U.S. Rep. Sander Levin
Ways and Means Committee Ranking Member

U.S.-JAPAN AUTOMOTIVE TRADE: PROPOSAL TO LEVEL THE PLAYING FIELD

For generations, the Japanese auto market has been closed to virtually all imports from all countries. As a result, U.S. automakers have been shut out of Japan, and forced to compete on an unlevel playing field in all other auto markets, as Japanese automakers have leveraged their advantages at home into advantages abroad. Negotiations to open the Japanese auto market have repeatedly and totally failed in the past. We therefore need to take a new and more assertive approach to the problem. In particular, the United States should condition any further opening of its already largely open auto market on an opening of the Japanese auto market. The following proposal is an attempt to address this longstanding problem.

I. <u>U.S. Tariff Phase-Out: Based on Reciprocal Market Access</u>

The U.S.-Japan Motor Vehicle Trade Terms of Reference of April 12, 2013 provides that the United States will reduce its tariffs on Japanese cars and trucks (currently set at 2.5% and 25%, respectively) according to the longest tariff phase-out period in TPP. But there is no certainty as to what that period will be. Moreover, if history is any guide, there is no guarantee that Japan will open its market before the end of that period.

To address these problems, in addition to the type of phaseout reflected in the Terms of Reference, there needs to be:

(1) a phaseout of the tariff sooner if Japan's import penetration rate[1] increases substantially from its current rate, as an incentive to open Japan's market to imports; and

(2) a lower reduction of the tariff if Japan's market remains substantially closed.

Specifically, tariffs shall be phased out in the following manner:

[1] The import penetration rate reflects imports from <u>all</u> countries into any given market. Japan's current import penetration rate in 2012 was 5.9% , compared to an OECD average of 58% and a U.S. import penetration rate of 47.9%.

Tariff Phase-Out

1. Base Tariff Phaseout

(Reflecting April 12, 2013 U.S.-Japan Motor Vehicle Trade Terms of Reference and with Backload)

Year	U.S. Auto Tariff	U.S. Truck Tariff
0-25	2.5%	25%
26	2.0%	20%
27	1.5%	15%
28	1.0%	10%
29	0.5%	5%
30	0.0%	0%

2. Earlier Phase-Out If Japan Opens Its Market Before Year 25

Japan Import Penetration	U.S. Auto Tariff	U.S. Truck Tariff
Current Rate: 5.9%	2.5%	25%
When reaches 20%	2.0%	20%
When reaches 25%	1.5%	15%
When reaches 30%	1.0%	10%
When reaches 35%	0.5%	5%
When reaches 40%	0.0%	0%

3. Lower Reduction If Japan Keeps Its Market Closed

If Japan's import penetration in year 25 is less than one half the OECD rate (i.e., 29%), then the rate of the U.S. tariff phase-out will be cut in half – i.e., the U.S. tariff will phase down, in equal installments, to 1.25% for autos and 12.5% for trucks rather than to 0.

For example, if in year 25, Japan's import penetration is 20%, it would face a U.S. auto tariff of 2.0% and a U.S. truck tariff of 20% in that year. These rates would then phase down to 1.25% for autos and 12.5% of trucks according to the following schedule:

Year	U.S. Auto Tariff	U.S. Truck Tariff
26	1.85%	18.5%
27	1.70%	17.0%
28	1.55%	15.5%
29	1.40%	14.0%
30	1.25%	12.5%

NOTE: Auto parts shall be subject to a similar phase-out regime.

II. Ending Currency Manipulation

While many non-tariff barriers have kept the Japanese auto market closed for decades, currency manipulation has been one of the most significant and persistent. And it affects all product and services markets, and has been a problem in other TPP countries and throughout the Asia-Pacific region. Currency manipulation not only makes it more difficult to enter the Japanese market, it also gives Japanese producers an unfair competitive advantage in the U.S. market and in third-country markets, making it even more difficult for the United States to reach its objective of doubling exports over five years.

All parties to the TPP agree to the following four obligations concerning exchange rates:

- Core Obligation to Avoid Exchange Rate Manipulation. Each TPP Party shall avoid manipulating exchange rates to gain an unfair competitive advantage over other TPP Parties. In determining whether a Party has manipulated an exchange rate, a panel would consider the same evidence the IMF considers pursuant to Article IV of the IMF Articles of Agreement (see 2012 and 2007 Executive Board Decisions, paras. 22 and 15, respectively). These include:

    - Protracted, large-scale intervention in one direction in the exchange market;
    - Excessive and prolonged official or quasi-official accumulation of foreign assets; and
    - Large and prolonged global current account surpluses.

  As part of the agreement, the TPP parties will establish specific benchmarks by which to determine whether the obligation has been breached (e.g., foreign asset accumulation may be excessive if it exceeds all of the Party's external debt coming due within the next year, the so-called "Greenspan-Guidotti rule").

- Consultations regarding Other Actions that Weaken an Exchange Rate. The TPP Parties agree to consultations where a Party believes another Party has taken action with the purpose and the effect of weakening its currency (e.g., official statements from the other Party's that its currency is overvalued; the use of fiscal or monetary policy to achieve a particular exchange rate target), particularly where the Party has a significant current account surplus or a history of exchange rate interventions.

- Manipulation by Non-Parties. The TPP Parties agree to take coordinated action to address currency manipulation by non-parties.

- Transparency. Each TPP Party agrees to transparency in its exchange rate practices. This commitment includes obligations: to disclose data on its foreign exchange interventions and on its accumulation of official and quasi-official assets; to subscribe to the IMF's Special Data Dissemination Standard on reserve transparency; and to report to the IMF's Currency Composition of Official Foreign Exchange Reserves database.

These obligations are general in nature, rather than specific to the auto sector.

The core obligation to avoid exchange rate manipulation, and the transparency obligation, would be subject to the normal dispute settlement mechanism of the TPP agreement, with two modifications for exchange rate disputes: (1) the panelists would be required to have expertise concerning exchange rate issues; and (2) the timeline for resolution of the dispute would be expedited.[2]

Finally, as the TPP negotiations proceed, Japan should take corrective measures concerning its accumulated reserves, particularly given that the yen has depreciated nearly 30 percent since October 2012. Japan claims that, with its expansionary monetary policy, it is not targeting the exchange rate for competitive purposes. But in the recent past, Japan clearly has targeted its exchange rate for competitive purposes, intervening massively in the foreign exchange markets and accumulating over $1 trillion in foreign exchange reserves. Now is the time for Japan to begin selling those excessive reserves. Doing so would help to address the undervalued yen and would serve as a gesture of goodwill that Japan's days of currency manipulation are behind it.

III. Current and Future Non-Tariff Barriers (Other than Currency Manipulation)

Existing Barriers. Japan will agree to eliminate all existing non-tariff barriers in the auto sector, including auto parts.[3] These barriers have included: a discriminatory system of taxes; onerous and costly vehicle certification procedures for imported automobiles; a complex and changing set of safety, noise, and pollution standards, many of which do not conform to international standards and add significant development and production costs for automobiles exported to Japan; an unwillingness by Japanese dealerships to carry foreign automobiles and insufficient enforcement of competition laws to address anti-competitive practices; zoning restrictions that make it difficult, if not impossible, to establish new dealerships in important markets; and exclusionary consumer preferences shaped by decades of government policies directed at promoting the national car companies.

Future Barriers. Japan will agree to effective mechanisms to avoid adopting new non-tariff barriers, and to immediately address new concerns with existing measures.[4] For example:

- Proposed Measures. If the United States objects to a proposed measure[5] and establishes *prima facie* evidence to a dispute settlement panel[6] that the measure is either inconsistent

[2] U.S. FTAs generally provide for the reinstatement of MFN tariffs in the event of a breach of the agreement. That same remedy would apply in the case of currency manipulation. However, with respect to trade in motor vehicles, if the U.S. tariff has not yet been eliminated, the period of time before the tariff is eliminated would be extended.

[3] As envisioned in the U.S.-Japan Motor Vehicle Trade: Terms of Reference, a special accelerated dispute settlement procedure allowing for the reimposition of the current MFN tariffs would apply in the auto sector. As a result, failure to eliminate a non-tariff barrier would result in a "snapback" to the current tariff level of 2.5% for automobiles, or 25% for trucks. This snapback mechanism would also apply in the case of currency manipulation (a non-tariff barrier), to the extent that the currency manipulation involves trade in automobiles; if the snapback provision cannot be implemented because the U.S. tariff has not been eliminated, the period of time before the tariff is eliminated would be extended for a period equivalent to the duration of non-compliance.

[4] These mechanisms include, but are not limited to, those found in the U.S.-Japan Motor Vehicle Trade: Terms of Reference (e.g., opportunities for input throughout the process of developing and implementing regulatory measures; reasonable periods to comply with new regulations; and post-implementation review of regulations).

[5] A process will be established through implementing legislation that would enable stakeholders to request that the United States object to a measure. If the United States decides not to object, it will be required to explain its decision in the Federal Register.

with the TPP agreement or otherwise nullifies or impairs any benefit accruing to the United States directly or indirectly under the agreement, Japan will not implement the measure until the matter is resolved either through negotiations or dispute settlement.

- Non-Violation Nullification and Impairment. If a proposed measure is implemented and, although not inconsistent with the agreement, results in the nullification or impairment of the benefits of the agreement to the United States, the United States would be authorized to suspend its concessions in an amount equivalent to the level of nullification or impairment, or to utilize the "snapback" provision (or, if the snapback provision cannot be implemented because the U.S. tariff has not been eliminated, to extend the period of time before the auto/truck tariff is eliminated).

[6] The agreement would provide for expedited procedures for judging such issues.