

GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED
L/5623
2 March 1984
Limited Distribution

PANEL ON JAPANESE MEASURES ON IMPORTS OF LEATHER

Report of the Panel

I. Introduction

1. At the request of the delegation of the United States the Council agreed to establish the Panel on 20 April 1983, and authorized the Chairman to draw up its terms of reference and to designate its chairman and members in consultation with the parties concerned (C/M/167, item 12).
2. On 12 July 1983 the Council was informed that following such consultations the composition and terms of reference of the Panel were as follows (C/M/170, item 14):

Composition

Chairman: Mr. M. Huslid
Members: Mr. D. Jayasekera
Mr. H. Reed

Terms of reference

"To examine, in the light of the relevant GATT provisions, the matter referred to the CONTRACTING PARTIES by the United States (L/5462), relating to restrictions maintained by Japan on the import of certain semi-processed and finished leather, and to make such findings, including findings on the question of nullification or impairment, as will assist the CONTRACTING PARTIES in making recommendations or rulings, as provided for in Article XXIII:2."

3. The Panel met on 26 September, 15 November and 13 December 1983, 17 January, 2 February and 9 February 1984.
4. In the course of its work the Panel consulted with the delegations of Japan and the United States. Arguments and relevant information submitted by both parties, replies to questions put by the Panel as well as all relevant GATT documentation served as a basis for the examination of the matter. In addition, in accordance with requests they had made in the Council, the delegations of Australia, the European Communities, India, New Zealand and Pakistan were invited and heard by the Panel. The delegations of Australia and New Zealand also submitted written briefs.
5. During the proceedings the Panel provided the two parties adequate opportunity to develop a mutually satisfactory solution in the matter before it.

6. The Panel urged the parties to respect the need for confidentiality and requested them not to release any papers or make any statements in public regarding the dispute. The same was impressed upon the five other delegations when they appeared before the Panel.

II. Factual aspects

7. The case before the Panel concerned import restrictions maintained by Japan on the following lines in the Japanese tariff:

- 41.02-2 Bovine cattle leather and equine leather, dyed, coloured, stamped, embossed or other, other than parchment dressed (excluding chamois-dressed leather or patent leather; including cattle, horse, buffalo, calf and kip leather, and including both finished leather and semi-tanned leather which includes "wet blue" leather, i.e. semi-processed chrome-tanned leather, shipped wet, purchased by tanners for further processing);
- 41.03-2-(1) Sheep and lamb leather, dyed, coloured, stamped or embossed, other than parchment-dressed (excluding chamois-dressed leather or patent leather);
- 41.04-2-(1) Goat and kid leather, dyed, coloured, stamped or embossed, other than parchment dressed (excluding chamois-dressed leather or patent leather).

8. Article 52 of the Foreign Exchange and Foreign Trade Control Law (Law No. 228 of 1949, as amended), requires importers of products specified under the import quota system to obtain import licences where the Government has so provided by Cabinet order. This authority was implemented in the Import Trade Control Order (Cabinet Order No. 414 of 1949). The Import Trade Control Regulation (MITI Ordinance No. 77 of 1949) sets forth specific import licensing procedures. Import quotas on leather were imposed under the authority of the above legal provisions in 1952 and still remain in force.

9. Allocation of the global leather quota is the responsibility of MITI which practices a combination of two methods to allocate quotas: (1) the "trader" quota formula based on import records and available to selected firms which have a history of importing; and (2) the "user" quota formula, used to distribute quotas to selected end-users and/or firms that represent them. In the course of the work, Japan explained further the allocation system and its implementation for finished leather as well as wet-blue chrome (see below).

10. A previous Article XXIII complaint by the United States concerning this matter was withdrawn upon the conclusion on 23 February 1979 of a bilateral understanding between the United States and Japan, which came into effect on 1 April 1979. At that time, the two parties "reserved their rights under the GATT; should the conclusions of the bilateral consultations not be put into practice to the mutual satisfaction of both governments, it was understood that the matter may be further subject to GATT proceedings" (BISD 26S/320-321).

11. New quotas for bovine and equine leather as well as bovine and equine wet blue chrome were established in Japanese fiscal year 1979 in addition to the quotas existing previously. These new quotas were allocated to countries with a record of substantial supply of hides to Japan, based on the share of supply of raw hides, through bilateral consultations with the countries concerned.

12. The bilateral understanding between Japan and the United States referred to in paragraph 10 expired on 31 March 1982.

13. A number of bilateral negotiations between Japan and the United States were held in 1982, without a new bilateral agreement being reached. A draft drawn up in May 1982, which dealt mainly with wet blue chrome, was found by the United States Government to be insufficient as a basis for a mutually acceptable understanding. In September 1982, a further proposal was made to alter the licensing system for both finished leather and wet blue chrome. The Government of the United States considered, however, that there had been no real amelioration of the original situation that had been the subject of its complaint.

14. On 9 November 1982 the United States requested Article XXIII:1 consultations, as notified to the CONTRACTING PARTIES in a communication dated 16 December 1982 (L/5440). Such consultations were held first on 27 and 28 January 1983. As they were not successful in producing a mutually satisfactory solution the United States brought the matter to the CONTRACTING PARTIES in document L/5462 dated 25 February 1983. Before the Panel was established, further Article XXIII:1 consultations were held on 30 March and 12 April 1983.

III. Main arguments

(a) General

15. The United States stated as its basic complaint that the existence of the import quota on leather was inconsistent with the prohibition on quantitative restrictions in Article XI of the General Agreement. Before 1963, these quotas had been maintained as balance-of-payments measures under Article XII; since that time, however, they had lacked any GATT justification and, in addition, nullified or impaired tariff bindings on leather falling under item 41.02. The only justification offered was the desire, as a matter of Japanese social policy, to protect the jobs of a certain minority population. However, GATT rules made no exception for such a purpose and it would not be in the interest of Japan, the United States or the world trading system if Japan's example in this case were followed by other contracting parties. Because the measures were inconsistent with specific GATT obligations, there was prima facie nullification or impairment of benefits accruing to the United States under the General Agreement, and the attainment of GATT objectives was impeded, within the meaning of Article XXIII:1. In support of its case, the United States quoted paragraph 5 of the Agreed Description of the Customary Practice of the GATT in the Field of Dispute Settlement (Annex to the Understanding Regarding Notification, Consultation, Surveillance and Dispute Settlement, see BISD 26S/210-218).

16. The United States also requested that, apart from finding nullification or impairment of benefits accruing to the United States under the GATT, the Panel should suggest that the CONTRACTING PARTIES recommend elimination of the Japanese system of GATT-inconsistent restrictions which consisted of, firstly, the import quota system, and secondly, administrative obstacles intertwined with the quota, which could not be effectively eliminated until the quota was eliminated. As for the administrative aspects, the United States held, as subordinate points, that the failure of Japan to publish the total amount of the import quota and its failure to publish relevant administrative rulings were inconsistent with Articles XIII:3 and X:1 respectively. The way in which Japan administered its quotas on leather, including its refusal to publish the global quota amount or a list of licence holders, was inconsistent with the reasonableness requirements of Article X:3. The effect of these restrictions could be seen in the low level of United States exports to Japan despite continuing efforts by United States leather exporters, whose competitiveness was demonstrated by successful large-scale exports to other East Asian markets.

17. Japan recalled that various developed countries still maintained a considerable number of residual import restrictions for reasons which were specific to each item. From a realistic point of view it did not seem appropriate to seek only a legal judgement on these issues. Japan had made its utmost efforts to liberalize residual import restrictions in general. Leather and leather footwear were the only manufactured items which remained restricted and constituted a hard core, reflecting the extremely difficult conditions of the Japanese leather industry due to complex domestic social problems and its low-level competitiveness. In spite of this, the Japanese Government had expanded the quotas over the years and had, in financial year 1979, sharply increased the amounts of the import quota.

18. Japan added that whether or not Japan's quota system nullified or impaired the interests of United States leather exports depended solely upon whether or not the allocation system and its implementation functioned so as to hinder United States trade. This was not the case. No benefits accruing to the United States under the GATT had been nullified or impaired by Japan. Japan had actually benefited the United States and other countries by opening a large quota for them. This had resulted in the steady increase in United States exports of leather to Japan, even in comparison with the level of exports from other developed countries. The large quota would continue to offer sufficient opportunities for the United States to export to Japan and Japan had proposed further access in efforts to seek a realistic resolution of the matter through bilateral consultations. In Japan's view, the existence of the quotas themselves would not imply that real injury had been caused and that trade interests were impaired.

19. Japan maintained that if the United States appreciated fully the compelling circumstances under which Japan maintained its import restrictions on leather and the earnest efforts which Japan had made to improve access to the Japanese market, it would withdraw its referral of the issue to the GATT. If the United States took the realistic approach of accepting the proposals made by Japan it would be in a position to see what their effects would be. To ask for unrealistic recommendations did not

contribute positively to the spirit of the General Agreement, the aim of which was to expand trade. In compliance with the consensus reached when the terms of reference of the Panel had been established, the Panel should take a more substantive standpoint and ask the United States what specific impairments it claimed. Japan also recalled that the understanding of the Chairman of the Ministerial Meeting held in November 1982 had been (SR:38/9, page 2) that "some governments would require a certain amount of time to fulfil the undertaking", laid down in paragraph 7(i) of the Ministerial Declaration (BISD 29S/11).

(b) Article XI

20. The United States stated that the quotas on leather represented a clear and continuing infringement of Article XI. They did not fall within any of the exceptions in paragraph 2(c) of that Article and justification for balance-of-payments reasons had not existed since 1963 when Japan got Article VIII status in the International Monetary Fund, and disinvoked Article XII of the GATT (L/1976). The sole reason claimed by Japan for its retention of quantitative restrictions on leather was the desire to protect the Dowa people. While fully appreciating the sensitive nature of the problem, the United States could not agree that import quotas were an acceptable way of solving domestic social problems. Such problems were irrelevant to the present case, and irrelevant to the terms of reference of the Panel. A finding by the Panel which would in any way support Japan's assertion that import quotas were a necessary and acceptable means to protect minority workers would set a dangerous precedent, completely inconsistent with the GATT. Nearly all contracting parties had domestic social problems that were highly political, emotionally charged issues. Even if protection of the people in question could justify a quota, Japan had not demonstrated that the quotas were necessary to the well-being of this people, less than one per cent of which was directly employed in tanning. It recalled that in the case of Quantitative Restrictions against Imports of Certain Products from Hong Kong¹ the Panel had found that France's maintenance of quantitative restrictions constituted a prima facie case of nullification or impairment. The Panel had rejected the argument of the European Communities that social and economic conditions could justify these restrictions. It had been of "the opinion that such matters did not come within the purview of [Article] XI ... and in this instance concluded that they lay outside its consideration".² The Panel had also found the restrictions to be illegal regardless of their duration. Japan's insistence on the economic and social necessity of the import restrictions was inconsistent with its simultaneous claim that the import quotas had not adversely affected United States exports.

21. Japan explained to the Panel in detail the historical, cultural and socio-economic background of the case, relating to the so-called "Dowa problem". The main points contained in this statement are set out below:

- (i) This was a most serious and important social problem deriving from the fact that a segment of the Japanese people, owing to discrimination based on a class system formed in the process of the historical development of Japanese society, was placed in an inferior position economically, socially and culturally;

¹Report in L/5511, adopted by the Council on 12 July 1983 (C/M/170).

²L/5511, paragraph 27

- (ii) A major characteristic of the problem was that large numbers of people (according to a survey of 1975 the population was about 1,120,000) lived together in particular districts (about 4,400) on account of actual discrimination in social life. The growing number of persons who in recent times had left these particular districts were still subjected to discrimination in social standing either directly or indirectly;
- (iii) The Dowa districts had been founded by those who suffered from political, economic and social discrimination in the feudal society. Especially in the early 17th century, the people of Dowa districts had been, as an established social institution, classified as being outside and below the class hierarchy of Samurais, peasants, artisans and merchants, and had been subjected to severe institutional discrimination in all aspects of social life: prohibition on a change of occupation, moving, and association or marriage with people other than their own Dowa Class, obligation to wear certain humble clothes, etc.;
- (iv) In 1871, the people of Dowa districts had been emancipated from institutional discrimination, following the Meiji Restoration with which Japan emerged as a modern state. However, this emancipation was only formal as in actual social life, these people continued to lead a destitute life under miserable conditions not too different from those in the feudal or pre-modern days;
- (v) After World War II, democratic reforms had been carried out in all aspects of Japanese political, social and economic life. Certain budget measures had been implemented in 1953 to cope with the problem. The Law on Special Measures for Dowa Projects (from 10 July 1969 to 31 March 1982) had been enacted in 1969. As the problem remained unsolved, the Law on Special Measures for Area Improvement Project had been put in force from 1 April 1982 until 31 March 1987. Dowa projects or area improvement projects now in progress were aimed at such purposes as improvement of the living environment, enhancement of social welfare and public health, promotion of district industries, promotion of employment, improvement of education and cultural activities and protection of human rights. The total of project appropriations (including appropriation for Dowa districts under general budgetary items) in fiscal year 1983 was Y 238 billion (about US\$1 billion) (the total amount between Japanese fiscal year 1969 and 1983 was Y 1,955 billion);
- (vi) According to a survey in 1975, the main occupations of the people in question were (a) small scale farming (39 per cent of farms in Dowa districts were under 0.3 hectares and 63 per cent under 0.5 hectares) and (b) small enterprises and workers of traditional Dowa industries like leather industry, shoe and other footwear manufacturing. Not many were employed in modern industries. About 37 per cent of the people working were engaged in extremely small firms with four or less workers and about 64 per cent in firms with thirty workers or less. Also, 35 per cent of the total workers of Dowa districts were temporarily employed or were day-labourers, while the national

average was 7.4 per cent. The ratio of the people on welfare assistance in the Dowa districts as a whole was about 6.3 times that of the national average;

- (vii) It could be said objectively that the material life of the Dowa districts had improved to a large extent compared with the past, although the elimination of poverty still had a long way to go, with the problems caused by poverty such as quality of education and employment remaining in not a few cases. Likewise, in Japanese society at large, psychological discrimination, though reduced to a large extent, still existed. Thus the Japanese Government had been taking active measures to enlighten and educate the Japanese public to that end.

22. Japan added that the districts in question constituted more than a minority problem as the phenomenon was unique and relating to subsistence and survival. The Japanese tanning industry, which was a traditional and symbolic industry for the population in question, consisted of approximately 1,300 enterprises employing directly about 12,000 workers, with over 80 per cent of the concerns employing not more than nine workers. Its technological level was low and it mostly depended on overseas raw hides. As a result its international competitiveness was considerably inferior to United States' companies. Including employee family members and those engaged in related activities, the industry supported several hundred thousand people and regional economy (i.e. the second local industry in the Hyogo prefecture). Due to stagnant domestic demand under the recent economic recession, increased purchases of artificial leather and chronic competition among domestic producers, almost all Japanese producers were compelled to run a deficit operation. Should the import restrictions on leather be eliminated at the present stage the industry would collapse with unmeasurable social, regional-economic and political problems. The only viable alternative liberalization in leather was an expansion of quotas over an extended period of time, a path consistently pursued by Japan. Thus, Japan's import quotas for Japanese fiscal year 1982 were six times larger than the figures for Japanese fiscal year 1978. Import restrictions in the Hong Kong/European Community case cited by the United States had been due to ordinary economic reasons quite different from the long-standing historical and social difficulties which were the background for the Japanese import restrictions on leather. Japan maintained that a careful examination would show that there had actually been no nullification or impairment of benefits accruing to the United States.

23. The United States recalled that the leather issue, including elimination of the global quota, had been discussed at numerous informal and formal meetings between the two Governments but that no proposal had yet been advanced by the Japanese side to bring Japan's system into conformity with the General Agreement by eliminating its GATT-inconsistent import restrictions on leather.

24. Japan replied that the purpose of the attempt to reach a new bilateral agreement had been, and remained, to adjust interests of both countries under the current import quota system. If the intention had been to eliminate the import restrictions, there would have been no need to conclude an agreement through bilateral negotiations.

25. The United States replied that even expanding licensing or licensing without a quantitative ceiling still involved maintenance of an import quota. The Panel in the Hong Kong/European Community case had found that a similar French "SLQ" scheme of discretionary licensing without quantity ceilings was still in fact an import quota inconsistent with the General Agreement.

(c) Articles X:1 and XIII:3

26. The United States recalled that according to Article X:1 all laws, regulations and administrative rulings pertaining to requirements, restrictions or prohibitions on imports or exports "shall be published promptly in such a manner as to enable governments and traders to become acquainted with them". Japan contravened Article X:1, because the MITI did not publish the size of the global quotas for leather, the allocation rules, the names of licence holders, the quantity of their licences, nor the size of unfilled quota balances, either for the quotas as a whole or for individual licence holders. Under Article 3 of the Import Trade Control Order, MITI need not publish any information concerning import quotas if it deemed such publication improper; thus, it appeared that under Japanese law, MITI could even institute and maintain a quota in secret. Despite repeated requests for information on the size of the global quota on leather, the United States did not learn this amount until one of the Panel's meetings. Furthermore, the Japanese Government had consistently refused to publish the volume or value of the global quotas on leather, in contravention of Article XIII:3(b), which provided that "in the case of import restrictions involving the fixing of quotas, the contracting party applying the restrictions shall give public notice of the total quantity or value of the product or products which will be permitted to be imported during a future period and of any change in such quantity or value". A similar requirement was provided in Article 3(c) of the Agreement on Import Licensing Procedures. The yearly import announcement published for leather contained no mention of quota amount or value, and its only description of quota allocation was that "quota allocations will be decided by the Quota Allocation Examination Board". As a result of the elaborate licensing scheme and the non-publication of information that was necessary for planning, commencing or completing an export transaction with Japan, the United States and other foreign exporters had been prevented in practice from filling even the small quotas granted.

27. Japan replied that except for the size of quotas, the entire process of import quota allocation was published, as required in Article X:1, in the import announcements in the MITI Gazette. Japan added that Article XIII:3(a) did not require the publication of the names of licence holders, hence Japan had no obligation to publish the quantity of their licences nor the size of unfilled quota balances.

(d) Article X:3

28. The United States recalled that according to Article X:3 all laws and regulations pertaining to import requirements, restrictions and prohibitions had to be administered in a "reasonable manner". Article X:3 inherently related to both information published concerning a quota and administration of the quota. Japan's refusal to publish the volume or value of its import quotas on leather, information which the drafters of the General Agreement had recognized as necessary for importers to be able to make practical use of quotas, in itself indicated unreasonableness.

Also unreasonable was Japan's refusal to publish certain information necessary and useful for exporting leather to Japan, such as unfilled quota balances, quota allocations, names of quota holders and quota allocation rules. Moreover, in administering the leather quotas, the Government of Japan had allocated licences so as to channel import trade through Japanese producers and distributors of leather who had no incentive to fully utilize the quota amounts allocated to them. In many instances existing licence holders did not utilize their licences, but still remained eligible annually to receive licences. New users with a genuine intent to import leather were often unable to secure licences for sufficient quantities to meet their needs, or they were prevented from importing leather at all. To preserve the existing distribution system for leather, MITI would not allocate import licences to end-users such as footwear producers. Thus, foreign exporters could only sell through a chain of middlemen. As a result, the minuscule quota available to foreign suppliers was effectively reduced even further. If a contracting party were to administer an import quota - even a GATT-legal one - by systematically and knowingly granting import licences only to domestic producers of competing products who had every incentive not to import, this would clearly fall outside the scope of "reasonable" conduct under Article X:3.

29. Japan explained the present criteria of allocation. As for wet blue chrome MITI allocated, through the Tanners' Council of Japan, the individual amounts to each tanner who wanted to import this product, and to those who had orders from tanners. In view of the fact that each tanner's demand was taken into account, the Council was in no way controlled by the Government. Also tanners that were not members of the Council had actually been allocated quotas through the Council. However, in order to remove United States doubts, Japan had proposed a system whereby quotas could be obtained without passing through the Council. It had also been proposed not to enforce the ceiling established. As for finished leather, in order to make imported leather available to large numbers of end-users, often not familiar with import procedures, quotas were allocated to leather wholesalers whose operations complied with detailed orders reflecting the business scale of users and preferences in the market. Eligible for quotas were (i) those with leather import records from the previous year, mostly large-scale trading firms who had been involved in the importation of leather for many years, and (ii) members of the Japan Leather Wholesalers' Association and those having orders from it, i.e. mostly relatively small firms which had been recognized as eligible since 1973. Tanners did not receive quotas for finished leather. Importers wanted trade expansion and, once they had been allocated quotas, the Government had no intention of interfering with their transactions, nor did it have any administrative means to do so.

(e) Article II

30. The United States argued that, not only did Japan's import restrictions on leather constitute a prima facie case of nullification or impairment, they also represented actual nullification and impairment of the tariff bindings on leather falling in CCCN 41.02 which were negotiated and paid for in Japan's GATT accession negotiations. In the United States/France Import Restrictions case in 1962, which was closely similar to the present dispute in that a contracting party had continued to maintain quantitative restrictions inconsistent with Article XI after having disinvoked Article XII, the Panel had found, inter alia, "that the

maintenance by a contracting party of restrictions inconsistent with Article XI after the contracting party concerned had ceased to be entitled to have recourse to Article XII constituted nullification or impairment of benefits to which other contracting parties were entitled under GATT and the effects of such nullification or impairment were aggravated if such maintenance of restrictions continued for an extended period of time" (BISD/11S/94).

31. According to Japan, the bindings on sheep, lamb, goat and kid leather concerned CCCN 41.03-1 and 41.04-1, which had already been liberalized. The import quotas on sheep, lamb, goat and kid leather corresponded to CCCN 41.03-2-(1) and 41.04-2-(1), the tariffs on which were not bound. Therefore, Japan neither nullified nor impaired United States benefits under Article II in connection with sheep, lamb, goat and kid leather. Furthermore, Japan did not consider the previous case referred to as similar to the present one, for the same reason as set out above.

(f) Trade in Leather

32. The United States explained that its exports of leather to the world had increased more than seven-fold between 1970 and 1982, from a value of approximately US\$37 million to US\$279 million. Its share of the world leather market had increased from about 6 per cent in 1972 to nearly 10 per cent in 1981. While in 1977, 26 per cent of United States leather exports had gone to the Far East market outside Japan, by 1982, 60 per cent (US\$168 million) had been to this market. The substantial growth of United States leather exports to these countries stood in sharp contrast to the negligible growth rate of United States leather exports to Japan, whose leather market could be reasonably valued at US\$1 billion per year, but whose total leather imports from all sources in 1981 represented only 7,664 metric tons (US\$73 million), continuing a decline from the 1979 peak of 11,433 metric tons (US\$135 million).

33. The United States industry's competitiveness in world markets was proven by the steady growth of United States leather exports worldwide and particularly in the Far East. United States leather exports would be competitive in the Japanese market on a wide range of leather types and qualities, especially heavier leathers (such as those used for boot uppers, boot soles, shoe soles, etc.) as well as leather for sporting goods and for gloves and other garments. The United States could have exported substantial quantities of leather to the Japanese market, were it not for Japan's import restrictions. United States tanners had exported the same type of leather to Japan as to any other country, i.e. basic categories that were common to all leather industries in the world. The Japanese fashion might be different from the United States fashion, but this might not need to affect leather types. An industry survey had projected that the United States' exports to Japan would have been ten times larger if the Japanese market had been as open as that of the EC. Trade figures showed that from 1977 to 1981, Japan had imported only US\$6 to US\$8 million of United States leather annually, i.e. under 2 per cent of United States leather exports. In 1982 United States leather exports to Japan had been US\$9.8 million (3.5 per cent of total United States leather exports).

34. In practice, the 1979 understanding had been ineffective in meeting United States objectives; performance under the understanding, in terms of

increased market access for United States leather, had been disappointing. The global quota had been expanded by the establishment of special "hide suppliers' quotas" for crust and finished leather (the latter being partly reserved for automotive seat leather for use in cars to be exported) and for semi-processed wet blue chrome leather. However, United States exporters could not come near to filling the quota because of the administrative obstacles in the licensing system. A relaxation of some of the restrictions had not been enough to remove uncertainties about the Japanese leather market and to generate the necessary interest and effort for successful entry into the market. The experience showed that enlarged quotas and/or superficial procedural changes were not a solution. Every other country that had entered into a bilateral agreement with Japan had experienced the same difficulty. The common difficulties, in spite of differing products, prices, exchange rates and distances from the Japanese market, indicated that the problems were more than merely commercial in origin.

35. Japan stated that the Republic of China, to whom the United States exported 40 per cent of its total exports to the Far East, imported mostly wet blue chrome for which Japan had made suggestions as already indicated. The Republic of Korea, to whom the United States exported nearly a quarter of its total leather export to the Far East, imported for manufacturing products such as shoes which were then re-exported to the United States. This practice was also seen in Taiwan and Hong Kong, but not in Japan. The very concept of viewing the Far East as one market, irrespective of needs to respond to orders regarding details in the Japanese market, was one of the reasons why the United States leather was not imported in larger quantity to Japan.

36. Japan's imports from the United States had stood at US\$2 million in 1978, before the conclusion of the bilateral agreement, and had grown to US\$9 million in 1982, i.e. an increase of 4.5 times compared to a 1.9-fold increase of United States leather worldwide during the same period, and 3-fold and 3.5-fold United States' export increase to Italy and the Federal Republic of Germany respectively, who both, moreover, imported less leather totally from the United States than did Japan. The United States exports to France and the United Kingdom had actually decreased during the same period. Therefore, Japan considered that the Japanese market was sufficiently open to the United States. Furthermore, the fact remained that a considerable portion of the quotas was unused. United States suppliers had not carried out appropriate research and development and quality improvement efforts and had not, unlike European suppliers, met detailed requirements concerning trading lot, delivery time, etc.

37. The proposals Japan had made bilaterally, both with respect to the quota and licences for wet blue chrome, meant that anyone who had the intention and capability to import could get quotas allocated and that United States access to the Japanese market was completely guaranteed.

IV. Other statements

38. Australia, the European Communities, India, New Zealand and Pakistan all stated their interest as exporters of leather to Japan and said that they were affected by the Japanese regime of quantitative restrictions on leather imports. Furthermore:

- (i) Australia, whose major interest was item 41.02, had entered into a bilateral arrangement with Japan for the period October 1979-September 1982, but stated that no substantial exports had taken place under it. Its exports to Japan in 1982/83 of raw hides and skins had amounted to \$A38 million and its total world exports of semi-processed and processed leather in that period had amounted to \$A40 million. Nevertheless, its export of such leather to Japan had been negligible;
- (ii) The European Communities explained that it had a trade deficit with Japan in the leather sector, (importing 110 tons and exporting 49 tons, in 1982), a phenomenon they found particularly strange in the bovine sector in view of the relative herd sizes and tanning capacities. They had asked for the Japanese régime to be progressively liberalized on an m.f.n. basis but no satisfactory solution had been achieved in regular bilateral meetings held since 1976;
- (iii) India, whose main interests were items 41.03.100 and 41.04.100, said that, after having had recourse to the special dispute settlement procedures of the GATT in matters involving developed and less-developed contracting parties, had reached a settlement with Japan concerning finished leather in July 1980, but had not had its expectations fulfilled. Its exports (according to Japanese statistics) had declined from US\$3.2 million (accounting for a 65.8 per cent share in Japanese global imports of sheep and goat leather) in leather year 1980, to US\$2.2 million (market share of 61.7 per cent) in leather year 1982. Exports of finished sheep leather had declined from US\$64,000 (market share of 11.2 per cent) to US\$5,000 (market share 1.4 per cent);
- (iv) New Zealand noted that, in addition to a global quota on certain tariff lines, Japan had negotiated exclusive bilateral quotas with Australia, Canada and the United States for bovine products of tariff line 41.02-2. With particular emphasis on wet blue semi-processed bovine hides, it had sought access bilaterally for several years without success. Its global exports of semi-processed hides and skins had increased by 27 per cent from 16,000 tons to 21,000 tons between 1982 and 1983, while exports to Japan had increased by 12 per cent from 134 tons to 151 tons. Japan was currently New Zealand's largest market for raw hides and skins with about 44 per cent by volume of its total exports. By comparison, Japan represented only 0.008 per cent of its semi-processed hide and skin exports. The retention of the principle of basing additional quotas on raw hide imports would close New Zealand's access as exports of raw hide would diminish in accordance with the steady move to processing;
- (v) Pakistan, whose main interests were in CCCN 41.03 and 41.04, had held discussions with Japan in the spring of 1982 as part of the consultations in the Committee on Trade and Development without sufficient light having been shed on why it should be necessary to maintain the restrictions. Its exports to Japan in 1982 had been approximately Y 78.5 million, which it considered to be an amount sufficiently significant for it to show interest in the matter.

39. In the view of Australia, the European Communities, India and New Zealand, the restrictions would not be justified in the light of Japan's GATT obligations, notably Articles XI and X:1, and had the effect of nullification or impairment of benefits accruing to them under the GATT. Australia, India and New Zealand also referred to Article X:3 and held that the non-discrimination provisions of Article XIII:3(b) had also been contravened. Reference to Article XIII was made by the European Communities as well. New Zealand added that paragraphs 2(a) and 2(d) of Article XIII were not observed, in particular because quotas for semi-processed hides were apportioned according to import levels of raw hides. Australia, the European Communities and India furthermore stated that the restrictions nullified and impaired bound tariff concessions contrary to Article II. They also referred to the fact that the Committee on Import Licensing had already noted that Japan did not respect its obligations under the Agreement on Import Licensing Procedures regarding publication of quotas for leather products and had requested Japan to take appropriate action. Among further points raised were the following:

- (i) Australia noted that the restrictions were claimed to be necessary to protect the livelihood of a particular social group but that no clear indication had been given as to the basis on which the measures might be justified under the GATT. Australia requested that Japan institute measures designed to bring the restrictions progressively into conformity with its GATT obligations, with the ultimate objective of removing them in the foreseeable future.
- (ii) The European Communities also held that the dynamism of Japan's economy and the relative small number of jobs involved could not support the argument that liberalization would lead to a restructuring of the Japanese leather sector with unacceptable consequences for the Japanese community concerned. The Community, reserving its GATT rights, considered that Japan should remedy this situation on an m.f.n. basis.
- (iii) India added that the maintenance of illegal quantitative restrictions was all the more serious as these adversely affected the trade interests of less-developed contracting parties which had serious balance-of-payments problems, whose leather industry was also manned by backward communities, and whose social uplift was a concern of the government. It asked the Panel to find that Japan was in contravention of its GATT obligations.
- (iv) New Zealand, reserving its GATT's rights, sought a programme of significant liberalization of access with a view to the removal of the present quota restrictions within the near future.
- (v) Pakistan noted that contracting parties had an obligation to justify quantitative restrictions under the relevant GATT provisions but that in this case no justification had been given. Beside the legal aspects, the quotas prohibited producers and exporters from further expanding their activities. Also, there was a lack of information on their application including what kind of licensing was used. Generally, the impression was that some hidden elements of discrimination were involved in the quota allocation.

V. Findings and conclusions

40. The Panel considered the matter referred to it by the CONTRACTING PARTIES regarding restrictions maintained by Japan on the import of certain semi-processed and finished leather, in accordance with its terms of reference set out in paragraph 2 above. It considered the arguments put forward by the parties to the dispute, as well as the points made by other delegations indicating an interest in the matter to the extent that these points bore on the case before it.

41. The Panel noted that the approach of the two parties had important differences. The United States approach was based essentially on legal arguments. Its main contention was that the Japanese restrictions were in contravention of Article XI and that, in addition, the restrictions also contravened Articles X:1 and 3 and XIII:3 and adversely affected tariff bindings. Japan's case, on the other hand, rested almost entirely on considerations resulting from the particular problems connected with the population group known as the Dowa people.

42. The panel first considered the United States' complaint that quantitative restrictions maintained by Japan on the leather in question (see paragraph 7), were inconsistent with Article XI of the General Agreement which prohibits the use of quantitative restrictions.

43. The Panel appreciated the difficult socio-economic situation of the Japanese leather industry and the particularly sensitive problem of the Dowa population. The Panel appreciated the fact that leather and leather footwear were the only manufactured items which were subject to residual restrictions in Japan. This, in the Panel's view, bore witness to the difficulties which were involved in this case. The Panel also noted the fact that Japan had, despite its problems, increased the volume of leather imports permitted under its import régime and had continued to pursue a policy of expanding quotas over an extended period of time.

44. The Panel noted that Article XI:1 prohibits the use of quantitative restrictions. It recognized that situations might exist in which the maintenance of such restrictions would be justified under the relevant GATT provisions. It noted, however, that Japan had not invoked any provision of the General Agreement to justify the maintenance of the import restrictions on leather. The Panel decided that in such circumstances it was not for it to establish whether the present measures would be justified under any GATT provision or provisions. The Panel considered that the special historical, cultural and socio-economic circumstances referred to by Japan could not be taken into account by it in this context since its terms of reference were to examine the matter "in the light of the relevant GATT provisions" and these provisions did not provide such a justification for import restrictions. It noted that a panel report¹ adopted by the CONTRACTING PARTIES in 1983 had, in a similar situation, concluded "that [such matters] did not come within the purview of Articles XI and XIII of the GATT and ... lay outside its consideration". The Panel therefore found that the Japanese import restrictions at issue, made effective through quotas and import licenses, contravened Article XI:1.

¹Panel report on Quantitative Restrictions against Imports of Certain Products from Hong Kong (L/5511, paragraph 27).

45. The Panel noted that Japan had ceased to invoke Article XII regarding balance-of-payments difficulties in 1963. It noted that the Panel report referred to above had also concluded that the fact that "restrictions had been in existence for a long time ... did not alter the obligations which contracting parties had accepted under GATT provisions".¹ The Panel found this to be valid also in the present case.

46. In accordance with established GATT practice², the Panel therefore found that the Japanese restrictions on the products under consideration constituted a prima facie case of nullification or impairment of benefits which the United States was entitled to expect under the General Agreement.

47. The Panel noted that its terms of reference in this case explicitly required it "to make findings on the question of nullification and impairment". It also noted that since a prima facie case had been established, according to the established GATT practice³, it was up to Japan to rebut the presumption that nullification or impairment had actually occurred.

48. Against this background the Panel considered Japan's argument that the existence of the quotas themselves did not necessarily mean that nullification or impairment of benefits accruing to the United States had actually been caused, but that this depended solely upon whether or not the allocation system and its implementation functioned so as to hinder United States' trade.

49. The Panel examined the trade figures supplied by Japan in support of this contention, which related to the period from 1978 (before conclusion of the bilateral agreement) to 1982. It noted that these figures showed that, while United States' total exports of bovine and equine leather had increased from about US\$113 million to about US\$213 million, or approximately 88 per cent, its exports to Japan had increased by about 350 per cent, from US\$2 million to about US\$9 million. In comparison, United States' exports to the Federal Republic of Germany and Italy had, taken together, increased from about US\$2.6 million to about US\$8.5 million, i.e. a growth of only 227 per cent, and United States' exports to France and the United Kingdom had actually declined by 36 per cent in the same period from about US\$7.7 million to about US\$4.9 million.

50. On the other hand, the Panel noted that, according to figures supplied by the United States, whilst United States bovine and equine leather exports to Japan had increased by about US\$7 million - more than twice as much as the growth of exports to the four member States of the European Community referred to - they had increased by about US\$82 million, from about US\$38 million to US\$120 million, to three other East Asian markets

¹L/5511, paragraph 28.

²Annex to Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance (BISD, 26S/216, paragraph 5).

³Annex to Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance (BISD, 26S/216, paragraph 5).

taken together¹, each of which, since 1980, had imported more such leather from the United States than had Japan. The Panel also noted that while United States' bovine and equine leather exports to Japan in 1982 represented about 67 per cent of its exports to the four European Community countries, they were equivalent to less than 8 per cent of its exports of such leather to the three East Asian markets.¹ The Panel further noted that United States exports to Japan of the two other leather categories in question, i.e. sheep and lamb and goat and kid leather, were small and would not change the picture presented above.

51. The Panel then considered the Japanese argument that the quota did not limit United States' exports to Japan because United States' exporters had not filled the large quota opened for them and that the limiting factors were the recession of the Japanese leather market and lack of efforts by United States' suppliers in research and development, in improving quality and in responding to the specific needs of the Japanese market. It also took into account Japan's arguments that the licensing system was not an obstacle.

52. It noted the United States' arguments that its industry had exported the same type of leather to Japan as to any other country, that it could have filled the quota were it not for the accompanying administrative obstacles in the licensing system and that it could have exported more leather than provided for under the quota, if the Japanese régime had not existed.

53. The Panel found that the United States' exports of bovine and equine leather to Japan had increased considerably both in percentage terms and in absolute figures in the period under consideration and that this might be attributed to the relaxation of Japanese restrictions, as Japan had claimed. However, the Panel could not escape the conclusion that the import restrictions were maintained in order to restrict imports, including imports from the United States. It noted that, while the Japanese market was not fully comparable to other markets in East Asia, the evidence relating to these markets still tended to support the view that the Japanese restrictions limited United States' exports of leather to its market.

54. The Panel then turned to the arguments based on the fact that the United States had not filled its quotas. It noted that these consisted of contradictory assertions by the two parties that, by their nature, were difficult to evaluate. It did, however, consider that the fact that the United States was able to export large quantities of leather to other markets, and that other supplying countries had supported the arguments of the United States, tended to confirm the assumption that the existence of the restrictions had adversely affected United States' exports.

55. In any event, the Panel wished to stress that the existence of a quantitative restriction should be presumed to cause nullification or impairment not only because of any effect it had had on the volume of trade but also for other reasons e.g., it would lead to increased transaction costs and would create uncertainties which could affect investment plans.

¹The People's Republic of China, Hong Kong and the Republic of Korea.

56. The Panel therefore found that the arguments advanced by Japan were not sufficient to rebut the presumption that the quantitative restrictions on imports of leather had nullified or impaired benefits accruing to the United States under Article XI of the General Agreement.

57. The Panel noted that the United States had, as a subsidiary matter, argued that Japan had also nullified or impaired benefits under Articles II, X:1, X:3 and XIII:3. In view of the findings set out in the paragraphs above, the Panel found that it was not necessary for it to make a finding on these matters.

58. The Panel noted that some of the delegations which had indicated an interest in the matter before it and which had made statements to the Panel had argued that Japan's import régime on leather contained discriminatory elements and therefore contravened Article XIII:1 and 2. The Panel did not make a finding on this matter as it had not been raised by the United States and was not, therefore, within its terms of reference. It wishes however to draw the attention of the Council to the fact that this point was raised.

59. On the basis of the findings reached above, the Panel suggests that the CONTRACTING PARTIES recommend that Japan eliminate its quantitative restrictions maintained on the import of the products subject of the United States' complaint (see paragraph 7) and thus conform with the GATT provisions.

60. The Panel noted that Japan had indicated that it would not be possible for it to eliminate its quantitative restrictions on leather immediately. The Panel recognized the difficulties faced by Japan but noted that "the first objective of the CONTRACTING PARTIES is usually to secure the withdrawal of the measures concerned if these are found to be inconsistent with the General Agreement".¹ The Panel felt that the Council might wish to consider whether or not Japan should be given a certain amount of time progressively to eliminate the import restrictions in question and, in this context, to consider the factors referred to above, in particular those in paragraph 43.

¹Annex to Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance (BISD 26S/216, paragraph 4).