U.S.-Japan Economic Partnership for Growth

United States-Japan Investment Initiative
2006 Report

June 2006
United States-Japan Investment Initiative 2006 Report

Executive Summary

Foreign direct investment is essential for the vitalization of the Japanese economy. As of the end of 2005, foreign direct investment in Japan totaled ¥11.9 trillion ($100.9 billion). This represents an increase of 80 percent when compared to the value at the end of 2001. The year 2001 was the base year for Prime Minister Koizumi’s target of doubling the stock of foreign direct investment in Japan in five years, an objective that Japan is steadily accomplishing.

One of the significant events this year was the entry into force of the new Japanese Corporate Code in May 2006. Many investments made among advanced countries take the form of merger and acquisition. Thus, the entry into force of this Corporate Code is expected to have a positive effect on increasing foreign direct investment in Japan, especially the provisions relating to “flexibility of merger consideration” (although such provisions will not come into effect until May 2007).

The U.S.-Japan Investment Initiative was established in June 2001 between the leaders of the two countries within the framework of the U.S.-Japan Economic Partnership for Growth. This Initiative provides important, mutually-beneficial opportunities to exchange opinions on improving the investment environment and removing any obstacles for the respective countries. Issues discussed in the past for improving the investment climate in Japan include: (i) facilitation of cross-border mergers and acquisitions, (ii) deregulation to create new business opportunities in the fields of education and medical services, (iii) labor-related laws and systems, and (iv) translation of Japanese laws and regulations into foreign languages. Issues on the U.S. side which were raised by Japan and led to opinion exchanges between both governments on the improvement of the U.S. investment climate include: (i) visa and other consular issues, (ii) cargo security, and (iii) the Exon-Florio provision.

Public outreach under this Initiative has included Invest-in-Japan symposiums held in November 2005 in New York and San Jose, and Investment Seminars are planned to be held in Sendai and Yokohama, Japan in October 2006.
Both the Japanese and U.S. governments welcome foreign direct investments. Under the U.S.-Japan Investment Initiative, the two governments intend to continue constructive discussions to improve the investment climate in our countries and to implement various activities to facilitate foreign direct investment.
# Table of Contents

I. Introduction

II. Current Situation of Foreign Direct Investment in Japan and the United States
   1. FDI in Japan
      (1) FDI Trends in Japan
      (2) Recent Topics
         A. Entry into Force of the Japanese Corporate Code
         B. Local Government Forum for Promotion of Foreign Direct Investment
         C. Program for Acceleration of Foreign Direct Investment in Japan
         D. Project to Assist Local Efforts to Attract Foreign Capital
      (3) Japan’s Strengths
   2. FDI in the United States
      (1) FDI Trends in the United States
      (2) Recent Topics
      (3) U.S. Strengths

III. Discussions in the U.S.-Japan Investment Initiative 2005-2006
   1. U.S. Concerns
      (1) Cross-border Mergers and Acquisitions (M&A)
      (2) Demographic Issues and Investment
         A. Education
         B. Medical Services
      (3) Labor-related Laws and Systems
      (4) Translation of Japanese Laws and Regulations into Foreign Languages
   2. Japan’s Concerns
      (1) Visas
      (2) Cargo Security
      (3) Exon-Florio Provision

IV. Conclusion

Appendix 1: Invest-in-Japan Symposium
Appendix 2: Examples of Recent Entries of the U.S. Companies
Appendix 3: Accomplishments over the Past Five Years
I. **Introduction**

The U.S.-Japan Investment Initiative was established in June 2001 by U.S. President Bush and Japanese Prime Minister Koizumi as a forum to exchange opinions for the improvement of the foreign direct investment climate in Japan and the United States within the framework of the U.S.-Japan Economic Partnership for Growth. This Initiative is chaired jointly by the Japanese Ministry of Economy, Trade and Industry (METI) and the U.S. State Department, and two working group meetings have been held this year, on December 2, 2005 and June 5, 2006, to discuss possible measures for the improvement of the climate for foreign direct investment in the respective countries.

As part of the public outreach program, Invest-in-Japan Symposiums were held in November 2005 in New York and San Jose. Following the seminars held in Nagoya and Chiba last May, investment seminars are also planned for Sendai and Yokohama, in the autumn of 2006.

Recent developments in the global economy have led to an increase in the cross-border activities of private companies, and the importance of foreign direct investment has been rising. Foreign direct investment (FDI) allows an investment-receiving country to acquire new technological or managerial know-how and to improve management efficiency and competitiveness. FDI is also recognized as effective for increasing employment opportunities, creating consumer demand, expanding consumer options and improving convenience for consumers.

Recognizing this, the Initiative plays an important role in allowing the U.S. and Japanese governments to share views on improving the FDI environment in their respective countries, and in contributing to the economic growth of both countries.
II. Current Situation of Foreign Direct Investment in Japan and the United States

1. FDI in Japan

(1) FDI Trends in Japan

In Japan, FDI has been significantly increasing since the latter half of the 1990s. Factors contributing to this growth include the expansion of business fields open to foreign companies as a result of deregulation, a decrease in cross-shareholdings by Japanese companies, improved conditions for mergers and acquisitions as a result of the world-wide trend of industrial restructuring, and improved attractiveness of the Japanese market as a result of reforms to bankruptcy-related laws and corporate accounting systems. In recent years, the Government of Japan, in an initiative led by Prime Minister Koizumi, has successfully increased FDI in Japan, resulting in FDI stocks of ¥11.9 trillion at the end of 2005 (or $100.9 billion at the end-of-2005 exchange rate of 117.97 yen/dollar, the official exchange rate of the IMF International Financial Statistics of April 2006). At the end of 2005, FDI in Japan was 1.8 times larger than in the year 2001 when Prime Minister Koizumi declared his target of doubling the stock of foreign direct investment in Japan in five years.

Source: Statistics on the balance of foreign assets and liabilities, Ministry of Finance/Bank of Japan

Note: The definition of statistics was changed in 2005. The end-2005 number includes capital reserves, which were not included in previous year figures.
Of this ¥11.9 trillion, direct investment from the United States accounts for ¥5.2 trillion. Investment from the EU accounts for ¥4.2 trillion, and that from ASEAN accounts for ¥2.6 billion.

Although FDI in Japan has been increasing rapidly in recent years, its share of GDP is still extremely small when compared to that of other major advanced countries. Currently, the share is 2.0% in Japan, while it is 22.9% in the United States, 33.0% in England, 22.4% in Germany and 41.5% in France. According to the *World Investment Report 2005* issued by the United Nations Conference on Trade and Development (UNCTAD), Japan is ranked as low as 134th among 140 countries in terms of the ratio of FDI to GDP, although Japan’s Inward FDI Potential Index is ranked 16th.

![Inward Foreign Direct Investment Levels in Major Countries](image)

**Source:** IMF *International Financial Statistics*

(2) Recent Topics

A. Entry into Force of the Japanese Corporate Code

The Corporate Code was approved on June 29, 2005 during the 162nd Diet session and entered into force on May 1, 2006. Before this new code, consideration given to shareholders of merged companies was generally limited to stock of the
surviving company. This restriction served as a disincentive to otherwise advantageous mergers. The new Corporate Code has eased the restriction to allow the surviving company to provide cash or stock of its parent company instead of or in addition to its own stock. However, this provision will come into effect one year after the entry into force of the Corporate Code in order to allow firms time to determine whether they should adopt defensive measures against hostile takeover attempts and to prepare for such defensive measures that might be justifiable and acceptable to stockholders.

B. Local Government Forum for Promoting Foreign Direct Investment

Recognizing the increasing significance of FDI as a measure for revitalizing the local economy, the Governor of Osaka, Mayor of Fukuoka, and other local government officials took the initiative in organizing the “Forum of Local Authorities for the Promotion of Foreign Direct Investment in Japan.” The forum consists of members of 44 prefectural governments and 14 cities. The first forum was held in March 2006, adopting a proposal to the central government with the following three requests: (i) the government should strengthen its assistance to local governments in promoting activities to attract foreign capital and foreign-owned companies; (ii) the government should improve systems for facilitating the activities of foreign individuals, foreign-owned companies and foreign capital; and (iii) the government should strengthen national measures for promoting foreign direct investment. This proposal has been discussed by the Japan Investment Council Expert Committee Meeting and was reflected in the Program for Acceleration of Foreign Direct Investment in Japan designed by the government for expansion of foreign direct investment.

C. Program for Acceleration of Foreign Direct Investment in Japan

In January 2003, Prime Minister Koizumi declared his target of “doubling the cumulative amount of FDI in Japan in five years.” In March of the same year, the Japan Investment Council (JIC) headed by the Prime Minister issued the “Program for the Promotion of Foreign Direct Investment in Japan.” Since then, government-wide efforts have been made to improve the business environment and review administrative procedures in relation to this Program. During the JIC’s meeting in March 2006, and with the goal of doubling FDI in sight, the government decided to take further steps to promote FDI and announced a new goal “to increase the balance of FDI into Japan to 5% of the country’s GDP, double the present percentage by 2010.” In response to this, the Program for Acceleration of Foreign Direct Investment in Japan was established during the JIC meeting held in June 2006.
D. Project to Assist Local Efforts to Attract Foreign Capital

Recognizing that independent efforts by local organizations to attract foreign capital are essential to promote FDI, METI has been assisting local governments, through the Japan External Trade Organization (JETRO), in promoting activities to attract foreign companies by utilizing their regional strengths. This initiative follows implementation of a project for “Most Active Areas in Japan in Attracting Foreign Direct Investment” that took place in fiscal years 2003 and 2004. This project “adopted” 12 regions and assisted local organizations there in carrying out activities to attract foreign capital, and also assisted foreign companies in preparing to start a business in those areas.

(3) Japan’s Strengths

Japan’s GDP grew by 2.7% in real terms in 2005, the largest growth since the Initiative was established in 2001. The current recovery has been underway for 52 consecutive months through May 2006, which is the second longest economic growth period after World War II.

According to the report issued by the Ministry of Finance on April 26, 2006, Japan’s economic recovery is not limited only to urban areas but is gaining momentum in all regions around the country. The expansion is being sustained by strong business investment, increasing personal consumption and an improved job and wage outlook. The unemployment rate in fiscal 2005 registered a favorably low figure for the first time in seven years. This trend indicates that new business opportunities in Japan are increasing. More than anything else, the fact that the Prime Minister of Japan has taken the initiative in promoting countrywide efforts to increase FDI by welcoming foreign companies to start business in Japan sends a strong “welcome” message to business-seeking foreign companies.

In addition, various structural reforms taking place in Japan have resulted in the remarkable correction of the “high-cost structure” which used to hamper foreign companies wanting to invest in Japan. In particular, deregulation introduced in the fields of electricity, communication and energy have helped reduce costs for business.

According to UNCTAD’s World Investment Report 2005, Japan is ranked 16th among 140 countries in terms of the Inward FDI Potential Index as an indicator of attractiveness. UNCTAD explains that this high evaluation for Japan is because Japan has an enormous market accounting for about 11% of world GDP; rich human
resources with valuable expertise; a well-organized infrastructure in the fields of
distribution, information and communication; and a good business environment with
improved laws and systems poised to catch up with the trend of economic globalization.

2. FDI in the United States

(1) FDI Trends in the United States

The United States attracts significant FDI inflows from countries around the
world due to its open economy, strong growth, and high rate of return. Deregulation
and technological change have made the United States particularly attractive to
investors. FDI inflows into the United States, which peaked at over 3% of GDP in
2000, declined over 2001-2003, largely due to the global economic slowdown, increased
economic uncertainty, and the worldwide decline in mergers and acquisitions. FDI
inflows recovered in 2004, resulting in 8.2% year-on-year growth in the foreign direct
investment position in the United States. FDI has capitalized on opportunities and
helped reinforce economic successes during economic growth. During periods of
economic weakness, it has played a key role in diversifying and stabilizing the economy.
For example, in the 1980s FDI from Japan and other countries provided a critical
catalyst for change, which increased U.S. competitiveness, employment and
productivity.

### Foreign Direct Investment Position in the United States on a Historical Cost Basis, 1999-2004

<table>
<thead>
<tr>
<th>Year end</th>
<th>Billions of Dollars</th>
<th>Percent Change from Preceding Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999</td>
<td>955.7</td>
<td>22.8</td>
</tr>
<tr>
<td>2000</td>
<td>1,256.9</td>
<td>31.5</td>
</tr>
<tr>
<td>2001</td>
<td>1,344.0</td>
<td>6.9</td>
</tr>
<tr>
<td>2002</td>
<td>1,344.7</td>
<td>0.05</td>
</tr>
<tr>
<td>2003</td>
<td>1,410.7</td>
<td>4.9</td>
</tr>
<tr>
<td>2004</td>
<td>1,526.3</td>
<td>8.2</td>
</tr>
</tbody>
</table>

Source: Survey of Current Business (Feb 2006), Bureau of Economic Analysis,
Department of Commerce

In 2004, the most recent year for which data is available, foreign direct
investment stock in the United States was up from the previous peak in 2003: FDI
measured at historical costs totaled more than $1.5 trillion (see chart above). The largest investment positions are held by the United Kingdom (16%), Japan (12%), Netherlands (11%), Germany (11%), and France (10%).

Foreign Investment Outlays in the United States
by Type of Investment, 1999-2004
(millions of dollars)

<table>
<thead>
<tr>
<th>Type of Investment</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Outlays</td>
<td>274,956</td>
<td>335,629</td>
<td>147,109</td>
<td>54,519</td>
<td>63,591</td>
<td>86,219</td>
</tr>
<tr>
<td>U.S. business acquired</td>
<td>265,127</td>
<td>322,703</td>
<td>138,091</td>
<td>43,442</td>
<td>50,212</td>
<td>72,738</td>
</tr>
<tr>
<td>U.S. business established</td>
<td>9,829</td>
<td>12,926</td>
<td>9,017</td>
<td>11,077</td>
<td>13,379</td>
<td>13,481</td>
</tr>
</tbody>
</table>

Source: Foreign Direct Investment in the United States (June 2006), Bureau of Economic Analysis, Department of Commerce

Foreign capital makes an important contribution to the U.S. economy. U.S. affiliates of foreign companies account for 5.3 million jobs and 6% of private sector GDP, while investment by Japanese companies accounts for 600,000 jobs and almost 1% of U.S private-sector GDP (BEA, 2003). For example, in 2005 Honda employed 12,500 persons in Ohio and 19,000 persons nationwide. Toyota estimated it had created over 32,000 direct positions and 386,000 total jobs in the United States, including direct, dealer and supplier employees and jobs created through their spending, with direct investment totaling $13.9 billion dollars in 2005.

(2) Recent Topics

A. State Efforts

Most American states have international affairs offices that promote investment by offering a wide variety of services and information for companies interested in investing in their state. Many states even maintain offices in cities abroad to encourage trade and investment. For example, the South Carolina Department of Commerce provides assistance for international investors on its web site
Its Global Business Development Team provides assistance for foreign investors through three international offices in Tokyo, Munich and Shanghai. According to the Department’s 2005 Capital Investment Report, foreign direct investment accounts for some 127,500 jobs in South Carolina, or 8.4 percent of private industry employment, and $1.26 billion in new investment in 2005 brought more than 3,000 new jobs. Ten Japanese companies have invested in the state. The Department produces a guide book, "Opportunities for Japanese Manufactures in South Carolina" (http://www.sccommerce.com/teamsconfds/JapanManufacturing.pdf), which provides information on South Carolina’s business tax structure and financial incentives, promotes the state’s friendly environment, and surveys the history of Japanese business in South Carolina. Information on the web site of the State of Colorado's International Trade Office (http://www.state.co.us/oed/ito/invest/invest.html) provides information in Japanese, Spanish, German, and French, and the State has a detailed on-line guide for interested investors at http://www.state.co.us/oed/guide.

Foreign affiliates in Colorado employ over 90,000 people, own over $13 billion in property, plant and equipment and pay wages 13% higher than the national average. Another example is the State of Ohio’s International Trade Division (http://www.odod.ohio.gov/itd/), which works to identify prospects for foreign direct investment in Ohio and helps interested businesses. Ohio has over 208,600 people employed at foreign-owned companies; in 2004 alone, new and expanded investment by foreign-owned companies in Ohio exceeded $1.5 billion.

Many states and localities in the United States offer incentives including tax exemptions and targeted investment in infrastructure. However, incentives are just a small part of the success of the United States in attracting foreign investment. It is the investment climate in the United States, based on strong legal institutions, an open economy, an educated and productive workforce, and an attitude that welcomes foreign investment that has made possible the United States’ success in attracting FDI.

(3) U.S. Strengths

The market size and openness of the U.S. economy continue to make the United States an attractive investment destination. In response to corporate scandals in 2001-02, the Government of the United States acted swiftly to improve and strengthen its corporate regulatory systems to restore confidence in capital markets. Since the attacks of September 11, 2001, the United States has been identifying ways to enhance security protection for the country. As it does so, the United States is
striving to ensure that such measures do not hinder trade and investment flows. The Government of the United States is taking this as an opportunity to identify new ways to speed the flow of legitimate business and to increase logistical integration between domestic and foreign businesses. Through the use of IT and other technologies, the United States hopes that legitimate trade and investment can flow in a seamless, secure fashion even faster than before. In designing these new systems, the Government of the United States continues to listen to the views of the private sectors and governments of other countries to ensure that the new measures meet the desired goals without impeding legitimate trade and investment flows.

III. Discussions in the U.S.-Japan Investment Initiative 2005-2006

1. U.S. Concerns

(1) Cross-border Mergers and Acquisitions (M&A)

The Government of the United States called attention to the importance of substantially equal treatment for Japanese and foreign stocks when they are used as “consideration” in triangular mergers under the new Corporate Code. The provisions of the Corporate Code relating to “flexibility of merger consideration” -- which will permit the use of triangular mergers, cash mergers, and other types of mergers using properties other than shares of surviving companies as consideration, including using foreign shares -- will come into effect as of May 1, 2007.

The Government of the United States pointed out that tax treatment would also be an important factor in triangular mergers, and expected taxation measures relating to triangular mergers to be secured before the entry into force of provisions permitting triangular mergers on May 1, 2007. The Government of Japan is studying tax treatment relating to “flexibility of merger consideration” available under the Corporate Code, taking into consideration the appropriateness and equity of taxation and the prevention of tax avoidance, and will reach a conclusion before the related provisions of the Corporate Code come into effect.

The Government of the United States appreciates that the Government of Japan has clarified the interpretation of Article 821 of the Japanese Corporate Code and that the House of Councilors has adopted a supplementary resolution, when this code was passed, which reaffirms that this Article is not intended to disadvantage existing foreign companies in Japan. The Government of the United States also
welcomes the release of a Japanese Ministry of Justice notification “Regarding the
treatment of commercial registration procedures attendant on the execution of the
Corporate Code” that further clarified the purpose and interpretation of Article 821. However, the Government of the United States continues to request that Japan promptly amend Article 821 to ensure that new restrictions and liabilities are not placed on legitimate businesses.

The Government of the United States has also said that the objective of
defensive measures against takeover should be to raise corporate value and not to
defend management’s own interests. In response to this, the Government of Japan explained the concept of reasonable defensive measures against hostile takeover attempts as concluded by the study group on corporate value established under METI. In addition, the Government of Japan released indicative guidelines that provide rules for reasonable defensive measures, including a principle that the objective of defensive measures against takeover should be to secure and increase corporate value and the common interests of all stockholders.

(2) Demographic Issues and Investment

The Government of the United States has requested that Japan improve its
investment climate especially in the fields of education and medical services, where the United States is confident its companies could provide high-quality services to satisfy the needs of Japanese society as it faces a declining birth rate and aging population.

A. Education

As a result of the reform introduced in December 2004, students who have finished courses at foreign university branches in Japan can be considered for admission into Japanese universities/colleges in appropriate programs, on condition that those branches are officially designated by the Ministry of Education, Culture, Sports, Science and Technology (MEXT) of Japan as meeting certain prerequisites. This has led to eased student access to discount rail passes and clarified the residence status of foreign students in designated foreign university branches in Japan. The Government of the United States welcomes this reform, and at the same time requests that Japan act more promptly in processing foreign universities’ applications for this designation.

In addition, the Government of the United States has asked that the taxation of foreign university branches in Japan should be the same as for Japanese educational
institutions, and further requested that the Government of Japan should implement a nationwide measure or alternatives.

The Government of Japan has been making efforts to provide prompt official designation of those foreign university branches who applied under MEXT’s procedure. To date, three U.S. universities’ Japan branch campuses have been so designated, and a fourth U.S. university’s application is under consideration by MEXT. Regarding tax treatment, the Government of Japan explained that it would work within the framework of existing systems so that foreign university branches in Japan could take practical and reasonable steps to address the issues they have raised.

The Government of the United States appreciated the efforts by the Government of Japan and also requested that discussion continue.

**B. Medical Services**

The Government of the United States expressed its active support for healthcare reform in Japan, noting that American businesses including pharmaceutical companies and medical equipment companies have already established themselves as leading players in the Japanese market, and particularly mentioned the following three points:

First, the Government of the United States requested Japan to allow commercial firms to enter the medical services business, in order to increase the pool of capital available to medical institutions and improve productivity. The Government of the United States said that, while the special deregulation zone program in Japanese structural reform had in principle made it possible for commercial firms to enter hospital operations, actual approval of such zones had been quite limited and was ineffective in facilitating the entry of commercial firms into hospital operation. The Government of the United States suggested that Japan should ease the requirements for establishing special zones to provide treatment using advanced medical technology. The Government of Japan is planning to introduce a scheme that allows medical institutions meeting certain prerequisites to issue publicly-offered bonds as a means of raising funds. At the same time, the Government of Japan disagreed on the need to ease requirements for medical special zones, noting that one application for a special zone submitted by one local government had been approved in July 2005, and that officials had received some further inquiries about the possibility of starting hospital operations in the designated special zones.

Secondly, the Government of the United States noted that outsourcing of diagnostic blood testing in Japan had yielded significant efficiency gains and requested
that outsourcing to commercial firms of other low-risk, repetitive medical treatments and examinations such as MRI, PET and CT imaging, be allowed with greater flexibility. The Government of Japan responded that non-doctors should not be allowed to perform medical procedures because they were not low-risk for patients and reiterated that commercial firms, which cannot operate medical institutes, are not permitted to provide medical services even if they employ doctors to do so.

Thirdly, the Government of the United States expressed interest in the introduction of “mixed medical services” (that is, services including both treatments reimbursed under Japan’s public health system and other treatments not approved for reimbursement). In its view, such services could reduce medical expenses, promote efficiency and mitigate financial pressure on the medical insurance system. The Government of the United States also believes that the current scheme is extremely restrictive. The Government of Japan maintains the principle that the public health insurance system should basically ensure all necessary medical treatment for the insured, and thus the Government of Japan does not share such views. According to this principle, and taking into consideration patients’ welfare, the Government of Japan has decided to implement reform in accordance with the fundamental agreement made in December 2004 on the issue of “mixed medical services” between the Minister of Health, Labour and Welfare and the Minister of State for Regulatory Reform. So far six new treatments, which are not necessarily advanced, have been approved.

(3) Labor-related Laws and Systems

The Government of the United States suggested that improving labor mobility would be a key to maximize the value of organizations, highlighting the following four requests:
- Raise tax-deductible contribution limits for defined contribution pensions; allow employees to make contributions, instead of having them deducted from their salary; and allow investment advice to be made available as an optional service, to assist participants in determining optimal investment strategies and ensuring that proper actions such as portfolio rebalancing are performed in a timely manner. The U.S. Government suggested that these changes would make such plans more attractive, which would be beneficial to employees as well as employers.
- For disputed dismissals, introduce monetary settlements as an alternative to reinstatement in the former position.
- Introduce a white collar exemption that would replace the current working hours
scheme for supervisory and managerial employees under the Labor Standards Act, in order to better foster workers’ abilities.

- Ease regulations under the Worker Dispatch Law to provide workers with increased employment opportunities, including for those who prefer to work limited hours or enjoy greater workplace freedom.

In response to the above suggestions, the Government of Japan explained as follows.

Non-taxable contribution limits on defined contribution pension plans were raised in October 1, 2004, following review of the benefit levels for public pension plans. The Government of Japan believes that it is necessary, at the current moment, to observe utilization of these plans following implementation of the increased limits. The Government of Japan expressed its view that contributions by employees have the same characteristics as personal savings, since employee contributions are optional and each employee chooses the way to manage the reserved funds. Therefore, the Government of Japan currently does not intend to introduce a scheme to allow employee contributions. Based on the legal provision, the Government of Japan will consider the necessity of the revision of the Defined Contribution Pension Law when five years will have passed since its implementation, in October 2006, taking into account input from interested parties.

Concerning the rules of dismissal, Article 18-2 of the Labor Standards Law is aimed at avoiding conflicts and settling a dispute by clarifying the rules of dismissal in advance.

The Government of Japan is planning to promote discussions for clarification of the rules concerning labor contracts, taking into consideration current circumstances in which individual labor-related disputes are increasing over the issue of dismissal.

The Labour Standards Law provides for extra pay for those workers who are asked by their employer to work overtime under a labor-management agreement. It also provides an exception for persons in supervisory or managerial positions. Because of diverse work patterns, even certain workers in non-managerial positions are regarded as included in this exception. The Government of Japan is planning to discuss the system that enables workers to work autonomously under light supervision and what the scope of exception should be in this case.

The Government of Japan further explained that the 2003 amendment of the Worker Dispatch Law is based on the basic philosophy that dispatched workers should be positioned as a temporary workforce within the context of traditional Japanese
employment customs to respect long-term employment. The Government of Japan also explained that they do not see any grounds at this moment to abolish restrictions on dispatch duration.

(4) Translation of Japanese Laws and Regulations into Foreign Languages

The Government of the United States welcomed the Government of Japan’s project to prepare translations of Japanese laws and regulations into foreign languages, noting that this would contribute to increased transparency for foreign investors, and requested that close consultation with the foreign business community be continued as this project is implemented and that sufficient funding be allocated to ensure its success.

On March 23, 2006, the Government of Japan decided to take necessary measures so that English translations of approximately 200 laws and regulations would be produced under the Translation Development Program for FY2006-2008. This decision was based on the final report made by the “Study Council for Promoting Translation of Japanese Laws and Regulations into Foreign Languages,” composed of experts as well as relevant ministries and agencies. In April 2006, the Government of Japan started providing information on this project at the Cabinet Secretariat’s website (http://www.cas.go.jp/jp/seisaku/hourei/data1.html). The Government of Japan will make efforts to ensure the successful implementation of this Program.

2. Japan’s Concerns

(1) Visas

The Government of Japan has expressed its desire that measures taken by the United States to improve border security are implemented in a way that minimizes negative impact on Japanese visa applicants. In Investment Initiative meetings, the Government of Japan expressed its concern about the high travel cost, delays, and inconvenience of applying for a visa since U.S. missions accepting visa applications are limited to Tokyo, Osaka and Naha.

The Government of Japan pointed out that current visa revalidation procedures, which requires applicants to apply outside the United States for interview and collection of biometric data, imposes significant burdens on legitimate Japanese businesspeople and their families staying in the United States. The Government of
Japan also requested that the Government of the United States resume visa revalidation within the United States.

U.S. consular experts at Investment Initiative meetings pointed out several measures taken by the Department of State to improve visa issuance, including adoption of a web-based appointment system that allows applicants to apply at the consulate of their choice and augmentation of visa positions at U.S. missions in Tokyo and Osaka. In particular, in April 2006 the United States introduced a pilot program to conduct non-immigrant visa interviews in Sapporo on a monthly basis and will evaluate this program to consider whether it warrants expansion to other posts in Japan.

U.S. consular experts explained that collecting biometric data during the revalidation process is a legal requirement and that it is technically impossible to collect such data within the United States. As a result, Japanese businesspeople must renew visas at U.S. missions overseas that issue visas, which include Tokyo, Osaka, Naha and Sapporo in Japan. The system allowing appointments to be made up to three months in advance at U.S. missions in Japan eases the difficulties of scheduling trips to Japan to revalidate these visas. More detailed information is available at the following websites: http://tokyo.usembassy.gov and http://travel.state.gov/visa_services.html. Japanese businesspeople may also apply for renewals at U.S. embassies and consulates in Canada or Mexico. These embassies and consulates offer an appointment system through their websites, accessible at http://www.nvars.com. While some posts do not currently offer visa revalidation for third country nationals, the Department of State is exploring improved information sharing that will make it easier for some applicants to apply for renewals outside their home countries. The Department of State and the Department of Homeland Security are working cooperatively toward improving visa revalidation procedures worldwide.

(2) Cargo Security

The governments of the United States and Japan share the view that it is important to take into account the need to facilitate international trade while improving transport security.

The Government of Japan expressed concern that U.S. requirements to provide cargo manifests twenty-four hours in advance of lading for maritime shipments, under the Trade Act of 2002, would cause delays and additional expense for shippers. Moreover, the Government of Japan requested that greater flexibility be used in
applying the manifest rule to C-TPAT (Customs-Trade Partnership Against Terrorism) members, which represent a lower risk from a security viewpoint. Noting that most of the security measures applied to trading companies and their supply chain after September 11 attack have had a costly impact on their operations, the Government of Japan recommended the United States to evaluate the reasonableness of security measures which have already been introduced. The Government of the United States advised that the cargo manifest requirement is an essential element of its counter-terrorism efforts which would continue, but it also explained that the 24-hour period could begin as soon as the container was sealed, even at the point of production. Since the attacks of September 11, 2001, the overall inspection rates for cargo entering the United States have doubled; however, inspection rates for C-TPAT participants are only 1/6th that of non-C-TPAT companies. The Government of the United States welcomes discussions with the Government of Japan and is exploring how to extend further the advantages of C-TPAT membership to maritime shippers. The Government of the United States will ensure transparency in the process of implementation and further revision of C-TPAT. Both Governments desire to facilitate legitimate trade while recognizing the need to continue to improve transport security and make every effort toward enhancement of compatibility between trade facilitation and security.

(3) Exon-Florio Provision

In the United States, Section 721 of the Defense Production Act of 1950 (the “Exon-Florio provision”) provides authority to the President to suspend or prohibit any foreign acquisition, merger or takeover of a U.S. corporation that is determined to threaten the national security of the United States. While the Government of Japan understands the necessity of regulations for national security reasons, it is concerned that the mechanism lacks predictability and transparency and thereby inhibits investment. Japan has also expressed concerns about pending legislation to amend Exon-Florio.

In response to Japan’s concerns, the United States has noted that the Exon-Florio provision is implemented by the Committee on Foreign Investment in the United States (CFIUS), which seeks to serve U.S. investment policy through thorough reviews that protect national security while maintaining the credibility of the traditionally open investment policy of the United States. Implementing regulations have established a voluntary system of notification. CFIUS encourages parties to
transactions that may be particularly complex to pre-notify CFIUS of their intent to file a voluntary notification. Reviews are conducted on a transaction-by-transaction basis. Because the process deals with national security and business proprietary information, the Exon-Florio provision provides that information supplied by the companies contemplating a transaction is held confidential and is not made public, except in the case of an administrative or judicial action or proceeding. The President retains the authority to review concluded transactions only when the transactions were not notified to CFIUS, or in cases where parties have omitted material information or submitted false or misleading material information during CFIUS review.

The Executive Branch of the U.S. Government supports improvements to the CFIUS process to reflect the post-September 11 security environment. While not yet taking a formal position on any pending legislative proposals, the Executive Branch has stated to Congress that such improvements should be guided by the following principles:

- To update the CFIUS process to further integrate national and homeland security interests for a post-September 11 environment;
- To continue to welcome investments in the United States; and
- To preserve what works about CFIUS, and improve and update where needed, while maintaining the integrity of the decision-making process.

In implementing these principles, the Executive Branch has indicated it will work to update the scope of national and homeland security considerations; preserve the professionalism and independence of CFIUS security reviews, and protect sensitive proprietary information provided by companies; strengthen scrutiny of CFIUS cases involving state-controlled companies; and improve the transparency of decisions to Congress so that it can fulfill its important oversight responsibilities.

IV. Conclusion

Five years have passed since the June 2001 establishment of the Investment Initiative under the framework of the U.S.-Japan Economic Partnership for Growth, and the two governments’ activities to further improve the investment climate in their respective countries and raise people's understanding of the role of inward direct investment have taken root. Moreover, the public programs under this Investment Initiative are effectively working not only to publicize the benefits of inward FDI but also to provide opportunities for companies of both countries to meet and discuss
concrete business opportunities that have facilitated investment, job creation and growth.

In Japan, recent movements to promote reform and the combined efforts of central and local governments to promote FDI have brought about a steady increase in inward investment toward the target set by Prime Minister Koizumi of doubling the stock of FDI. At the same time, during the Japan Investment Council meeting held in March 2006, a new target was set to further increase FDI into Japan to the equivalent of 5% of the country’s GDP by 2010. This new target requires the implementation of additional measures, and accordingly the Government of Japan needs to work toward further improvement of the business environment through continued efforts to address issues identified in the Initiative.

In the United States, FDI from Japan continues to grow, registering a 10% increase from the previous year in 2004. Japan is ranked second among all countries in terms of the amount of investment in the United States. While there has been some concern that national security measures triggered after the September 11 terrorist attack could make trade and investment procedures more complicated, creating a bottleneck either for investment from Japan and elsewhere or for corporate activities within the United States, efforts to maintain the openness of the economy have allowed U.S. investment growth to recover from the global slowdown after September 11. The Government of the United States carefully considers opinions and suggestions from Japan and will continue to take these views into account in its efforts to ensure that measures which strengthen national security at the same time contribute to the growth of trade and investment.

The U.S.-Japan Investment Initiative will continue its activities under the direction of the leaders of the two countries. Both governments will continue efforts to promote measures for the improvement of the investment climate in their respective countries with an understanding of the significance of this Investment Initiative and FDI for further growth of both economies and their important role in the global economy.
Appendix 1: Invest-in-Japan Symposiums

Every year, the U.S.-Japan Investment Initiative holds symposiums in the United States to give publicity to the Japanese investment environment, as well as seminars in local cities in Japan to lecture on the mutual benefits obtainable from foreign direct investment.

In November 2005, when the Initiative entered its fifth year, Invest-in-Japan symposiums were held in New York and San Jose.

The symposiums pay close attention to regional characteristics so that useful information about the Japanese investment environment can be directed to the needs of participants. The symposium in New York targeted retailers and the service industry, and the San Jose symposium targeted information technology business.

Both symposiums included panel discussions by entrepreneurs and experts from both countries that fostered active debates and information exchanges to provide insight into the Japanese investment environment and successful examples of direct investment in Japan. The exchange of opinions gave the 200 participants in the two symposiums a good opportunity to learn about the Japanese investment environment, contributing to mutual understanding between the two countries.

While investment seminars in Japan were held in the spring of every year in the past, this year the two governments decided that the seminars would benefit from integration into an international event in order to attract more corporate participants from the United States. The next seminars are planned for Sendai and Yokohama in October 2006, in conjunction with the CATEC (Combined Exhibition of Advanced Technologies) exhibition to be held in Chiba at that time.
Appendix 2: Examples of Recent Entries of the U.S. Companies

Many U.S. companies invested in Japan with the support of JETRO's Invest Japan Business Support Centers (IBSCs). The following five companies all entered the Japanese market in 2005.

○ **Proofpoint Japan KK**

This company develops software for computer protection against spam emails. The Japan branch was established in Tokyo in May 2005, aiming to expand its customer base and promote customer support services in the Japanese market. Proofpoint's entry into Japan took advantage of a new business opportunity generated by the entry into force of the Japanese Law on the Protection of Privacy Regarding the Processing of Personal Data. The company is planning to expand its business in the Asian market after first consolidating its position in Japan first. JETRO assisted the company in collecting information on the tax systems and labor-related laws and in conducting publicity activities.

○ **Tetra Tech Japan**

Tetra Tech is a major American company that provides consultation services concerning the environment and technological services. The company is especially well known for its high-level technology and rich experience in water purification projects and gas/oil-related projects. The Japan office was established in May 2005 as a base for expanding environmental business projects in the Asia Pacific region. In addition to supporting the company start-up, including free office space and consultation on legal matters, JETRO assisted the company in collecting information on traditional bidding procedures for public works in Japan as well as on water quality-related projects.

○ **Rimage Japan Co., Ltd.**

This company manufactures and markets DVD and CD vending machines (for on-site writing of DVD and CD contents). The Japan branch was established in Tokyo in May 2005 as the first step in entering the Asian market. JETRO provided the company with consultations on legal procedures and also helped them to arrange appointments with lawyers and accountants.
GEOVECTOR K.K.
This company develops applications for cellular phones. The Japan branch was established in June 2005, aiming to launch a new service based on geographical location information technology. JETRO provided the company with consultations on corporate registration and also assisted them in finding an office and collecting market information.

eRide Asia Pacific Limited
This company develops and markets IC chips and supersensitive low-power Global Positioning Systems (GPS). The Japan branch was established in Tokyo in September 2005 following a decision by the Ministry of Internal Affairs and Communications to promote the use of cellular phones with a built-in GPS function beginning in 2007. JETRO assisted the company with company establishment procedures and in seeking human resources in the fields of legal affairs, real estate, distribution, accounting, etc.
Appendix 3: Accomplishments over the Past Five Years

During the five years since the U.S.-Japan Investment Initiative was established in June 2001 by the U.S. and Japanese leaders under the framework of the U.S.-Japan Economic Partnership for Growth, Japan and the United States have exchanged various opinions regarding the improvement of the investment climate of their respective countries. Through the exchanges, many improvements have been made to the investment environment by the two countries, and we take this opportunity on the fifth anniversary to review those improvements with the aim of further advancing such measures in the future.

1. Accomplishments of Japan

Corporate Governance

The amendment of the Commercial Code in May 2002 made it easier for Japanese corporations (kabushiki-kaisha) to adopt an American-type corporate governance structure. The corporate governance structure introduced by the amendment is more familiar to foreign investors and thus it promotes their investments. The amendment made it possible to choose a corporate governance structure with three board committees -- the appointment, audit and remuneration committees, each of which must consist of at least three directors with a majority of outside directors -- as well as one or more statutory officers (shikkou-yaku) responsible for conducting business operations without a traditional statutory auditor. Under this structure, a statutory officer may decide important matters (including issuance of new stocks and corporate bonds) which would require resolutions by the board of directors under the traditional-type governance structure.

The Corporate Code, which came into force in May 2006, requires all large corporations and corporations with committees to adopt a basic policy with respect to the establishment of internal control systems to ensure appropriate operations of such corporations, including a system to ensure that all actions by directors or statutory officers (as the case may be) conform with applicable laws and regulations and the articles of incorporation.

Increase in Labor Mobility

The defined contribution pension plan was introduced in 2001 to provide a new pension option to supplement benefits under the public pension plan. It is a
portable pension plan so it plays an important role in promoting labor mobility which facilitates FDI. As of March 31, 2006, there were 1866 officially approved statutes for corporate pensions with 1,733,000 enrollees.

**Services in Specialized Fields**

Investors need access to lawyers and certified public accountants with special knowledge to help them navigate Japanese laws and systems while pursuing FDI in Japan. The Cabinet decided in March 2002 to launch a plan for promoting judicial system reforms, including setting a target to increase the yearly number of examinees who pass the National Bar Examination of Japan to about 3000 persons around 2010.

In addition, a bill was submitted to the Diet in 2003 to amend the Court Organization Law for Justice System Reform, including an amendment of the Special Measures Law concerning the Handling of Legal Business by Foreign Lawyers (the “Gaiben Law”). The purpose of this amendment to the Gaiben Law was to promote cooperation and collaboration between Japanese lawyers and foreign lawyers registered in Japan. The overall amendment took effect on April 1, 2004, with the principal part of the Gaiben Law amendment taking effect on April 1, 2005.

The government has also promoted reform of overall systems related to certified public accountants, including the examination system.

**Cross-border Mergers and Acquisitions (M&A)**

The amended Special Measures Law for Industrial Revitalization, designed to promote cross-border mergers and acquisitions (M&A), entered force in April 2003. It introduced special measures as exceptions to the Commercial Code that permit mergers using stocks of a parent company as a consideration (triangular mergers) or mergers using cash as consideration (cash-out mergers), subject to appropriate permission from a minister in charge. Under the amended law, it is possible to use stocks of a foreign parent company or cash as consideration in mergers or other similar transactions. This means that a foreign company may, with its own stocks or cash as consideration, use mergers and other similar transactions when it acquires a Japanese company through its Japanese subsidiary.

In addition, under the new Corporate Code, it is possible for mergers to use cash or other properties (stocks of a parent company, in the case of a triangular merger), instead of stocks of a surviving company as a consideration (this new rule will go into effect on May 1, 2007).
Revision of Accounting and Auditing Systems

Accounting and auditing, which are basic infrastructural services for capital markets, play an important role in improving the investment environment.

As for accounting, the Government of Japan has developed a number of new and revised accounting rules related to principles of consolidated financial statements, fair value accounting for financial instruments, accounting for income taxes, retirement benefits and impairment of assets. On auditing, in May 2003 the Certified Public Accountant Law was revised (effective April 2004). Based on the revised law, measures for prohibiting accountants from providing their clients with non-auditing services such as consulting were introduced to strengthen auditor independence, and the Certified Public Accountants and Auditing Oversight Board (CPAAOB) was established.

These developments continuously improved the quality of accounting and auditing, and enabled investors to access more useful accounting information, including accurate financial information needed in M&A transactions. They were in line with international developments and contributed to improvement of the investment climate.

Education

The Government of Japan established a study group on the issue of university quality assurance to respond to the internationalization of higher education. This study group concluded that the following two options should be available to foreign university branches in Japan: (i) foreign university branches in Japan that seek a status equal to that of Japanese counterparts should apply through the official certification process based upon the standards for establishment of universities, which are applied equally to Japanese counterparts, and (ii) foreign university branches in Japan recognized in their home country as legitimate universities are to be given the status of “foreign university” in Japan. As a result, a reform was introduced in December 2004 which paved the way for foreign university branches in Japan to obtain a status in the Japanese education systems.

As a result of this reform, students who have finished courses at foreign university branches in Japan are entitled to admission into Japanese universities and colleges based on the types of the courses taken, on condition that those branches are officially designated by MEXT to meet certain prerequisites. This reform also resulted in improvement of the situation concerning the issues of student discount rail passes and the residence status of foreign students in foreign university branches in Japan.
Up to the present, three U.S. university branches in Japan have been officially designated by MEXT.

Medical Treatment

The Government of Japan determined in February 27, 2003 that commercial firms should be permitted to enter the business of hospital operation in Japan. This decision allowed firms to practice advanced medical technology not covered by the public medical insurance system in such fields as reproductive medicine, genetic treatment, and cosmetic surgery using the exemption measure available for special zones for structural reform under the management of the Headquarters for the Promotion of Special Zones for Structural Reform. To implement this decision, a bill on relevant matters was brought to the Diet and approved in May 2004, and has been in effect since October of that year. In May 2005, one local government submitted applications for the official designation of specific regions as special zones under this system, and this application was approved in July 2005.

Regarding “mixed medical services,” the Government of Japan has decided to implement a reform in accordance with the fundamental agreement made in December 2004 on the issue of “mixed medical services” between the Minister of Health, Labor and Welfare and the Minister of State for Regulatory Reform. So far, six new treatments, all under the category of “not necessarily advanced,” have been approved.

Translation of Japanese Laws and Regulations into Foreign Languages

The government’s project is underway to translate Japanese laws and regulations into foreign languages (English translations to be produced first) with the goal of increasing transparency for foreign investors. Under this project, the Government of Japan will take necessary measures to produce English translations of approximately 200 laws and regulations in accordance with the Translation Development Program for FY2006-2008.

2. Accomplishments of the United States

Visa Issuance and Revalidation

The United States has undertaken a number of measures designed to improve security while making it easier for legitimate travelers to obtain visas and renew them, including for investors from Japan. Since October 26, 2004, biometric visas must be issued to all travelers who require a visa, which requires a personal appearance by
most applicants. The Department of State has adopted a web-based appointment system, which allows applicants to apply up to three months in advance at the consulate of their choice, and added new visa officers at U.S. missions in Tokyo and Osaka. These measures have significantly reduced the visa processing backlog in those posts. To reduce the cost of travel from northern Japan for visa interviews, the Department of State initiated a pilot program to conduct in-person non-immigrant visa interviews at the U.S. Consulate in Sapporo on April 19, 2006. The Department of State is evaluating this pilot to determine whether this program warrants further expansion. Visa holders can now use the web-based appointment system to facilitate renewal during travel. While some posts do not currently offer visa revalidation for third country nationals, the Department of State is exploring improved information sharing that will make it easier for some applicants to renew their visas outside their home countries.

Cargo Security

The United States strengthened rules and programs addressing cargo security in the wake of the September 11 attacks and continues to look for ways to improve both the security and efficiency of trade. The U.S. Bureau of Customs and Border Protection (CBP) and Japanese Customs’ authorities have worked closely in implementing these changes. Under the Container Security Initiative (CSI), Japanese Customs teams have been stationed at the ports of Long Beach. Yokohama became a CSI port in 2003, Tokyo became operational in May 2004, and Nagoya and Kobe were brought into the program in August 2004. CBP published final rules on the advance collection of cargo manifest information on December 5, 2003. An essential element of U.S. counter-terrorism efforts, these rules were necessary to improve security and to ensure the smooth flow of trade and are applied to all shippers, domestic and foreign. Under the Customs-Trade Partnership Against Terrorism (C-TPAT), certified shippers receive reduced container inspections by U.S. Customs based on their commitment and active participation in the program. Since the attacks of September 11, the overall inspection rates for cargo entering the United States have doubled; however, inspection rates for C-TPAT participants are only 1/6th that of non-C-TPAT companies.

Sarbanes-Oxley Act of 2002

Reforms to U.S. securities law contained in the Sarbanes-Oxley Act have raised concerns that conflicts may exist between U.S. and foreign requirements for internal oversight standards. The Securities and Exchange Commission (SEC) made
a concerted effort, including holding public roundtables and soliciting public comments, to gain a better understanding of these concerns and, as a result, has made many accommodations for Japanese and other foreign market participants. For example, the SEC adopted a rule that provides a limited exemption from Sarbanes-Oxley requirements for jurisdictions such as Japan with boards of auditors or statutory auditors. The SEC remains willing to receive further information regarding the effect on individual firms of a provision requiring independent auditors when an auditing committee system is used. The Public Company Accounting Oversight Board (PCAOB) and the SEC have issued a rule allowing foreign public audit firms to provide less information in registering than originally proposed, and a mechanism has been included to permit foreign firms to document non-disclosure of certain information that is confidential under home country rules. The PCAOB has proposed rules regarding how it would cooperate with foreign audit oversight bodies in the inspection of foreign registered firms and continues to discuss with foreign governmental bodies the scope of its oversight authority with respect to accounting firms located outside the United States. With regard to internal control over financial reporting, the compliance date for foreign private issuers including Japanese firms has been extended one year to their first fiscal year ending on or after July 15, 2006.

### Exon-Florio Provision

Section 721 of the Defense Production Act of 1950 (the “Exon-Florio” provision) provides authority to the President to suspend or prohibit any foreign acquisition, merger or takeover of a U.S. corporation that is determined to threaten the national security of the United States. In response to Japan’s concerns that the mechanism lacks predictability and transparency and thereby inhibits investment, the United States has provided extensive information about the process. While not yet taking a formal position on any pending legislative proposals to amend Exon-Florio in light of the post-September 11 security context, the Executive Branch has indicated it will work to update the scope of national and homeland security considerations: continue to welcome investments in the United States; preserve the professionalism and independence of CFIUS security reviews, and protect sensitive proprietary information provided by companies; strengthen scrutiny of CFIUS cases involving state-controlled companies; and improve the transparency of decisions to Congress so that it can fulfill its important oversight responsibilities.
Requirements for Drivers' Licenses

The Social Security Administration (SSA) ended the assignment of non-work Social Security Numbers (SSNs) for the purpose of driver's licensing on October 27, 2003, after publication of the proposed rule in March 2003. In response to a request from the Government of Japan during the public comment period, the SSA, with the assistance of the American Association of Motor Vehicle Administrators and the support of the Department of Transportation, assisted several states that required SSNs for driver's licensing to develop alternative identifier systems. All states but Illinois had taken steps to resume issuing driver's licenses in this situation by November 2003. Following passage of a bill by the Illinois General Assembly in May 2004 and approval by the Governor of Illinois, foreign citizens temporarily residing in that state were allowed to obtain driver's licenses without a SSN on January 1, 2005.

International Investment and Trade in Services Survey Act (IITSSA)

In response to a request from Japan to ease the reporting burden under the IITSSA, the United States undertook to minimize the amount of information required. A new electronic filing system further eased collection of this data.

Investment in Areas Outside of Tokyo

To assist Japan in revitalizing local economies and encouraging investment in local areas, the United States agreed to work closely with Japan to assist local areas in understanding what business environment best attracts investment. As part of this effort, the United States has participated in a series of seminars in various Japanese and U.S. cities and sponsored the first official U.S. investment missions to some of these areas. These investment seminars have continued to be an important avenue to promote U.S. direct investment in Japan and to raise local understanding of the role that policy plays in promoting investment.