR in this paper, it is worth noting that some scholars have identified the following internal problems as driving the restructuring of JNR: excessive government involvement, unclear management responsibility, limitations on the pursuit of varied and dynamic business activities and "abnormal" labor-management relations. See, Masami Sakita, "Restructuring of the Japanese National Railways: Review and Analysis", Transportation Quarterly. Vol XLIII, No 1 January 1989 at 30.

development.[50] By the end of the 1970s, a national infrastructure was in place.

In the 1980-1985 period, when conducting research on Japan's industrial development policies, I interviewed Japanese government officials in several ministries as to the active debate then underway on the need for regulatory reform of NTT driven by the growth of data communications. The fusion of computers and communications was producing strong pressures for market entry from the domestic and foreign computer firms.

These technological developments also produced and exacerbated interministerial conflict. At various points in the 1980s, for example, MITI and MPT have been engaged in intense struggles over oversight responsibility for the information-processing industry. In the early 1980s, with increased demand for Value-Added Network Services (VANS), MPT proposed a VANS law that would allow private companies to supply services to third parties.

This bill engendered fierce struggles between MPT and MITI. MPT was keen on regulating value-added network services in the apparent belief that such regulation was needed to avoid "confusion" in the marketplace. MITI, drawing from its experiences fostering a domestic computer industry comprised of a number of competing firms, argued that restrictions would interfere with the

[50] T. Pepper, M. Janow and J. Wheeler, supra note 46.

development of the information-processing industry--including computers which were under its jurisdiction[51]. The resulting draft law ultimately was set aside. Instead, various amendments to the Public Telecommunications Law were enacted liberalizing third party use of leased circuits. Thereafter various companies entered the market for value-added services. The reasons for liberalization of VANs as well as the restructuring of NTT and telecommunications more broadly appear to have been both competitive and budgetary.

A competition-based argument often advanced states that it was NTT's monopoly position in the area of data transmission that had led to Japan's falling behind the United States in this aspect of information processing. Further, that innovation was impeded by the regulatory environment and by the overly close ties between NTT personnel and manufacturing firms. This type of argument arose in part since the original rationale for Japan's monopoly structure had eroded--installation of telephone lines had largely been

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[51] I recall the furor that developed in late 1983 when MPT revealed draft legislation on VANS that barred firms with 50 percent or more foreign ownership for offering nationwide, large scale data networks. At the time, there were hints that such measures were needed to prevent IBM Japan and ATT from taking over a still developing market in Japan. US officials and business representatives objected strongly and argued that the proposed legislation was discriminatory and protectionist. Interestingly, MITI also supported that position arguing that enhanced services should be considered outside the scope of existing regulations on basic transmission services. MPT took the opposite approach, which was consistent with its own desire to retain control over as much of the industry as possible. For a more detailed elaboration of these developments See, Pepper, Janow and Wheeler, supra note 46.

achieved on a national basis, and there was a tremendous growth in demand for leased circuits capable of handling new data transmissions.

A budgetary rationale for NTT deregulation also featured prominently. Government debt in Japan had grown from 9.2 percent of GNP in 1974 to 41.2 percent in 1982.[52] In 1982, the Ad Hoc Commission on Administrative Reform proposed that NTT be reorganized into private companies to raise capital to reduce debt. It also argued that the time had come for Japan to allow more competition in telecommunications, if only because it had no choice if it wanted to keep up with developments in international markets.[53]

International political pressure also drove regulatory reform in telecommunications. NTT procurement practices, MPT's standards, certification and testing procedures, its regulation of mobile communications such as cellular telephone and third party radio, have all been sources of bilateral U.S.-Japan trade friction.

With respect to procurement, and in contrast to AT&T, NTT did not manufacture its own equipment. Rather, until the late 1970s NTT procured only from domestic electronics companies. NTT was

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[52] J. Haley, supra note 47 at 134.

[53]The Commission recommended the privatization of the Japan National Railways, NTT and the Japan Monopoly Corporation as necessary cost-saving reforms.

practically a domestic monopsonist for such equipment, and its procurements from domestic sources were critical to the development of domestic electronics firms. In the late 1970s, international, especially U.S., criticism of NTT procurement practices became acute. As one expert notes, "cost-effective, comparable if not superior equipment was routinely frozen out by narrow specifications that had little if anything to do with actual performance"[54] Foreign trade pressures eventually led to substantial revisions of NTT's procurement procedures and practices.[55]

Product standards and testing were another subject of bitter bilateral trade tension. In the so-called MOSS talks, the U.S. Government requested that Japan simplify its procedures for approving certain equipment, and provide greater entry for competitive U.S. products. Some modifications in standards ensued--e.g. self-certification for value added networks, changes in technical standards, and modifications in standard setting procedures.

Legislation for the privatization of NTT and the JMC was enacted in

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[54] Tsuruhiko Nambu, "A Comparison of Deregulation Policies" in E. Noam, Seisuke Komatsuzaki, Douglas A. Conn, Telecommunications in the Pacific Basis: An Evolutionary Approach (Oxford: Oxford University Press, 1994) at 42.

[55] See for example the Government Procurement Code negotiations that occurred in the context of the Tokyo Round, and the bilateral U.S.-Japan NTT procurement agreements.

1984 and became effective in 1985. Telecommunications were subject to the resulting Telecommunications Business Law (TBL), and NTT was regulated under the NTT Corporation Law.

NTT nominally became a private company, although more than 51 percent of its shares were held by the government, its budget was still subject to Diet approval, many MPT officials were still on its staff, and it was required to provide universal service. NTT was permitted to provide both local and long distance services but it was prohibited from entering the international market, which remained under KDD's jurisdiction. In addition, NTT initially was not permitted to change its tariff structure.

The revised TBL provided for new entry in the categories it established. Service providers were divided into Type I and Type II carriers. Type I, primary carriers, own their own telecommunications facilities and were able to supply both basic telephone services as well as data processing and value-added network services. Three firms were permitted to enter into the long distance market: Daini Denden (DDI), Japan Telecom (JT), and Teleway Japan. Under the TBL, Type I carriers are subject to extensive MPT regulatory oversight. MPT controlled both market entry and exit and regulated permissible rates of return. According to some experts, MPT's regulatory approach had a number of adverse effects. Since NTT was not permitted to lower its tariff structure, the three new common carrier companies have put NTT

under competitive pressure in the long distance market by selling below NTT. At the same time NTT was obliged to continue providing universal service and local service at a loss. Initially, rate rebalancing or access charges were not permitted. Limitations on the number of new entrants in this market coupled with constraints on NTT's tariff structure also had the effect of limiting the competitive pressures faced by the new common carriers (NCC).[56]

Type II carriers lease lines from Type I carriers, and under the TBL are permitted to supply data processing and other enhanced services with less MPT oversight than Type I carriers, although Type II carriers are subject to certain filing requirements. Numerous firms, foreign and domestic, have entered into this market.

In the late 1980's, yet another area of bilateral tension developed in the telecommunications sector. This time the dispute centered on the effect of the revised regulatory scheme as it affected foreign access to Japan's still nascent third party radio and cellular telephone market. As noted, under the revised law NTT was able to offer services nation wide but several new common carriers entered the market. IDO, a subsidiary of Teleway Japan, used NTT cellular technology. A second carrier, DDI, used Motorola technology. Both of these were subject to MPT review and MPT

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[56] See, Susumu Nagai, "Japan: Technology and Domestic Deregulation", supra note 54 in E. Noam, et. al.

imposed territorial restrictions on the services that each could offer. IDO was assigned the Tokyo metropolitan area, which was an immensely profitable area, while DDI was awarded the Kansai area, a much smaller market. This regulatory arrangement meant that NTT protocol applied to the Tokyo-Nagoya corridor while NTT and Motorola competed everywhere else. Motorola, feeling that this scheme severely limited its access to the Japanese market, pressed the U.S. Government to seek a negotiated solution with the Government of Japan. Certain new provisions in the 1988 Trade Act were invoked to trigger a trade action equivalent in nature to a section 301 investigation. Difficult bilateral negotiations ensued and an agreement was ultimately reached in 1990.

In that agreement, MPT agreed to certain deregulatory measures. Specifically, it agreed to reallocate spectrum so as to allow Motorola to compete in the Tokyo-Nagoya area. However, in keeping with MPT's desire to keep the market players limited to two companies, instead of letting DDI into this profitable market segment, MPT obliged Motorola and IDO to work together. MPT also obliged IDO to spend considerable funds to build the necessary infrastructure to handle the Motorola system. After considerable delay, which Motorola claims substantially reduced their indisputable technological lead in this product market, Motorola gained access to the Tokyo area market.

MPT's revised regulatory arrangement put IDO in the peculiar

competitive position of being obliged to operate a system that directly competed with its already functioning system. It was not hardly surprisingly that several years later Motorola complained to the U.S. government that the arrangement was not resulting in the access to the market envisioned by the earlier arrangement. The subsequent bilateral government-to-government negotiations were particularly acrimonious. [57] In 1994, the two governments eventually reached agreement: MPT agreed to provide greater spectrum for Motorola-type cellular systems and used its regulatory powers to pressure IDO to provide greater deployment, operation and promotion of the Motorola type system.[58]

While the telecommunications sector has seen substantial deregulation, the process of NTT's "privatization", and more generally Japan's approach to the reform of its telecommunications regime has generated and continues to generate domestic and international controversy. The U.S. government, continues to urge MPT to introduce more transparency in its regulatory practices (e.g., by permitting formal comment on regulations before they become final decisions) and to ensure equal access to its

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[57] This dispute was particularly bitter because MPT had begun to promote a digital system while Motorola's analog system was getting fully operational. Many in Japan argued, as a result, that the U.S. Government had taken up a single company issue and that Motorola was obliging Japan to use technology that was on the way out.

[58] For more detail on these trade disputes see, Laura D'Andrea Tyson, "Who's Bashing Whom", (Washington D.C.: IIE, 1992) chapter 3.

negotiated local network interconnection regime.

Just this month the Telecommunications Council has issued a report recommending a break-up of NTT. There are reports that the Council's recommendations are opposed by NTT itself, and did not even receive the unanimous support of Council members. It has, however, been reported to have the supported of Keidanren and MPT, although even this last point is far from certain. Career MPT officials have been quoted in Japanese and foreign papers to the effect that Japan's telecommunications policy lags that of the U.S. and that reform is needed to bring it up with the rest of the world.[59] The current Minister of MPT, a Social Democrat, reportedly has given only lukewarm support to the plan while the SDP has opposed the breakup.[60]

Why has this transpired? Press reports indicate that there is a widespread feeling that NTT's overwhelming share of the local network has stifled competition, kept telecom prices high, unduly restricted the offering of new services, and hindered Japan's entry into the advanced information age.[61] The Council has recommended

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[59] Wall Street Journal, March 1, 1996.

[60] Wall Street Journal, March 1, 1996, A10.

[61] See, Financial Times, March 1, 1996. A recent report by JEI states that although three common carriers entered the market after the deregulation of 1985, by the end of FY 1994 they had obtained less than one-third of the market, mainly because NTT still monopolizes the local connections through which long

that NTT be split into a single long-distance company and two regional companies, and that the long distance company offer international and local telephone as well as cable vision, data and mobile communication systems. It has also stated that Japan's biggest international carrier, KDD, should be allowed to enter the domestic market.

If this plan is implement, which still remains unclear[62], regional companies will be prohibited from offering cable, long distance or international services in their own regions, but they will be able to do so outside of their own areas. This plan posits quite a different model than that seen in the U.S. following the breakup of ATT. In the U.S. case, the baby bells remained regulated and guaranteed access to local phone service. The Council's proposal suggest the possibility of greater competitive entry. Initially shares of the new regional entities would remain quasi-public although share ownership restrictions will apparently also be

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distance calls must originate and terminate. Payments to NTT for handling the local part of their long-distance calls comprise over 49 percent of their total revenues. And NTT has retained nearly a complete monopoly on local calling. NTT has also managed to keep
competitors out of the local market with its ability to undercut their charges. See, JEI Report No. 8B, March 1, 1996.

[62] Arguments against this plan have been raised by NTT's President. Specifically, he has argued that the plan does not guarantee that competition will intensify. Further, he argues that: the level of service could decline and costs rise, particularly as revenues from long-distance operations would no longer subsidize local service; and that Japan needs a flagship telecommunications carrier to represent it in international fora, among other arguments. See, JEI Report No. 8B, Id.

relaxed if the Council's recommendations are implemented. Foreign shares will be permitted to grow from the current ceiling of 20 percent to less than one-third.

The future structure that is envisioned is not, however, entirely unregulated. The plan recommends that MPT regulate the rates and conditions under which NTT regional entities can share their networks with competitors. Regulatory oversight will remain highly centralized and under the sole jurisdiction of the MPT. This is in contrast to the U.S. model where the FCC, the Department of Justice, courts and state commissions all provide various dimensions of oversight.[63]

At a minimum, it seems fair to infer from this brief summary of recent history that telecommunications is a sector in which regulatory policy has lagged well behind technological developments, and where a complex mix of domestic and international market pressures have obliged changes in regulatory structure.

3. Foreign Pressure

Much--perhaps too much--has been written on the role of "gaiatsu".

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[63] Another structural difference between U.S. and Japanese regulatory practices is reflected in the fact that MPT is headed by a politician, usually with little prior knowledge of telecommunications, while the FCC, in contrast, has often been chaired by an expert appointee.

Although I would argue that the role for gaiatsu has changed considerable over the last decade, it has unquestionably been an important agent of regulatory reform in the decade of the 1980's and remains so to some degree to this day.[64] The foregoing discussion of telecommunications is illustrative.

In numerous instances, international trade policy initiatives (both multilateral and bilateral) have obliged government officials to modify domestic regulations that have had intended and unintended consequences for foreign and new market entrants. Such issues have arisen repeatedly within the context of bilateral U.S-Japan trade friction.

In the 1988-1992 period alone, the United States and Japan entered into some 13 bilateral agreements. These included four agreements

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[64] I have argued elsewhere that foreign pressure has been especially effective when the following conditions are present: first, a globally competitive U.S. industry committed to penetrating the Japanese market and prepared, when necessary, to stay the course in negotiations that can become highly contentious. Second, a willingness on the part of the U.S. Government to apply bilateral and multilateral economic and political pressure on the Japanese Government for corrective measures. Third, the ability of the Japanese Government to deliver on those requests. Fourth, the existence of constituencies in Japan that see U.S. demands as in their economic interests or at least legitimate on their own terms. Fifth, the negotiation of measures that provide an effective context for on-going monitoring efforts by U.S. and Japanese government officials. Sixth, an identification of market access priorities that reinforce market trends. see, M.E. Janow, "Trading with an Ally" in G. Curtis, ed., The United States, Japan and Asia (New York: W.W. Norton, 1995).

covering Japanese Government internal procurement practices and procedures (supercomputers, satellites, construction services and computer hardware and software), five agreements covering Japanese government telecommunications standards, regulations and licensing procedures (third party radio and cellular telephone, telecommunications equipment and three agreements on international value-added telecommunication services), one agreement covering technical standards (wood products), and three agreements covering market access problems involving both government policies and private practices (amorphous metals, semiconductors and paper products).

There were also other initiatives such as the Structural Impediments Initiative that resulted in some changes to Japan's Large Scale Retail Store Law and Anti-Monopoly Act, and focused attention to internal practices with respect to land use, administrative guidance, customs procedures and other regulatory matters.

As formal border barriers to trade have been gradually reduced through multilateral trade negotiations, trade negotiations with Japan have come to focus increasingly on internal regulations that can distort trade and access to markets. Regulatory schemes that may have been designed largely with domestic concerns in mind are now being subjected to considerable international scrutiny.

Recent attention to Japan's treatment of software and sound recordings under its intellectual property laws (which are under MITI and MOE's jurisdiction), its allegedly discriminatory taxation of alcoholic beverages (which is under MOF's jurisdiction), allegations of inadequate enforcement of Japan's competition laws (which are under the JFTC's jurisdiction) and Japan's regulation of entry and products in its insurance markets (which are under MOF's jurisdiction) are but a few examples of the range of regulatory matters and agencies that are now subject to intense foreign scrutiny.

In some of the sectoral disputes between the United States and Japan, the United States sought remedial steps in the form of deregulatory actions by the Government of Japan--notable examples include telecommunications and standards, licensing and certification related agreements. More commonly, the U.S. Government sought to remove what it saw as discriminatory or anti-competitive biases in Japan's regulatory arrangements and the introduction of measures to increase administrative transparency, accountability, fairness and market access.

Viewed from a historical perspective, Japan in the 1990s has witnessed considerable regulatory reform and some economic deregulation. However, I share the view well expressed by John Haley that there is little evidence that the reforms reflect ideological changes with respect to the proper role of the state in

directing or managing the economy. Rather, reforms have been undertaken in response to market or other changes that domestic regulators could not ignore for one reason or another, rather than owing to any fundamental shift in economic policy making or ideology.[65]

C. The Current Deregulation Debate in Japan

As we turn now to look at the current climate for economic deregulation in Japan, we will consider the applicability of the Derthwick & Quirk factors to contemporary developments in Japan. Namely, in the Japanese context, is there perceived to be a powerful economic logic for further economic deregulation? If so, is this backed by extensive empirical analyses conducted by independent researchers? If not, does it matter? More generally, is there a convergence of elite opinion in favor of economic deregulation? Do agents of change hold powerful positions of leadership? Are there institutional mechanisms supportive of change? And finally, what role, if any, is foreign pressure playing or likely to play?

As we noted in the discussion of NTT reform, the traditional regulatory failure rationale for further economic deregulation and regulatory reform, which we have seen in the U.S. and elsewhere, is clearly part of the debate in Japan. Nor has this debate been

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[65] See, J. Haley, supra note 47 at 125.

limited to the telecommunications area. Even MITI commented in its 1995 White paper: " in order to reduce the domestic/external price gap we must correct the gap in productivity which is brought about by anticompetitive and inefficient regulations and trading practices."[66]

Several government agencies (such as MITI, EPA, and to some degree MOF) have produced and disseminated official documents stressing that economic deregulation would enable firms to move into more promising lines of business and consumers to enjoy the price benefits of yen appreciation.[67]

Publications issued both by private research institutes and business groups stress that deregulation would have the added benefit of reducing government intervention in the economy and detailed oversight of business activities. Deregulation has been cited by Japanese as well as foreign business leaders as offering

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[66] Tsusho Hakusho at 146.

[67] According to a 1995 MITI White Paper, for example, in November 1993 the cost of living in Tokyo was 41 percent higher than in New York. Durable goods were 36 percent higher, clothing 64 percent higher and food 62 percent higher. MITI also found that prices for traded goods, raw materials, intermediate goods, and capital goods were 30 percent higher than in the United States, 19 percent higher than in Germany and 46 percent higher than in South Korea. Services were found to be 51 percent higher than in the U.S., 96 percent higher than in Germany and 475 percent higher than in Korea. MITI, in 1995, widely disseminated the results of a survey that it had conducted of businesses which found that Japanese firms identified excessive government regulations as the main reason for price gaps in services.

the possibility of an improved business climate for new market entrants both foreign and domestic.

Is advocacy of economic deregulation new? No. The importance of deregulation for the Japanese economy is, in fact, not a new idea. As noted in the previous discussion, in the early 1980s, a government commission under the chairmanship of Toshio Doko, former chairman of Keidanren, stressed the importance of deregulation as a means of reducing government expenditures and rationalizing administrative procedures. In the mid-1980s, a commission under the chairmanship of Haruo Maekawa, former Bank of Japan governor, advocated deregulation as one of a number of measures designed to stimulate domestic demand and increase imports.

More recently the efforts of the Hosokawa administration, and in particular the interim and final conclusions of its Hiraiwa Commission report of late 1993, have again beemed a spotlight onto the issue of deregulation. These reports argued that deregulation was a major means of achieving an open, vital, consumer-oriented society in harmony with the world community[68].

The report made it plain that economic deregulation should be the rule not the exception. The interim report argued that institutional and programmatic approaches were needed. For example,

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[68] See, A Report by the Advisory Group for Economic and Structural Reform. December 16, 1993.

it argued that a deregulation headquarters needed to be established in the Cabinet and headed by the Prime Minister. Further, that an impartial governmental organization should be established by law to monitor implementation and issue recommendations to ensure that deregulation proved effective. The report attached a list of some 500 regulations and laws as examples of rules to be eliminated or revised. The report also stressed that:

> fundamental revisions, while placing a burden on certain portions of the socio-economic structure in the short term, are absolutely essential in the medium and long term to construct a free socio-economic system based on the principles of self responsibility and market mechanism[69].

After the Hiraiwa Commission report was issued, an Administrative Reform Headquarters was established in the Prime Minister's Office. Later, in June of 1994, a package of deregulatory measures was announced. In March of 1995, a five year deregulation package finally was released. (The government later decided to accelerate the timetable to three years). The March plan was comprised of some 1091 items in 11 areas, including distribution, housing, labor, and telecommunications[70].

Although long on lists of laws and regulations and relatively short on a targeted agenda, the plan did stipulate that its purpose was

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[69] See, Interim Report of the Advisory Group for Economic and Structural Reform, November 1993.

[70] Of these, the largest categories were as follows: some 239 items in the category of standards, certification and import processing; 168 items in transportation, 121 in distribution, 131 in hazardous materials, disaster prevention and public safety, 86 in housing, 53 in information and telecommunications, etc.

to improve the nation's quality of life by narrowing internal and external price differentials, to remove economic regulations in principle, to minimize social regulations in line with policy goals and to undertake a number of industry related deregulatory initiatives[71].

In light of these developments, can one say that elite opinion has converged in favor of further economic deregulation? Thus far, the answer is far from clear.

1. Pro-Reform Voices

Japanese constituencies that have voiced support for deregulation are diverse. In the business community, supporters include a number of major business groups such as Keidanren, Nikkeiren, and Keizai Doyukai. While the Hiraiwa Commission was meeting and after the release of its report, various business groups undertook a number of initiatives to keep the deregulation issue alive. For example, Keidanren conducted its own studies on the gains to the

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[71] See, JEI Report No 20A, May 26, 1995. With respect to specific actions, it indicates for example, that the GOJ would liberalize leased lines to public telephone networks, simplify procedures government imports of foreign cosmetics, change food labeling requirements showing the last date the food is edible rather than the date of production, allow brokers to sell insurance, lift restrictions on setting up gas stations in certain areas, end in October 1995 the maximum period for time deposits, ease car inspections, expand taxi firm's districts, review and revise the deregulation program annual, review by the end of FY 1997 the ban on holding companies, strengthen the JFTC and review by the end of FY 1999 the Large Scale Retail Store Law.

economy that would be accrued through economic deregulation[72].

Keidanren also released a paper in 1994 urging the government to adopt an approach to economic deregulation that incorporated principles of zero base, openness, and sunset, all principles drawn from U.S. experiences with regulatory reform. The "zero base" principle would require evaluation of all existing regulations. Under the "sunset" principle, all new regulations would be reviewed within five years, and the "open" principle envisioned that interested parties would be permitted to provide input whenever legislation with a regulatory impact was debated in the Diet. This would also require government officials to disclose drafts of cabinet and ministerial orders involving regulations[73].

Support for economic deregulation does not appear to be limited to the business community. Numerous Japanese academics have analyzed the sectoral effects of Japan's regulatory policies and some have advanced both specific and general deregulation proposals. The four major daily publications of Nikkei have written 7208 articles on deregulation over the last three years.

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[72] For example, one Keidanren report estimated that between FY 1995-2000, deregulation would result in aggregate increases in real GDP of some 177 trillion yen. Aggregate increases in jobs would amount to approximately 740,000 workers. See, Kisei Kanwa no Keizai Koka ni Kansuru Bunseki to Koyotaisaku, Keidanren. November 15, 1994.

[73] See, JEI Report 20A May 26, 1995.

A survey by Keidanren released in October, 1995, found that 94 percent of the respondents were interested in deregulation. Some 88 percent said that they would be able to accept an increase in "self responsibility" as a result of deregulation.[74] (The latter point is important because bureaucrats often argue that the public is in favor of deregulation until it affects them adversely, at which point, they seek government assistance and redress).

All major political parties have made further economic reform and deregulation as part of their official platforms. To this extent, elite opinion has converged in favor of further regulatory reform and economic deregulation. Yet, there appear to be a number of obstacles in the way of further economic reform and deregulation. Let us briefly identify those challenges.

2. Challenges to Deregulation

a) Opponents

First, deregulation has its detractors and some have been quite vocal in their opposition. Less public, but nonetheless effective, opposition from within and outside of the government has reportedly quashed any number of specific proposals that had surfaced from within the government and from outside sources.

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[74] See, The Japan Times. October 10, 1995.

Some labor groups have stepped into the fray, expressing concern about the employment consequences of deregulation. An unidentified anti-deregulation group last year penned an article in a prominent Japanese magazine entitled " A Nightmare Called Deregulation" which purported to examine U.S. experiences with deregulation in the airlines, trucking and financial services sectors. This article, which received a lot of attention, argued that the U.S. experiences resulted in job losses, exacerbated income disparities, and failed to create new industries or jobs.[75] Those assertions were then rebutted by several prominent Japanese academic economists.[76]

Some ministries and agencies, notably MITI and the EPA, appear to be advocates of deregulation. However, other government ministries are resisting deregulation on specific and general grounds. Some consumer groups have opposed relaxation of restrictions, on health and safety grounds.

As a result of this interplay between supporters and opponents, a number of the proposals put forward by the Hiraiwa Commission were watered down. For example, bureaucrats resisted the notion of creating a new powerful impartial organization whose mission would be to map-out and monitor the implementation of deregulation proposals. Clearly, they saw such an organization as trespassing on

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[75] See, Bungei Shunju, August 1994.

[76] See, Nakatani Iwao and Ito Takatoshi, Economist August 30, 1994.

their own bureaucratic turf. Such an organization was eventually created, but it is being coordinated out of the Prime Minister's office.[77] Even supporters of deregulation have issued stinging critiques of the "wishy washy, something-for-everyone-but-not-enough-for anyone approach" to deregulation that has come out of the government.[78]

b) An Uncertain Political Climate

A second and related challenge to economic deregulation is the current political climate. Especially during this period of political transition it is unlikely that politicians will voluntarily raise those economic issues that polarize voters and that are not perceived by the public as requiring urgent attention. The current "jusen" situation is seen as a crisis requiring corrective measures. It is not clear whether important political leaders will use their scarce political capital to take on other economic reform issues that may be perceived to be of a less urgent nature.

The current Prime Minister, Ryutaro Hashimoto, is widely acknowledged by Japanese bureaucrats to be a decisive politician,

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[77] More recently, a deregulation subcommittee has been established in April, 1995. Headed by the chairman of IBM Japan, Takeo Shiina, the committee holds hearings and discusses proposals on some 46 items identified by the government.

[78] See, Nakatani Iwao, Economic Eye, Autumn 1994.

especially well versed in economic matters. His political future is far from assured, public support for economic deregulation is obviously mixed, and the intensity of his commitment to wide-ranging economic reform and deregulation is ambiguous.

Indeed, although Japanese politics underwent a dramatic development when the LDP dominance in the Diet came to an end in the summer of 1993, and although there is widespread public dissatisfaction with Japanese politics, observers of Japanese politics are divided over the degree to which substantive policy issues are, or are not, likely to dominate the political process. I am fairly pessimistic in this regard. The major parties, the LDP and the Shinshinto, are both conservative parties. Both are striving to appeal to the same body of voters, and both are gearing up for the first major election under the new rules. This means that both parties are stressing very similar and rather amorphous campaign themes: the need for reform, growth, deregulation and change. A bold and specific timetable on economic deregulation does not appear to be a highly visible part of the program.

c) An Ambiguous Public Mandate for Change

A third and related challenge to economic deregulation and regulatory reform is the absence of strong public sentiment insisting upon the necessity of such reforms.

Voter dissatisfaction with Japan's politicians and bureaucrats may be pronounced, but still there is no pervasive sense of crisis. According to an August 1995 opinion poll conducted by the Prime Minster's Office, 72.7 percent of the respondents said that they were content with their current standard of living. This survey has been conducted annually by the government since 1958; the latest survey revealed public satisfaction with their living conditions to be at an all time high.[79]

If this really is an accurate window into public attitudes, then one might well question whether there is really sufficient public unhappiness with the current state of economic and political affairs to produce the requisite pressure on both politicians and bureaucrats to cause them to depart significantly from current practices.

d) Structural Constraints

A variety of structural features of Japanese policymaking institutions and their role in regulatory reform suggest a very different dynamic than that described by Derthwick and Quirk. Several different aspects of that dynamic are worth brief comment here: the entrenched position of bureaucrats, the limited role of the courts, and the historically weak role of competition policy enforcement.

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[79] See, Yomiuri Shimbun, August 21, 1995.

Under usual circumstances, bureaucrats exert a high degree of control over policy formulation. Expertise on economic and other policy issues resides primarily in the bureaucracy. Historically, virtually all legislation has been drafted by bureaucrats and goes to the Diet through the Cabinet rather than through member bills.

Interpellations from the Diet usually are defended by senior bureaucrats. Political appointees to ministries are very few in number--usually only the Minister and the Parliamentary Vice Minister--and Ministers traditionally have had very little say over personnel decisions within a Ministry. Although some LDP policy committees have built up considerable expertise on selective policy issues, rarely have such political organs been the central locus of legislative initiatives. Even though some Japanese politicians argue that politicians must exert more control over the bureaucracy and become better educated on policy matters, the status quo shows little signs of disappearing anytime soon.[80] Also, there appear to be few mechanisms within the Diet or elsewhere analogous to the power and independence of Congressional Committees and their staffs which might serve as a central fulcrum for ideas and policy initiatives. Professor Gerald Curtis has observed that the U.S. bureaucracy is weaker, and control by Congress over policy making stronger, than in any parliamentary system. In some ways, Japan is

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[80] Ichiro Ozawa, for example, has suggested that government ministries should be infused with politicians and politicians need to assume more responsibility over policymaking. See, Ichiro Ozawa Blueprint for a New Japan, 1994.

on one end of this spectrum and the United States the other.[81]

Some analysts have concluded that politicians in Japan do not matter a great deal because the bureaucrats are really in charge of economic matters and politicians are little more than window dressing. Subscribers to this point of view tend to assert that bureaucrats and politicians are captive to special interests, and therefore it is unrealistic to expect meaningful reforms to come out of the bureaucracy let alone out of political circles. I for one think this perspective fails to pick up nuances important to Japan's political economy.

In my former experience as a trade negotiator for the U.S. Government, I observed that most of the regulatory reform proposals that arose in the context of trade disputes emanated from within the bureaucracy itself--albeit in the face of foreign pressure. Political intervention, however, often was critical. Why is this? Career civil servants often appear to have difficulty reaching agreement on issues when the proposed policy matter is either strongly opposed by domestic private interests or by other bureaucrats. Resolving problems appears to be especially difficult when issues cut across the jurisdiction of several ministries. In such circumstances, Japan's politicians have often played an important role in brokering compromises. This dynamic has been

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[81] See, Gerald L. Curtis Japanese Politics in Comparative Perspective, August 1995.

important in the context of trade issues between the United States and Japan, but it has also arisen in the context of domestic economic policy disputes as well.

At the current time, with the power base of politicians is so notably in flux, their ability to broker compromise between competing interests is more limited than in the past.

If this is so, is judicial review of administrative action or private litigation the more likely to drive economic deregulation and regulatory reform? Japan's legal tradition, at least since the Meiji era, has been to draft extremely general language in the body of legislation, thereby leaving the bureaucracy wide latitude within which to exercise its discretion depending on circumstances prevailing at the time. Informal and nonbinding administrative guidance also has been characteristic of much of Japan's approach to government oversight of economic activity.

There is an enduring, though not uniform, tradition of heeding informal suggestions put forward by government officials. The reasons for this are diverse. Some of these reasons include: because enabling legislation might be assumed to exist (or could be created); because retaliation for non-compliance is feared through bureaucratic exercise of collateral powers; because administrative guidance affords both sides a desired degree of flexibility; or because recourse to judicial review has been so weak that private

parties are reluctant to challenge a bureaucrat's authority.

Indeed, judicial review of administrative guidance has been limited. In order for administrative actions to be reviewable they must constitute an administrative disposition (shobun) or other exercise of public power. Since administrative guidance in Japan is by definition an informal process, it tends to fall outside of this definition.[82]

In the Structural Impediments Initiative (SII), the Japanese Government committed itself to put all administrative guidance in writing and to only use it in exceptional circumstances. While in government service I negotiated that SII language, and I have occasionally asked Japanese officials in the intervening years whether administrative guidance is now routinely written down and published. The question is usually met with some bafflement. A number of savvy officials have responded to the question, perhaps tongue in cheek, that administrative guidance is now entirely a thing of the past--except in areas where they are obliged to encourage domestic firms to voluntarily increase their purchases of

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[82] F. Upham, supra note 48. Scholars who have looked at this question in some detail tend to conclude that Japanese courts have reached the merits in reviewing administrative guidance in only a small class of cases. Agency action tends to be upheld so long as it constituted a good faith attempt to encourage and implement negotiation, attempting to resolve conflicts among the various affected groups. See, for example, Michael Young, infra note 83 and Jonathan Weinburg, "Broadcasting and the Administrative Process in Japan and the U.S." Buff. Law. Rev. Fall 1991.

foreign goods. If these responses are representative, there is little evidence that that particular SII undertaking is common knowledge or being implemented.

It also seems that domestic interests are only infrequently challenging Japanese government agencies for their continued use of informal measures. Why is this so?

Part of the answer lies in the flexibility that administrative guidance affords to both sides. It is probably a mistake to see administrative guidance as simply a one sided process, favored by bureaucrats and resented by Japanese business executives. It is more likely the case that administrative guidance is favored when the affected interests benefit from it and resented when it obliges them to act or refrain from acting as they would otherwise prefer. Administrative guidance affords a high degree of flexibility to both government officials and private parties and carries with it less accountability as compared with more formal measures that might either elicit public scrutiny or require legislative authority.

It is probably also a mistake to view Japanese bureaucrats as necessarily pro-active and decisive regulators. Numerous regulatory and trade problems have arisen precisely because regulators delegated important decision-making to the affected interests. Professor Michael Young, in an important article on

administrative guidance written some years ago put it well:

> administrative organs in Japan often seek to enshrine bargaining and negotiation between parties as the principle device for allocating regulatory burdens. Instead of relying on agency determinations, Japanese administrators have turned to enforced bargaining and negotiation. Administrators reallocate bargaining power between the parties so as to assure serious negotiations, but then distance themselves from the process, thereby allowing parties themselves to make the difficult determinations.[83]

Although Professor Young's article is now over a decade old, we continue to see contemporary expressions of his characterization of Japanese regulatory methods.

A well-publicized example in the retail sector is the Large Scale Retail Store Law (LSRSL). This law was designed to protect small and medium size independent merchants from competition by large scale chain stores[84]. Professor Frank Upham has argued that the LSRSL and the manner of its implementation may reflect a regulatory regime designed largely in response to such domestic social and political interests, where domestic regulators delegated its power to small private interests. Given the way the law worked in practice, large retailers had to purchase the right to open a store

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[83] See, Michael K. Young, "Judicial Review of Administrative Guidance: Governmentally Encouraged Consensual Dispute Resolution in Japan", 84 Colum. L. Rev. 923 (1984).

[84] The domestic law came under attack by larger domestic firms seeking to establish chains, it also became a symbol of a structural constraint to market access when foreign firms tried to enter the market and could not because of the law and its manner of implementation. See, Frank Upham, "A Tentative Model of Japanese Regulatory Style", draft paper prepared for the Festschrift for Professor Koichiro Fujikura, September 1994.

from small retailers. Professor Upham argues that that right was created not by law but rather by the government, through its de facto decision to delegate authority to local retailers. Whether this practice came into existence by design or accident, this regulatory scheme also contributed to the formation of cartels on the national, regional, and local levels.[85] It also thwarted entry by those large firms (including foreign firms) that were seeking to sell in the local market.

In recent years, regulatory methods of Japanese government agencies have become the focus of international attention and domestic public dissatisfaction and debate. There have been a number of scandals involving procurement practices in the construction and transportation sectors that appear to have increased public interest in enhanced transparency and accountability of government actions. The passage of the long-studied Administrative Procedures Law (APL) is one expression of this development. An intriguing question for the future is whether this law will actually be used, either by industries or individuals, to challenge formal as well as informal agency conduct. The APL provides only limited coverage over informal measures such as administrative guidance; it will be most interesting to see whether this proves a subject of domestic debate in Japan.

Another topic of great importance is the future role competition

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[85] See, Id., for the elaboration of this point.

policy will play in Japan.

The JFTC, which administers the Anti-Monopoly Law, has had an anomalous position in Japanese society since its inception in 1947. In the early postwar years there was a great deal of opposition to its very existence, and few expected it to gain authority or legitimacy. Gradually it has attained some of both, but this has fluctuated over the years and has often depended on the personal dynamism of its chairman.

For most of the postwar period, the JFTC has been under intense pressures for inaction from politicians and other government agencies. The long standing institutional tension between the FTC and MITI erupted into open hostility in two famous cases: the merger of Yawata and Fuji Steel in 1969, and the allegations by the FTC in 1974 that member companies in the Petroleum Industry Association had illegally restricted supply even when doing so at MITI's behest. The first case helped to establish the principle that the JFTC was the body that had a right to pass judgment on the desirability of proposed mergers. In the oil case, the FTC actually filed charges of illegal activity to restrict production and fix prices and oil executives contended that their actions were legitimate because they were based on administrative guidance. A court judgment in 1980 ruled that MITI lacked the authority to use administrative guidance to induce firms to take actions that were otherwise illegal. The decision although extremely important, it

still left many unanswered questions as to how much latitude MITI could take.

Open hostility between the JFTC and MITI now appears to be much reduced. Indeed, MITI officials now argue that MITI is a serious proponent of economic deregulation and regulatory reform and has itself become a champion of more vigorous enforcement of competition laws. At the same time, MITI's handling of certain sectors that are under its direct jurisdiction has, on occasion, been curious.

In 1993, in the face of much international criticism of business practices in Japan's glass industry, the JFTC conducted a survey of competitive conditions in that market and concluded that while the Anti-Monopoly Act (AMA) had not been violated, certain business practices were problematic. MITI, for its part, then issued guidelines identifying what in its opinion constituted good business practices. It also urged Japanese glass manufacturers to make certain adjustments in their business dealings, especially with regard to fidelity rebate schemes used by glass manufacturers with their affiliated distributors. These MITI guidelines presumably had no legal enforceability but were designed to supplement the findings of the JFTC and to alert the domestic industry to certain changes in business practices that MITI wanted to see materialize. In this somewhat curious fashion, the glass case may provide a "window" into the new rapproachment between the

two agencies.

Several other areas that may provide some insight into the future role of JFTC enforcement as well as JFTC's relations with other ministries are exemplified by JFTC's stance on exemptions and administrative guidance. Existing exemptions under the AMA are currently being "studied" by the JFTC. In years past MITI argued forcefully that most existing exemptions, especially those covering industries under their purview should be maintained.[86] It will be fascinating to see whether MITI is now prepared to accept the removal of AMA exemptions. In addition, the JFTC has in recent years periodically criticized other ministries, including MITI, for using administrative guidance. Recently, as part of the government's deregulation campaign, the JFTC has been charged with the difficult task of ensuring that government agencies do not undercut deregulatory measures through informal measures such as administrative guidance. JFTC's efforts in this challenging area are worth careful examination.

The perceived inadequacies of the JFTC in its enforcement of Japan's competition laws has become a source of international trade tension. Recent years have brought some positive developments for those who believe than an effective competition regime would benefit the Japanese economy and enhance opportunities for foreign

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[86] If I recall properly, the AMA exemption for barber shops was eliminated without MITI opposition. It may now be possible to get a (somewhat) cheaper haircut in Japan.

firms to access the Japanese market. Notable developments in this regard include: increases in the JFTC's budget and personnel; certain amendments to the AMA that increase penalties for anticompetitive conduct; increased enforcement actions; and certain procedural improvements aimed at reducing obstacles to private litigation.

e. What Role Foreign Pressure?

The Japanese Government, to its credit, has invited all interested foreign parties to comment on its economic deregulation proposals. It also has permitted some foreign interests to testify before certain committees studying deregulation. The U.S. and the E.U. governments have put forward detailed comments.[87]

Economic deregulation is one area where foreign interests and domestic interests can overlap. The interests of foreign companies and governments on the one hand, and Japanese new to market firms and consumer on the other, often are complementary. Deregulation offers a potential vehicle for channeling that complementarity.

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[87] The submissions differ in a number of respects. The U.S. government commentary contains extensive discussion of broad policy approaches that are seen as facilitating the creation of more open, competitive and transparent regulatory regimes. The U.S. Government also submitted an extensive list of regulatory reforms that it believes should be undertaken on a sectoral basis. Most of these are problems that have long been identified by the U.S. The submissions of the European Business community focus, almost exclusively, on specific sectoral problems arising from regulatory practices in Japan.

Foreign firms seek expanded access to the Japanese market and the removal of regulatory constraints that hamper such access. To the extent that such regulations raise costs to consumers and also thwart entry for new-to-market domestic firms, foreign and domestic interests are likely to share an interest in further deregulation and regulatory reform. This may increase the receptivity of domestic interests in subjects of reform identified by foreign parties. As noted earlier, in my view, historically foreign pressure has been the most effective when it has echoed the need the change identified by powerful domestic interests.[88]

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[88] In fact, there have often been important and vocal supporters within Japan for trade or regulatory reforms identified by the U.S. or other governments. For example, during the beef and citrus negotiations there were editorials in Japanese papers suggesting that concessions to the United States would benefit the interests of consumers and pointing out that the quota system provided undue profits to those handling the quotas at the expense of the consumer. In 1983, a group of Japanese economists proposed liberalization of agricultural products including beef and citrus. In 1985, the Maekawa Report called for more opening of the agricultural market emphasizing the importance of consumer views. Even the difficult issue of rice liberalization eventually produced domestic supporters. In early 1993, more than a hundred intellectuals and experts signed an advertisement calling for acceptance of tariffication of rice. Support within Japan for U.S. trade objectives was especially evident during the Structural Impediments Initiative (SII). This is in one sense not surprising because U.S. negotiators took great pains to try and identify issues that would benefit U.S. firms and yet were already contentious domestic issues in Japan. For example, when the U.S. identified the Large Scale Retail Store Law as an impediment to new market entrants seeking to establish larger retail chains, there were already Japanese retail chains pressing for reform. A poll by Asahi Shimbun in May 1990 showed some 58 percent of the respondents in favor of reducing regulations over large stores.

Any number of steps could yet be taken by private interests or foreign governments to reinforce this complementarity of interests. Thus far, private or public initiatives have been limited but on-going. Separate bilateral consultations on economic deregulation between the U.S. and Japan and the E.U. and Japan have occurred. U.S. and European Chambers of Commerce have prepared fairly detailed commentary outlining specific areas where economic deregulation or reform would prove advantageous to foreign firms. In this sense, it is not only U.S. firms that have an interest in further economic deregulation and regulatory reform but indeed all foreign firms that are seeking expanded access to the Japanese market.

At the current time, the U.S. government, for its part, does not seem to be putting much negotiating energy into bilateral consultations on economic deregulation. The reasons for this are not fully known, but it is likely that such negotiations are not seen as likely to produce tangible results in the near term.

On a more optimistic note, the subject continues to attract domestic and international attention along many different dimensions. The OECD, for example, has undertaken a number of studies on country experiences with economic deregulation and regulatory reform. It has several working groups examining sectoral and other effects. Those discussions may serve the useful purpose of alerting member countries to global trends. In the past, the

need to keep up with world trends has offered Japanese officials a needed rationale for undertaking reforms that were unpopular at home.

IV. Concluding Observations

Economic deregulation and regulatory reform is now a global phenomena. Traditional rationales for regulation have come to be challenged for a variety of reasons. Inefficiencies produced by earlier methods and justifications for regulation have become increasingly evident as market conditions have altered. But, as noted at the outset of this paper, while economic deregulation and regulatory reform is now widespread, the process is far from a linear nor predictable one across nations.

In Japan as well, initial rationales for regulation have proven in some areas to impose greater costs than benefits for both the regulated sector and the economy as a whole. In this sense, the Japanese experience with economic deregulation and regulatory reform shares some common elements with developments elsewhere in the world. Regulation in Japan still, of course, has its unique features which are producing their own particular dynamic over time.

Diverse and powerful interests within Japanese society now see economic deregulation and reform as necessary for Japan's continued

economic growth and vitality. These groups are more visible and vocal than in years past. Economic deregulation and regulatory reform also is being cast by important government and private sector groups as a competitive necessity and an international responsibility.

The perspectives offered in this paper on the forces driving regulatory reform in the postwar period has suggested that domestic and international market and technological factors have converged to necessitate on-going regulatory reforms. The costs to the Japanese economy of failing to continue the process of economic deregulation, and the domestic and international pressures in favor of economic deregulation seem to be sufficiently great that further reform initiatives are likely.

This being said, the institutional mechanisms that exist in the U.S. and elsewhere to drive reform--or tolerate it--do not appear to be fully available in Japan. For example, Japanese political leaders do not seem to have the institutional power base, nor perhaps the political will or public mandate to push through comprehensive reforms. To date, it is not fully clear that elite opinion has converged in support of economic deregulation. Regulatory agencies have less of a tradition of independent leadership than has been the case elsewhere. There have been no examples of deregulation resulting in the elimination of regulatory agencies nor, more importantly, a broadening or redefining of

regulatory oversight to include more than the existing regulatory authority. It is unclear whether or not academic researchers at major universities are producing policy-relevant sectoral analyses that are having a defining impact on the policy process. Japanese courts have not historically played a visible role in obliging agencies to avoid arbitrary and capricious regulations or have themselves been major agents of regulatory change. And, competition policy enforcement, though certainly more visible than in years past, remains less vigorous than in other advanced industrial economies.

My own expectation, therefore, is that economic deregulation will be a protracted and uneven process in Japan.

These broad generalizations of course only provide a small window into the political economy of deregulation in Japan. We have not,of course, addressed the specific reforms that are likely to be introduced, the lessons learned from foreign experiences with deregulation, nor the sectoral priorities that are likely to predominate at any given period. Much will depend on the perceived costs and benefits of economic deregulation and regulatory reform on a sectoral basis.