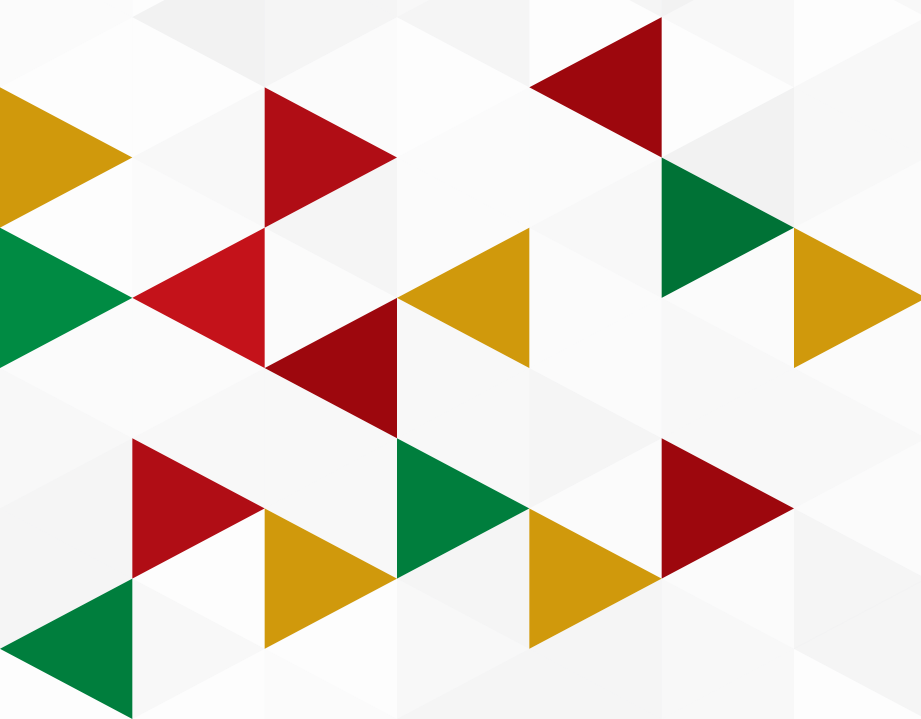


BRAZIL-JAPAN

ROADMAP FOR AN ECONOMIC PARTNERSHIP AGREEMENT BETWEEN JAPAN AND MERCOSUR



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CNI. THE STRENGTH OF THE BRAZILIAN INDUSTRY

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JOINT REPORT BY THE BRAZILIAN NATIONAL
CONFEDERATION OF INDUSTRY (CNI)
AND KEIDANREN (JAPAN BUSINESS FEDERATION)

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CHAPTER 1:
INTRODUCTION

July 2018

During more than 120 years of diplomatic relations since the signing of the Treaty of Friendship, Commerce and Navigation between Japan and Brazil in 1895, our two countries have built close and amicable ties through extensive exchange in many spheres, including politics, economy, culture, sports, and people. In the economic sphere, especially, Japan and Brazil have become important partners for one another and developed cooperative relations across a wide range of fields such as agriculture, resources and energy, infrastructure, manufacturing, and services.

Since convening the first meeting of the Brazil-Japan Economic Cooperation Committees in Rio de Janeiro, Brazil, in 1974, Keidanren and CNI have contributed to stronger bilateral economic relations by engaging in ongoing dialogue aimed at expanding economic exchange relating to trade, investment, and other topics, enhancing mutual understanding and ties based on a relationship of trust, and jointly promoting collaborative projects in various fields.

In particular, at the 20th meeting of the Economic Cooperation Committees held in Curitiba, Brazil, in 2017, representatives from Japan and Brazil agreed that before their 2018 joint meeting they would update the joint report on a roadmap for a Brazil-Japan economic partnership agreement (EPA) compiled by Keidanren and CNI in September 2015. With concern over the global rise of anti-globalism and protectionism, the Japan-Mercosur EPA will lead to the formation and strengthening of free and open economic zones, thus concluding the agreement will have profound significance¹.

To this end, Keidanren and CNI compiled this report after examining the significance of a possible Japan-Mercosur EPA (hereinafter, "the EPA") and matters that should be included in the EPA based on factors including the current state of economic relations between Japan and Mercosur, especially with Brazil, as well as business issues faced by companies and their wishes.

The report consists of an overview of recent economic relations between Japan and Mercosur (Chapter 2), issues to be addressed in the EPA (Chapter 3), and conclusions and recommendations (Chapter 4).

CNI and Keidanren also prepared another document which addresses specific bilateral initiatives specified in the previous report².

¹ "Survey about EPA between Japan and Mercosur"

<http://jp.camaradojapao.org.br/upload/files/Summary%20of%20survey%20result%20for%20HP%281%29.pdf>

In May 2018, Japan-Mercosur EPA Preparation Taskforce, *Câmara de Comércio e Indústria Japonesa do Brasil*, conducted a survey for 348 member companies in Japanese Chamber of Commerce in Brazil, Argentina, Uruguay, Paraguay and companies operating in Mercosur countries. 84% out of 259 companies answered that EPA between Japan and Mercosur is needed (180 out of 216 companies in Brazil: 83%, 30 out of 33 companies in Argentina: 91%, 6 out of 6 companies in Paraguay: 100%, 4 out of 4 companies in Paraguay: 100%) when asked the necessity of Japan Mercosur EPA.

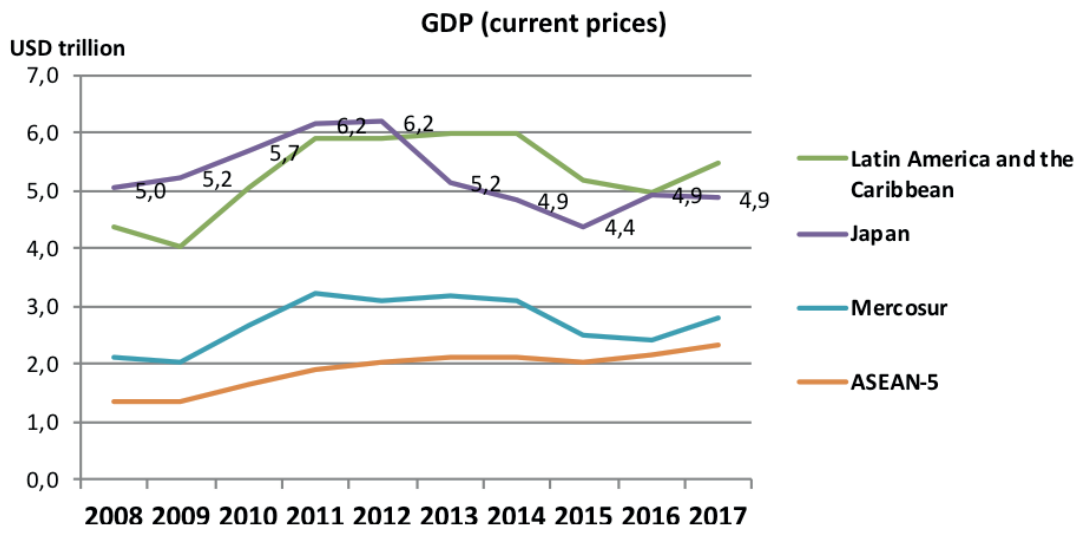
² "Brazil-Japan: Roadmap for an Economic Partnership Agreement" (September, 2015) <http://www.keidanren.or.jp/en/policy/2015/074.pdf>



CHAPTER 2:
**JAPAN-MERCOSUR
ECONOMIC RELATIONS**

Mercosur is a customs union composed of Argentina, Brazil, Paraguay and Uruguay. The GDP of Argentina is \$554.1 billion, \$1,799.7 billion in Brazil, \$27.3 billion in Paraguay, and \$53.2 billion in Uruguay. The population is 44.3 million in Argentina, 207.4 million in Brazil, 6.9 million in Paraguay and 3.4 million in Uruguay³. Mercosur is a very large economic zone (GDP \$2,427.0 billion, population 259.45 million) and represents 49% of the Latin America GDP (\$ 4,991.4).

Japan, on the other side, has a GDP very similar to Latin America and has a great economic potential. The GDP of Japan is \$ 4,948.3 billion and the population is 126.5 million.



Source: World Economic Outlook Database (April 2018 Edition), IMF

Value of trade between Japan and Mercosur have expanded, and despite the Lehman shock in 2009 and the decline in resource prices since 2013, export from Japan to Mercosur four countries from 2000 to 2017 increased by 31% (about \$ 4.2 billion in 2017) and Japan’s import from Mercosur countries increased by 136% (approximately \$ 7.9 billion in 2017). As destinations for exports from Japan, in 2017, Brazil ranked 27th, Argentina 55th, Paraguay 106th, and Uruguay 118th. As sources of imports to Japan, in 2017 Brazil ranked 21st, Argentina 58th, Paraguay 105th, and Uruguay 106th.

2.1 Mercosur Exports to Japan⁴

Looking at the major export items to Japan and export partners of each country, Brazil’s major export items to Japan are primary products such as agricultural products such as ores, slag and ash (27.3%), meat (17.4%), cereals (8.6%), coffee and tea (6.2%) and iron and steel (5.9%). It accounts for approximately 65.3% of the total exported value to Japan in 2017. Brazil’s major export partners are China (21.8%), European Union (16%), the United States (12.5%), Argentina (7.2%), and Japan is ranked fifth (2.4%).

³ Source: CIA Factbook

⁴ Source: TradeMap.

Argentina's exports to Japan are composed by fish and crustaceans (23.1%), aluminum and articles thereof (15.9%), ores, slag and ash (13.9%), inorganic chemicals (13.7%) and cereals (7.5%). It accounts for approximately 74% of the total exported to Japan in 2017. Brazil (15.9%), European Union (14.9%), the United States (7.7%) and China (7.4%) are the major export partners, and Japan accounts for 1.1% of the total export.

Paraguay's main exported items to Japan last year are residues and waste from the food industries (73.7%) and oil seeds and oleaginous fruits (24.7%). It accounts for almost all of the exports to Japan (98.4%). Major export partners are Brazil (32%), Argentina (14.5%), European Union (12.8), Chile (7.2%) and Russia (6.4%). Japan represents 0.5% of Paraguay's exports.

The main export items from Uruguay to Japan are wool, fine or coarse animal hair (40.5%), preparations of meat, fish or crustaceans (24.6%), tobacco and its manufactured (10.8%) and animal or vegetable fats and oils (9.1%). It accounts for 85% of Uruguay's exports to Japan. Major export partners are China (22.4%), Brazil (16.4%), European Union (11.1%), the United States (5.8%) and Argentina (5.3%).

Together, it can be said that from the Mercosur to the world, many raw materials, foodstuffs and animals, products by raw materials etc. are exported.

As of 2018, preferential tariffs from the Japanese General System of Preference (GSP) apply to Argentina and Paraguay, but Uruguay was excluded from preferential tariffs in 2017. Some preferential tariffs for Brazil have ceased in 2018, and all are expected to end in 2019.

2.2 Japanese Exports to Mercosur⁵

Looking at the major exports items from Japan to Mercosur countries, Mercosur represents only 0.6% of Japanese exports. The top five destinations of Japanese goods are the United States (19.3%), China (19%), European Union (11.1%), South Korea (7.6) and Taipei (5.8%). Mercosur, as a bloc, occupies the 21st place. Among the Mercosur countries, Brazil is the main partner of Japan, representing 0.5% of the Japanese exports, followed by Argentina (0.1%), Paraguay and Uruguay.

The major export items from Japan to Brazil are vehicles (25.2%), machinery and mechanical appliances (23.8%), electrical machinery (9.7%), organic chemicals (6.1%) and optical, photographic, measuring or medical equipment (5.7%). It accounts for 70.4% of Japan's exports to Brazil.

Argentina's main import items from Japan are almost the same ones imported from Brazil: vehicles (30.1%), machinery and mechanical appliances (20.6%), optical, photographic, measuring or medical equipment (9.3%), electrical machinery (8.2%) and organic chemicals (7.5%). These products represent 83.6% of Japan's exports to Argentina.

⁵ Source: TradeMap.

The main export items from Japan to Paraguay are vehicles (48.4%), electrical machinery (18.1%), machinery and mechanical appliances (10.6%) and rubber (4.9%), involving a total of 82.1% of Japan's exports to Paraguay.

Finally, Uruguay's main import goods from Japan are vehicles (22.7%), machinery and mechanical appliances (21.2%), rubber (20%), optical, photographic, measuring or medical equipment (11.8%) and electrical machinery (9%), representing 84.7% of Japan's exports to Uruguay.

Overall, in exports from Japan to Mercosur, machinery and transport equipment accounts for the largest proportion. Among them, exports of transportation equipment, electrical equipment, automotive-related items and the like are particularly high.

2.3 Bilateral investments⁶

The total greenfield foreign direct investment (FDI flows) of Japan in 2017 is \$47.2 billion, of which the amount of FDI to Mercosur is \$488.5 million, accounting for 1%. Furthermore, 1,828 jobs were created in Mercosur as a result of the Japanese investments in the region.

Japan was the 8th major investor in Brazil in 2017 and FDI totalized \$ 237.8 million in the automotive components, chemicals and consumer products sectors. In relation to Argentina, Japan was the 7th major investor in the country in 2017 and the Japanese FDI totalized \$ 250.7 million in the automotive and machinery sectors.

It is considered that promoting liberalization and protection of investment and services through the conclusion of the Japan-Mercosur EPA brings economic benefits to both the investment and recipient side.

⁶ Source: FDI Markets



CHAPTER 3:

JAPAN-MERCOSUR EPA

In order to further develop inter-regional trade and investment and other forms of economic exchange, Japan and the Mercosur countries must strictly comply with WTO rules. At the same time, to ensure that the EPA provides a comprehensive and solid legal basis for expanding such interaction, it must cover the areas outlined below in addressing pertinent issues.

3.1 Trade in Goods

- a. By improving trade in goods in a manner that ensures market access is free from significant distortions, the EPA must provide opportunities for more business operators to participate in inter-regional production networks and supply chains, promote greater international competitiveness by boosting added value and reducing costs throughout such supply chains, and thus offer greater benefits to consumers.
- b. To this end, as an agreement conforming to WTO rules the EPA should ensure that “duties and other restrictive regulations of commerce ... are eliminated on substantially all the trade between the constituent territories” as stipulated in Article XXIV, Clause 8 of the General Agreement on Tariffs and Trade. Based on this principle, while giving due consideration to the sensitivities of each country, the agreement should aim to form free and open markets at a higher level and make every effort to reduce and eliminate tariffs and non-tariff measures that have a negative impact on trade.
- c. In order to achieve an ambitious and comprehensive EPA, most of the tariffs should be eliminated in 10 years after the entry in force of the agreement, but leaving flexibility for sensitive goods to have longer transitional periods of 12 and 15 years. The agreement should have a priori exclusion of products from the liberalization schedule and the EPA should foresee the complete elimination of quotas.
- d. The list of sensitive goods should be minimized and avoid the exclusion of an entire sector from the liberalization process.
- e. Japan has a keen interest in eliminating tariffs on goods including motor vehicles and other transport equipment, motor vehicle parts, iron and steel products, machinery and mechanical equipment, electrical and electronic machinery and devices, and chemicals. Meanwhile, Mercosur seeks liberalization for beef and innards, poultry, biodiesel, corn, certain fruits, sugar and ethanol, soy oil, leathers, skins and footwear, processed foodstuffs, wood and textiles. For the EPA to contribute to win-win relationships bringing mutual benefits, it must aim for balanced outcomes.
- f. The EPA should also ensure that concessions are user-friendly for Small and Medium-sized Enterprises (SMEs) and other businesses.

3.2 Rules of Origin

- a. Rules of origin must be simple, flexible, and transparent. For the convenience of companies who will use the agreement, the EPA should enable users to select change of tariff classification criteria and added value criteria of Mercosur and Japanese companies.
- b. To simplify and facilitate procedures for issuing certificates of origin, the agreement should provide that the certification of origin can be done by self-certification and by private sectors that are delegated by customs authority and enable electronic application and issuance.
- c. Simple, flexible, and transparent administrative procedures should be adopted regarding certification and verification of origin.

3.3 Trade Facilitation and Customs Procedures

- a. In order to facilitate bilateral trade and allow companies to reap the full benefits of the trade preferences that the EPA aims to achieve, the agreement needs to harmonize and simplify customs procedures and enhance the transparency of customs administration.
- b. To this end, Japan and the Mercosur countries need to steadily implement measures for greater transparency of trade rules set out in the Trade Facilitation Agreement (TFA) that entered into force in February 2017 (internet availability of information on trade procedures, introduction of systems for rulings on matters such as tariff classifications prior to import of goods [advance ruling systems, etc.], and measures to expedite and simplify customs procedures (introduction of declaration and inspection prior to arrival of goods and risk-based inspections, as well as single windows for trade procedures, etc.).
- c. At the same time, negotiations for the EPA should further deepen TFA provisions and incorporate into the agreement matters that could contribute to reduce costs and time involved in administrative and customs procedures for trade between Japan and Mercosur such as enlarging the scope and establishment of deadlines in advance rulings, and establishing maximum time for clearance and release of goods. For example, the Trans-Pacific Partnership (TPP) stipulates provisions for issuance of advance rulings within 150 days after a request is lodged and release of express shipments within six hours after submission of the necessary documents.
- d. Since the Authorized Economic Operator (AEO) program contributes to effective and efficient customs administration and is an important element in facilitating and ensuring the safety of logistics in supply chains linking Japan and Mercosur, consideration should be given to mutual recognition of each country's AEO program.
- e. Japan and the Mercosur countries should also commit to establish possibility of appeal procedures and increase transparency on fees and charges collected by customs administration and other border agencies.

3.4 Technical Barriers to Trade and Sanitary and Phytosanitary Measures

- a. To promote trade between Japan and Mercosur, unnecessary barriers to trade should be prevented through the formulation, adoption, and implementation of regulations, standards, and procedures for assessing conformance.
- b. At the same time, the EPA should allow for reducing redundant and burdensome standards-related testing and certification procedures and consider incorporating mutual recognition and relevant provisions to reduce costs and delays in trade between the two regions. In this context, preference should be given to international standards.
- c. To this end, the EPA should incorporate provisions relating to technical barriers to trade (TBT) in order to improve transparency surrounding regulations, standards, and procedures for assessing conformance, and to enhance understanding of relevant administrative systems. It should also encourage cooperation and consultation on matters including harmonization and consistency of regulations and standards. In conjunction with these measures, a Sub-Committee on TBT Cooperation should be established comprising government representatives from both sides, representatives of standard-setting bodies and representatives of both private sectors to facilitate discussions that includes input from private-sector with the necessary specialist knowledge. The Sub-Committee should also address sectorial regulatory convergence.
- d. While continuing to avoid and remove unnecessary barriers to trade between the two regions, the EPA should include sanitary and phytosanitary (SPS) provisions aimed at protecting the lives and health of people, animals, and plants. The EPA should incorporate an ambitious SPS chapter that goes beyond the WTO SPS Agreement, addressing the requirements that SPS measures shall be based on science and on international standards. The chapter should refer to: (i) the promotion of a more prevention-based mechanism; and (ii) the expansion in breadth and depth of information-sharing. As well as promoting deeper understanding of related SPS measures and administrative systems, the EPA should establish a Sub-Committee on SPS Cooperation, which, through discussion and cooperation based on scientific principles and relevant scientific evidence, should appropriately deal with common matters of interest relating to SPS that could impact directly or indirectly on trade between Japan and Mercosur with the objective of achieving mutually acceptable solutions.
- e. At the same time, Japan and the Mercosur countries must deepen cooperation relating to international bodies' efforts to ensure food safety and address issues affecting human, animal, and plant life and health.

3.5 Trade Remedies

- a. Trade remedies including anti-dumping provisions, countervailing measures, and safeguards rectify unfair trade practices such as dumping and subsidies, and provide remedies for losses that these practices impose on industries in importing countries, but misuse of such measures can have a negative impact on free trade.
- b. Thus, as WTO members, Japan and the Mercosur countries should reaffirm the fundamental principles of WTO agreements and their rights and obligations under these agreements. As well as strictly observing these rules, they should consider incorporating WTO-plus elements (such as introduction of a “lesser duty rule” and prohibition of “zeroing”) into the EPA in order to enhance transparency of trade remedy measures and clarify their conditions.
- c. Since subsidies for specific sectors might create unfair competition among companies, not only in both parties’ countries, but also in global markets, the parties should commit to not introducing or maintaining export subsidies that are incompatible with the WTO Agreement on Subsidies and Countervailing Measures (SCM), and consider introducing into the EPA cooperative mechanisms to promote dialogue and coordination relating to adoption of subsidies.
- d. Parties should provide the existence of bilateral or preferential safeguards at least during the transitional period.

3.6 Investment and Services

- a. Promotion of foreign direct investment not only leads to more business opportunities for companies in the investing country, but also contributes to job creation, industrial development, and introduction of new technologies and business models in the host country. Since liberalization of trade in services would bring economic benefits to Japan and all the Mercosur countries and has the potential to greatly expand cooperation, the EPA must achieve comprehensive and high-level liberalization and protection of investment and services.
- b. To this end, with regard to investment the EPA should stipulate national treatment and most-favored-nation treatment both before and after setting up an investment, a ban on performance requirements that exceed levels set out in the Agreement on Trade-Related Investment Measures (TRIMs), freedom to transfer money, and widely-applicable procedures for settling disputes between investors and the host country. In case Japan and Mercosur countries decide to have market access lists in the Agreement, they should commit to liberalization based on the negative list system (the principle of abolishing regulations in all fields and making reservations for any remaining exceptional regulations) to maximize the benefits of abolishing and easing country-specific regulations restricting foreign investment and the activities of foreign companies. To prevent backtracking on

liberalization, the schedule of reservations based on the negative list should in principle impose mandatory ratcheting (an obligation to prohibit post-agreement addition of new reservations or other measures backtracking on initial liberalization commitments).

- c. To make the EPA more robust, consideration should be given to the possibility of including an investor-state dispute settlement (ISDS) mechanism for resolving disputes.
- d. Promoting Mercosur and Japan bilateral trade in services is an opportunity not only to increase market access for bilateral trade in services, but to increase the usage of services in manufacturing production and increase the economy's competitiveness as a whole. In order to reach a substantial liberalization in trade in services, efforts should be undertaken to achieve substantial sectorial coverage in accordance with the General Agreement on Trade in Services (GATS). A negative list system and ratcheting disciplines, when possible, should also be adopted for commitments to liberalize trade in services. Other topics such as maritime transportation and telecommunication are areas that Mercosur and Japan should also advance.

3.7 Intellectual Property Rights

- a. As well as ensuring a fair competitive environment, protection of intellectual property rights is essential to achieving industrial development through innovation. Thus the parties to the EPA should go beyond the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), promote prompt examination and transparent and efficient intellectual property administration, and put in place effective measures to ensure adequate enforcement of rights against infringements. To this end, the EPA should consider incorporating high-level rules that go beyond TRIPs.
- b. Restrictions on the amount and duration of royalties (including copyright and licensing fees) must be removed with a view to ensuring freedom of contract.
- c. Furthermore, the EPA should stimulate cooperation and technology exchange between Japan and Mercosur countries. An Intellectual Property Committee should be established to address these issues.

3.8 Energy and Mineral Resources

- a. As well as being strategically important for both Japan and Mercosur, cooperation in the energy and mineral resource fields contributes to sustainable regional development, and such ties should be further strengthened through trade and investment activity.
- b. To this end, the EPA should avoid rules on restrictive trade measures such as export controls and export duties relating to energy and mineral resources. The EPA should provide rules on transparency of measures that could affect the investment environment,

notification between countries when introducing new regulatory measures and steps to avoid disruption of existing contracts when adopting regulations, elimination/easing of local contents requirements and foreign capital ceilings, and enhancement of policy dialogue through the establishment of an Energy and Resources Sub-Committee.

3.9. Movement of Natural Persons

- a. Since smooth movement of natural persons is essential in enhancing business relations, to invigorate business between Japan and Mercosur the EPA should ease immigration, work, and residence conditions for intra-company transferees, specialists, and ensure prompt and transparent procedures.

3.10.E-Commerce

- a. Free cross-border data transfer and use is a prerequisite for innovation and a source of competitiveness for companies engaged in global business. Thus it is essential to ensure conformity with international rules and interoperability based on steadfast maintenance of an open and transparent internet and guaranteed cyberspace security.
- b. For these reasons, the EPA should incorporate provisions on non-discriminatory treatment of digital products and content, the balancing of data utilization with protection of user data and privacy, and obligations to permit cross-border transfers by electronic means. It should also ban the imposition of customs duties on electronic transmissions and content, and prohibit demands to establish computer-related facilities or provide access to software source code.

3.11.Government Procurement

- a. Mercosur and Japan are both in the top 5 largest markets in the world for government procurement. A chapter on the matter should be included in the EPA aiming at guaranteeing transparency and predictability in government biddings.
- b. The EPA should incorporate provisions equivalent to those of the WTO Agreement on Government Procurement and enhance transparency and predictability in bidding for public projects.
- c. Transparency should be fostered with specific disciplines such as procurements that are covered by the agreement; request for consultation by parties about procurement processes and all necessary information for foreign companies to participate in public procurement process of the party. Attention should also be given to clauses that prevent fraud in the agreement, such as the introduction of non-preferential rules of origin and denial of benefits. Both clauses guarantee that market accesses are given for countries in Mercosur and Japan.

- d. At the same time, each country needs to establish bidding systems that comprehensively evaluate all aspects of bids, including financial benefits such as reduction of life cycle costs; safety, disaster resilience, and sustainability; convenience and comfort; environmental and social responsibility; quality including operation and management; and contributions to local communities and economies such as human resource development.

3.12. Business Environment

- a. Even if investment and trade in services are liberalized, business can only be facilitated if domestic regulations in host countries are rational and administrative procedures are simple, transparent, prompt, and predictable.
- b. To this end, the EPA needs to establish mechanisms for government and business representatives to discuss issues relating to improvement of the business environment. These mechanisms should enable the parties to discuss and rectify a variety of problems affecting business activities, including domestic regulations, taxation, and labor issues.
- c. As well as ensuring the fairness and transparency of government procedures, in order to enhance predictability and avoid confusion caused by frequent revision of laws and regulations, general rules should be established on setting and announcing examination criteria and standard processing periods, procedures for filing notifications, and formulating ordinance.

3.13. Dispute Settlement

- a. The EPA needs to incorporate a robust mechanism for settling disputes relating to the most possible matters included in the EPA.



CHAPTER 4:
**CONCLUSIONS AND
RECOMMENDATIONS**

Although trade and investment flows between Japan and Mercosur are strong and economic relations are favorable, given the economic power of both regions there is tremendous potential for further economic and industrial cooperation. In addition to liberalization of trade in goods and services and removal of barriers to investment, establishment of rules on matters such as e-commerce and new legal frameworks aimed at further improving the business environment would build closer, more mutually beneficial economic ties between Japan and Mercosur, which could be expected to contribute to peace and prosperity in both regions and the world as a whole.

Thus, while maintaining consistency with WTO rules as a foundation, Japan and Mercosur should swiftly conclude an EPA that achieves comprehensive and high-level liberalization and rule-making, especially in the fields listed below. As well as seeking to create a balanced, win-win situation with mutual benefits, the EPA should aim for high-quality provisions that give due consideration to the sensitivities of each country while being constructive and proactive and comparing favorably with other multilateral FTAs and EPAs.

1. Trade in goods
2. Rules of origin
3. Trade facilitation and customs procedures
4. Technical barriers to trade and sanitary and phytosanitary measures
5. Trade remedies
6. Investment and services
7. Intellectual property rights
8. Energy and mineral resources
9. Movement of natural persons
10. E-commerce
11. Government procurement
12. Business environment
13. Dispute settlement

Note: the above list is not exhaustive.

Strong political leadership is essential to swiftly achieving such an ambitious EPA. We eagerly hope that leaders from Japan and Mercosur will display political will to achieve a Japan-Mercosur EPA at the earliest possible date. The business communities of Japan and Brazil will proactively participate and cooperate in governmental processes and contribute to accomplishing this objective.



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