

**Toward a Stronger Economic Partnership Between Japan and Canada:
Interim Report of the Task Force on the Japan-Canada Economic Partnership
Of the Committee on Canada**

26 August 2004

The Committee on Canada, Nippon Keidanren

Introduction: The Need for a Stronger Canada-Japan Economic Partnership

Current State of Canada-Japan Economic Relations:

Canada-Japan economic relations have proceeded quite smoothly in recent years, without any serious friction occurring. Nevertheless, trade and investment are at low levels relative to the size of the economies of the two nations.

At the same time, Canada's reliance on exports to the United States has increased since establishment of the North America Free Trade Agreement (NAFTA), while China has grown increasingly important as a source of imports, pulling ahead of Japan into a number two ranking.

Canada has the eighth largest economy in the world, and is a member of the quadrilateral trade forum and the G8. Further expanding and deepening economic relations between Japan and Canada is a matter of great significance to both countries.

Establishment of the Task Force on the Japan-Canada Economic Partnership

Dating back to when its name was the Canada-Japan Economic Committee, the Committee on Canada, through such venues as the Canada-Japan Business Conference, has long engaged in the deliberation of policies aiming at strengthening the Canada-Japan economic partnership. Efforts are also afoot at the government level. In a sub-ministerial economic agreement reached this past March, the two sides agreed to discuss a way for promoting two-way trade and investment in order to inject new life into Canada-Japan economic relations.

Building on this foundation, Nippon Keidanren this past May set up the Task Force on the Japan-Canada Economic Partnership (chaired by Hiroshi Zaizen, Chairman of the Committee on Canada's Steering Sub-Committee and corporate advisor to Mitsubishi Corporation) under its Committee on Canada with an eye to discussing matters relating to barriers to business and the framework needed for further strengthening of the Canada-Japan economic partnership. This Task Force has convened three times thus far to discuss issues relating to the strengthening of the Canada-Japan economic partnership. In addition to soliciting the views of the members of the Committee on Canada and of representatives from Canadian firms operating in Japan, the Task Force has conducted a "Questionnaire on Strengthening of Canada-Japan Economic Partnership" to the Nippon Keidanren's various committees such as the Committee on Canada, the Committee on US Affairs, and the Committee on Trade & Investment.

What follows is the Interim Report drawn up on the basis of these discussions.

Contents of the Interim Report

Introduction: The Need for a Stronger Canada-Japan Economic Partnership

1. An Analysis of the Canadian Market and Its Significance
2. Barriers to Canada-Japan Business
3. The Need for a Framework for Strengthening of the Canada-Japan Economic Partnership
 - (1) Efforts to Establish a Canada-Japan Agreement on Economic Partnership
 - (2) The Need for a “Framework” for Strengthening of the Canada-Japan Economic Partnership
 - (3) Thoughts on a Canada-Japan FTA/EPA
 - (4) Top-Priority Issues in the Effort to Strengthen the Canada-Japan Economic Partnership

Conclusion: Toward Strengthening of the Canada-Japan Economic Partnership

1. An Analysis of the Canadian Market and Its Significance

(1) Canada’s economic significance to Japan: Principal trading partner, manufacturing base for the NAFTA market

The base of the bilateral economic relationship is a complementary trading relationship based on Japan’s export of finished goods and machinery, and its import from Canada of resources and products in the agriculture, forestry, and fisheries sectors. Atop this foundation, there is two-way investment. Japan sees Canada as a base for the manufacturing of finished goods for the larger NAFTA market.

(2) Evaluation of the Canadian market

The results of the Task Force questionnaire indicate that the strengths of the Canada market are a number of infrastructure advantages, including excellent human resources, sophisticated technology, political and economic stability, a transparent legal system, its status as a prime place for locating businesses due to its proximity to the US market, and low-cost energy.

On the negative side, Canada has high taxes, overlapping federal and provincial regulation, high labor costs, lengthy labor-management negotiations as a result of strong labor unions, and burdens imposed by the requirement for bilingual English and French documentation.

(3) The future of the Canada market:

The results of the questionnaire show that Japanese firms doing business with Canada expect their exports to/imports from Canada to “either expand or remain stable” over the next ten years (see Table 4 in the attached questionnaire results). Reasons given for this expectation include Canada’s economic stability, an expanding NAFTA market, and economic recovery in Japan.

2. Barriers to Canada-Japan Business

(1) Canada's business barriers

The business barrier on the Canadian side most frequently mentioned in the questionnaire was "The requirement that directors be Canadian nationals," followed by "Slow issuance of visas to Japanese expatriates and their family members, and complicated application procedures," "Unemployment insurance and pension premiums," and "Taxation of transfer pricing" (see Table 5). As for the obtaining of visas, there was a complaint that "it has been necessary to retain a lawyer specializing in immigration law." These factors all increase costs to Japanese firms doing business in Canada.

Respondents also mentioned the fact that the governments of Japan and Canada take different views of deemed disposal of shares in connection with mergers.

(2) Japan's business barriers

In its Position Paper on Trade Issues in Selected Sectors of the Japanese Market (March 2003), the Canadian Chamber of Commerce in Japan (CCCJ) called for: regulatory reform in the financial services sector (reform of the postal insurance (Kampo) system; greater transparency in the supervisory actions of the Financial Services Agency; revisions to the Commercial Code; judicial reform; changes to competition policy and air transport policy (more runway slots at Narita Airport and reduction of landing fees there); amendment of the Building Standards Law; and amendment of the Food Safety Standards ; no application of safeguard to pork.

(3) Lack of a Canada-Japan social security arrangement; failure to amend the Canada-Japan tax treaty

The lack of a Canada-Japan social security arrangement means significant and unnecessary duplicate pension payments to the Japanese and Canadian pension systems. The CCCJ has long called for the conclusion of a Canada-Japan social security arrangement to resolve this problem. In December 2002, for example, the CCCJ issued its "Request for a Prompt Conclusion of a Canada-Japan Pension Agreement," in which it urged the governments of Japan and Canada to enter into negotiations as quickly as possible aimed at concluding a Canada-Japan social security arrangement, so as to lower the cost of investments between the two countries, and to facilitate easier movement for managerial and technical personnel. This same request was also put forward in May 2002 by the 25th Annual Canada-Japan Business Conference in the executive summaries of the two conference co-chairs, and again in March 2003 by the Toronto Japanese Association of Commerce and Industry in a set of recommendations entitled "Actions to Enhance the Business and Personal Environment Confronting Japanese Business in Canada."

We appreciate the fact that the negotiation of a Canada-Japan social security arrangement will start from this October in response to these requests. We call for the early conclusion of the agreement.

In addition, at a hearing held by the Task Force, the CCCJ representatives spoke about a number of new developments that have reduced the competitiveness of Canadian firms vis-à-vis their US counterparts. The US-Japan Social Security Agreement was concluded this past February, for example, while the amendment to the US-Japan Tax Treaty that was agreed in last November entered into force this past March. To meet these

challenges, the CCCJ representatives once again called strongly for the earliest possible conclusion of a Canada-Japan social security arrangement as well as amendment of the Canada-Japan Tax Treaty to match the content of the new US-Japan Tax Treaty.

Canada-Japan Social Security Arrangement

	Japanese expatriates in Canada	Canadian expatriates in Japan
No. of persons (2001)	1,800	2,294
Max. annual pension premiums (*)	\$1,832	\$5,912

(*1) Premiums paid to other country's pension system during a -year posting in 2004 (after refunded).

(*2) Expressed in Canadian dollars.

(*3) Estimated that the 50 % is refunded.

Source: The Canadian Chamber of Commerce in Japan

Canada-Japan Tax Treaty vs. Japan-US Tax Treaty

	Canada-Japan Tax Treaty	Japan-US Tax Treaty
Dividend income	Parent-subsidiary 5% (with exceptions) Others 15%	Parent-subsidiary Exempt (where certain conditions are met; otherwise 5%) Others 10%
Interest income	10%	10% (Interest received by financial institutions is exempt)
Usage fees	10%	Exempt

Source: Japanese Ministry of Foreign Affairs

3. The Need for a Framework for Strengthening of the Canada-Japan Economic Partnership

(1) Initiatives of Japan and Canada in terms of the Economic Partnership Agreements

Besides working to build up the WTO and various other multilateral trading systems, Japan has also sought actively in recent years to enter into economic partnership agreements with individual countries and regions of importance to our country. In addition to entering into the Japan-Singapore Economic Partnership Agreement (agreed to in 2001, entered into force in 2002), Japan has also begun negotiating economic partnership agreements with Mexico (agreement reached in March 2004), South Korea, Thailand, Malaysia, and the Philippines, and also reached an agreement with Australia in July 2003 on the Australia-Japan Trade and Economic Framework.

Canada, for its part, in addition to NAFTA has also entered into free trade agreements with Chile, Israel, and Costa Rica. It is also negotiating the Free Trade Area of the Americas (FTAA), and is also in talks with four Central American nations and Singapore. Further, Canada also agreed with the EU in March 2004 on the Framework of the Canada-EU Trade and Investment Enhancement Agreement.

(2) The Need for a “Framework” for Strengthening of the Canada-Japan Economic Partnership

In seeking a way to strengthen the Canada-Japan economic partnership, there is much we can learn from the Trade and Economic Framework between Australia and Japan (“Framework”; see the note below, preceded by an asterisk [*]).

Prime Ministers Junichiro Koizumi and John Howard signed the Framework agreement in July 2003. The Framework calls for Japan and Australia to take steps regarding liberalization of trade and investment. The Framework does not represent a binding document in the nature of a bilateral treaty or international covenant, yet it is expected to be effective in promoting bilateral investment, trade facilitation measures (e.g., customs cooperation, etc.), mutual recognition of technical specialist qualifications, and the development of e-commerce infrastructure.

An agreement such as this is not legally binding, yet there is still a very good chance of it promoting closer economic partnership, since once a broad-ranging general agreement like this has been reached, the two countries are likely to engage in regular talks and meetings toward that end. Also, in the midst of weakening Japan-Australia economic relations, the Framework has probably afforded increased opportunities for the two countries to establish forward-looking agreements. Japan and Canada would do well to take the Trade and Economic Framework between Australia and Japan as a model in arriving at some kind of framework agreement of their own. A framework agreement of this sort would eventually serve as a basis for future discussion of a comprehensive FTA/EPA between Japan and Canada.

*** Trade and Economic Framework between Australia and Japan**

The Framework does not represent a binding document in the nature of a bilateral treaty or international covenant. The primary contents includes the following: (1) areas for mutual cooperation, and an action plan (customs cooperation, mutual recognition of technical specialist qualifications, promotion of investment, etc.); (2) joint research by the two governments regarding liberalization of trade in goods and services; and (3) an agreement concerning the impact of trade and investment agreements with third countries.

(3) Thoughts on a Canada-Japan FTA/EPA

Some 70% of the Task Force questionnaire respondents indicated that it would be worthwhile to have a Canada-Japan FTA/EPA.

Many respondents also indicated that “repealing tariffs” would be a good way to spur increased exports to Canada as well as exports of Canadian products to Japan. In addition, large numbers of respondents also felt that “trade facilitation” and liberalization of “personnel movement” would be beneficial (see Table 6).

Japan has entered into economic partnership agreement negotiations with a number of East Asian countries. With progress being made in these negotiations and in the WTO New Round talks, it would be appropriate in the future to have discussions concerning an FTA/EPA with Canada.

Dealing with the agriculture, forestry, and fisheries sectors, which currently account for roughly 60% of Japan's imports from Canada,* presents certain difficulties. We should first agree on the aforementioned framework, and under that framework, work out agreements relating to the less problematic matters first.

There is relatively little trade friction between Japan and Canada. Considering the healthy state of the bilateral economic relationship, how to proceed with cooperative relations and how to inject new vitality into the two countries' economies appear poised to become issues of key importance. When this comes about, it will be necessary to focus on the considerable economic benefits that would flow from an FTA/EPA between Japan and Canada, both of which are members of the G8 and the quadrilateral trade forum.

* Main agricultural, forestry, and fisheries imports from Canada (2002: US\$3.982 billion)

Item	Real tariff rate	Value (US\$1000s)
Logs, lumber, processed lumber	No tariffs, 4.8%-6.0%	1,150,605
Pork	Specific duty, differential duty, or 4.3%	862,827
Coleseed	No tariffs	437,392
Wheat	55 yen/kg	300,597
Crabs	4.0%	131,741
Malt	21 yen/kg	75,508

(Source: JETRO Agrotrade Handbook 2003)

(4) Top-Priority Issues in the Effort to Strengthen the Canada-Japan Economic Partnership

A particularly large number of responses to the questionnaire point to the following three issues as matters deserving the top-priority attention in the effort to strengthen the Canada-Japan economic partnership: (1) conclusion of a Canada-Japan social security arrangement, and amendment of the Canada-Japan Tax Treaty; (2) promotion of two-way investment and tourism; and (3) promotion of cooperation aimed at improving the business environment in China (see Table 8).

(a) Prompt Conclusion of a Canada-Japan social security arrangement, and amendment of the Canada-Japan Tax Treaty

The prompt conclusion of social security agreement between Japan and the various countries to which Japanese expatriates are stationed in large numbers avoids duplicate insurance premium payments and reduces costs to Japanese firms, thereby enhancing the international competitiveness of countries that have entered into such agreements. Also, in the wake of the amendment to the US-Japan Tax Treaty, in order to further promote investment between Japan and Canada, it has now become all the more necessary to amend the Canada-Japan Tax Treaty to match the content of the new US-Japan Tax Treaty. This would lead to closer Canada-Japan economic relations.

It is expected that conclusion of a Canada-Japan social security arrangement and amendment of the Canada-Japan Tax Treaty would benefit both Japan and Canada;

therefore it is advisable that our two governments will enter into talks as soon as possible in order to work toward these ends.

(b) Cooperation aimed at promoting two-way investment

Direct investment in Japan means more to us than just capital. It also helps to revitalize our national economy by bringing in new business models, technologies, managerial expertise, and other business resources. There is a need to promote greater investment in Japan from Canada (which invests little in comparison with other developed nations) and also to promote more direct investment in Canada. (JETRO has been dispatching IT missions to Canada in an effort to expand trade and investment between our two countries' IT sectors).

(c) Cooperation aimed at promoting two-way tourism

Actively promoting two-way tourism is desirable, as the tourism industry has a large economic impact on related sectors such as transportation, hotel business and entertainment. The Japanese government is currently launching the "Visit Japan Campaign" in an effort to double the number of foreign tourists to ten million by the year 2010. As well, the Japan Business Federation has the newly-established Committee on Tourism Promotion (a tentative name) to examine necessary measures to increase the number of foreign tourists to Japan. On the other hand, the following ways has been proposed to increase the number of tourists and other travelers to Canada :

- Improve the image of Canada by strengthening Canadian tourism office's promotion efforts;
- Attract student groups (e.g. for language schools) by appealing merits of Canada such as its safe society
- Encourage Canadian tourism office and provincial governments to publish brochures on international convention facilities in major cities in Canada to attract conventions to Canada.

The prospects of encouraging tourism and commercial exchanges between the two countries at the same time are good.

(d) Cooperation aimed at improving the business environment in China

For both Japan and Canada, the relative importance of the Chinese market is growing. China is Japan's second largest trading partner, after the United States. And for Canada, as well, China has overtaken Japan as the country's second-largest source of imports. China joined the WTO in December 2001, and will hopefully be taking effective and prompt measures to honor its international commitments and carry out domestic structural reforms, as its WTO membership requires. As events unfold, it would most likely be beneficial if Japan and Canada could cooperate with China to help further improve its business environment by taking the following actions:

- Urge the Chinese government to take prompt and effective measures to honor its WTO accession commitments.
- Engage in cooperation to protect intellectual property rights, including measures to deal with the export of counterfeit goods from China.
- Urge the Chinese government to further dismantle its protectionist policies (such as the remission of value-added taxes) vis-à-vis domestic enterprises.
- Urge the Chinese government to be more transparent in its formulation of laws and setting of requirements for the obtaining of licenses and permits.

(e) Other matters

Expanded cooperation between Japan and Canada is also hoped for in the area of global environmental concerns and energy policy (e.g., promotion of joint research on wind and solar power), and also in the entertainment industry, where Canada is strongly competitive (games, software, cinematic special effects, audiovisuals, etc.).

Conclusion: Toward Strengthening of the Canada-Japan Economic Partnership

Japan and Canada enjoy healthy economic relations, but the two countries' interests to each other is gradually waning as the US and Chinese markets assume greater importance to both Japan and Canada. As the questionnaire results show, however, while Canada has relatively few barriers to business, there is nevertheless great room for Japan and Canada to engage in constructive new bilateral relations by cooperating in such areas as the environment, information technology, entertainment, tourism, and the Chinese market. In addition, Canada strongly wishes to strengthen its partnership with Japan. Both the public and private sectors should put forth further effort to expand interchange and strengthen partnership.

Firstly, the two countries' governments should start and promote negotiations aimed at establishing closer economic partnership as soon as possible, such as the "framework agreement" and "Canada-Japan social security arrangement" mentioned in the Interim Report. The business and industrial community must now build on the strong business environment that already exists by forming even deeper economic relations, and by building up a wide range of cooperative relations in a number of new fields that promise to be of benefit to both nations.