Japan's Pork Imports: New Agreement in the Trans-Pacific Partnership Free Trade Negotiations

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Introduction

On October 5, 2015, the 12 countries participating in the on-going Trans-Pacific Partnership (TPP) negotiations reached a broad agreement at the ministerial meeting in Atlanta U.S.A. During the meeting, Japan promised to reduce tariffs on foreign pork once the agreement comes to effect. However, because of the complicated structure of Japan's pork import system, the impact of tariff reduction would not be easy to determine for both foreign as well as Japanese researchers. This paper aims to explain the details of the new agreement on Japan's pork imports and further discuss its impacts on the pork market.

Japan's participation in TPP negotiations

The TPP is an Economic Partnership Agreement among the 12 Pacific Rim countries including Japan, and aims at promoting free trade among the member countries. The Partnership was initiated in 2006 with the four member countries, namely Singapore, Chile, New Zealand, and Brunei[1]. In 2010, negotiations for a new agreement started after including the four new member countries, namely, the United States, Australia, Peru, and Vietnam.

Initially, Japan maintained distance from the TPP and did not partake in the negotiations. On October 1, 2011, however, the then Japanese Prime Minister Naoto Kan stated that his cabinet was seriously considering participation in the TPP negotiations. This was the first time that a Japanese prime minister showed a positive attitude toward the TPP. Since then, Japan's inclusion in the TPP has been ardently discussed in the country. Fearing an influx of low-prices of foreign agricultural products, many agricultural groups were against Japan's participation in the TPP. On the other hand, many commerce and industry groups were supportive of Japan's joining the TPP, recognizing that the TPP would certainly open up various new business opportunities The current Prime Minister Shinzo Abe, who has held office since December 2012, preferred joining the TPP negotiations and promoted trade liberalization. Subsequently, based on Abe's initiative, Japan became a new member of the TPP negotiations on July 23, 2013. In addition to Japan; Malaysia, Canada, and Mexico also joined the negotiations after 2010. Consequently, the TPP currently comprises of the 12 countries.

After joining the TPP negotiations, and in order to mitigate the anxieties of agricultural groups, the Japanese government listed the five items—rice, wheat, meat (pork and beef), sweetening resource crops (sugar canes, beats, and starch), and dairy products—as "sacred agricultural products." The Japanese government has been striving for maintenance special import protections for these five items in the TPP negotiations.

As mentioned earlier, the governments of the 12 member countries reached a broad agreement on October 5, 2015. It should be noted, however, that the agreement is still subject to ratification in each country. The agreement provides member countries two years each for completing the domestic procedures for ratification, after which it should come into effect. If more than six countries, constituting over 85% of the total GDP of the 12 countries together complete the ratification procedures, and the remaining member countries failed, the TPP

* We would like to thank Mr. Akira Shiratake for English language editing.

agreement comes into effect by excluding these remaining countries. Thus, it is still uncertain when and whether the new agreement will become effective.

Gate price system for Japan’s pork imports

Japan’s pork market has been strongly protected by the unique and controversial tariff system, called the gate price system. Before discussing the details of the TPP agreement on Japan’s pork imports, it is necessary to review Japan’s current pork import system[2].

Figure 1 shows the basic structure of the gate price system (note 3). There exists a critical price, called the gate price, whereby the way of accessing tariff differs. Historically, the gate price has been revised according to the changes in the domestic pork market conditions. However, since 2000, the gate price has been fixed as 524 yen/kg. If the c.i.f. price is higher than the gate price, customs apply a 4.3% ad valorem tariff. If the former is lower than the latter, tariff assessment is the higher one from the following two: (1) 482 yen/kg, and (2) the gap between 546.53 yen (the gate price multiplied with 1.043) and the c.i.f. price.

In sum, the gate price system can be considered the combination of specific tariff (if the c.i.f. price is lower than 64.53 yen/kg), *ad valorem* tariff (if the c.i.f. price is higher than 524 yen/kg), and deficit payment type tariff (if the c.i.f. price is between 64.53 yen/kg and 524 yen/kg)[4]. In reality, however, 64.53 yen/kg is so unrealistically low that no imports could be accomplished at this price. Thus, in practice, we can ignore this part of the specific tariff in the current pork import system[5].

In the international pork market, pork is usually marketed in the form of primal cut meat. Pork prices differ according to the parts (for example, high prices for tender loin and low for picnic). However, the gate price system shown in Figure 1 is applied indifferently for all pork parts[6].

Japanese pork farmers often insist that Japanese government should keep the gate price system. They believe that this system should be effective to protect the Japanese pork market from low priced foreign pork. However, experts in the pork business suggest that the gate price system sometime entails tariff evasion problems. Let us assume that a pork importer imports 10 tons of tenderloin at a c.i.f. price of 800 yen/kg and 10 tons of picnic at a c.i.f. price of 300 yen/kg. If a pork importer reports 10,000 kg imports of tenderloin and 10,000 kg imports of picnic separately at customs, the total tariff will be 2,809,320yen (800 * 10,000 * 0.043 + (1.043 * 524 - 300) * 10,000 = 2,809,320). On the other hand, if an importer reports 20 kg imports of pork at a c.i.f. price of 550 yen/kg at customs (combining tenderloin and picnic), the total tariff will be 473,000yen (550*20,000*0.043=473,000). The latter is called a “combination import.” Thus, if a pork importer sets the c.i.f. price equal to the gate price by combining the expensive and cheap parts of pork, the company can easily minimize its tariff burden. Officially, according to the customs, undertaking combination imports to evade tariff (i.e., if a pork importer mixes different types of pork for customs entry) is an illegal action and a penalty could be imposed accordingly. In practice, however, it is difficult to identify combination imports. Generally, a pork importer frequently imports many different cuts, and reporting all imports at customs separately is quite troublesome.

Our previous study shows that a majority of the c.i.f. prices of Japan’s pork imports is close to the gate price[7]. This provides evidence that customs are not able to maintain a strict control over combination imports in practice.

In addition to combination imports, the gate price system has a more fundamental problem. If the international pork price falls below the gate price, importers have no incentive to look for cheaper pork. This is contrary to the discipline of the market economy. On top of that, the gate price system is likely to induce tariff evasion not only through combination imports but also in various other ways. For example, if a pork importer establishes a dummy company overseas and enters into a bogus transaction, the c.i.f. price could be easily manipulated. If c.i.f. prices are lower than 524 and higher than 64.53, a pork importer can evade tariff by reporting higher-than-actual c.i.f. prices. Although everybody knows a bogus transaction is a crime, judging whether one is bogus is often difficult.

In fact, there were well known cases of large-scale tariff evasions on pork imports. For example, in 2012, the Special Investigation Department of the Tokyo District Public Prosecutors Office arrested Kunihiro Dodani and Kenji Shibata on suspicion of tariff evasion of 13 billion yen in pork imports. In 2009, the Special Investigation Department of the Nagoya District Public Prosecutors Office arrested Kazuo Akaogi on suspicion of tariff evasion of 4.5 billion yen in pork imports. Two major pork import companies, namely Narita Foods and Mitsubishi Corporation, were revealed as having committed tariff evasion of 6 billion yen in 2009 and 5 billion yen in 2008, respectively.

Another problem of the gate price system is its inconsistency with the WTO rules. The WTO prohibits deficit payment-type tariffs because they distort the international commodity market. The Japanese government asserts that the gate price system should not be considered deficit payment-type tariffs because it includes both *ad valorem* and specific tariffs. However, it is uncertain whether this assertion is persuasive enough for foreign governments.

TPP agreement on Japan's pork imports

During the TPP negotiations, it was possible for the Japanese government to abolish the gate price system. However, the Japanese government opted to maintain the basic framework of the gate price system with reducing the degree of protection. The detailed agreements of the negotiations, reached at on October 5, 2015, are described below:
(1) The gate price should be maintained as 524 yen/kg.
(2) The specific tariff should be reduced to 125 yen/kg from the first to four years since the TPP agreements become effective. For the fifth year, it will be reduced to 70 yen/kg, and further reduced by 4 yen/kg every year from the sixth to ninth years. For the tenth year and thereafter, it will be fixed at 50 yen/kg.
(3) The 4.3% *ad valorem* tariff should be reduced to 2.2% in the first year when the TPP agreements become effective. Then, within 10 years, it should be reduced to 0%[8].

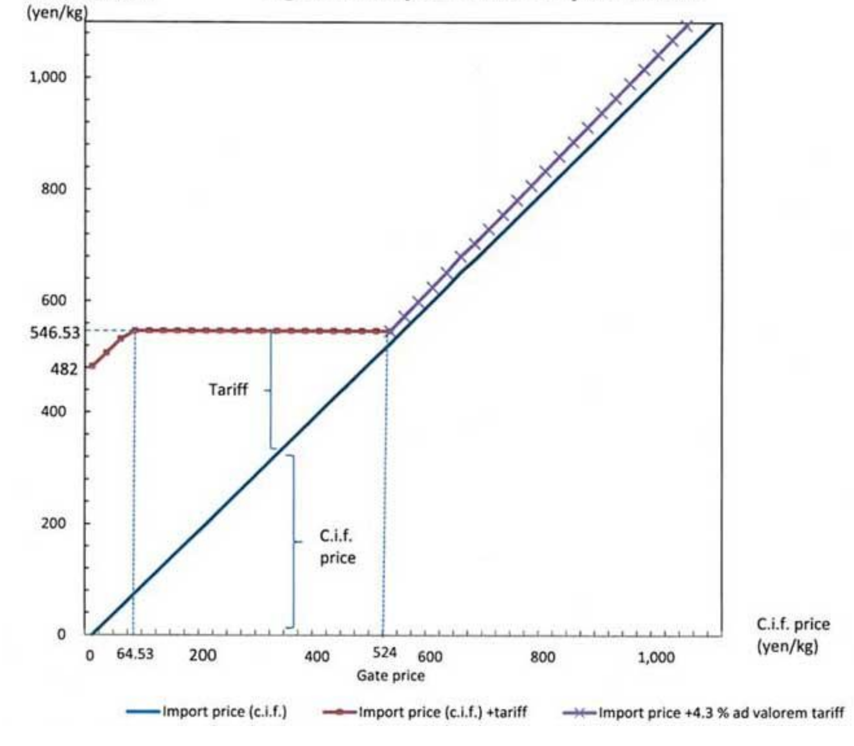
Considering only the agreement (2) may imply that the TPP agreement will provide a significant change in pork imports immediately after it becomes effective[9]. However, in practice, it is more important maintaining the gate price system. For example, if a pork importer continues to report the c.i.f. price at 524 yen/kg by combination imports, even in the tenth after the agreement becomes effective, the reduction of tariff rate is only 4.3 %.

At the same time, it should be noted that in order to make the average c.i.f. price close to the gate price, importers would have to import unwanted pork cuts also. For example, even if high price pork parts are in an oversupplied domestic pork market, trading companies may have to import not only low price parts but also high price parts in order to save tariffs. As long as the effect of tariff reduction is greater than the financial burden of importing unwanted parts, importers would continue undertaking combination imports. Currently, specific tariff is so high that pork importers continue combination imports. However, we have to consider the possibility that if the specific tariff is reduced to 50 yen/kg, those who want to import a certain type of low price foreign pork would prefer paying this specific tariff without combining with high priced pork parts. For most people in the pork industry, the specific tariff of 50 yen/kg is still high, making them continue to undertake combination imports. However, some of them may be interested in importing pork by paying this specific tariff. For example, domestic ham and sausage producers need only the low price parts of foreign pork for their ingredients. In fact, in the TPP agreement, Japan promised a drastic liberalization of ham and sausage imports. They stated that once the TPP agreement becomes effective, tariffs for foreign ham and sausages will be removed within 11 and five years, respectively. This implies that more fierce competition will be unavoidable for domestic ham and sausage manufacturers on an event of the TPP agreement comes into effect.

CONCLUSION

It should be noted that the impact of the TPP agreement will differ between domestic ham and sausage manufacturers, and pork farmers. This is because the former will encounter tough competition from imported ham and sausages if the agreement becomes effective. In contrast, since the basic framework of the current gate price system is maintained, the impact of the TPP agreement on pork farmers will be limited as long as combination imports continue. However, if customs employ strict surveillance over combination imports, low price foreign pork imports would be levied much more heavily regardless of whether the TPP agreement becomes effective or not. Accordingly, we should aim at focusing on customs' attitude toward combination imports.

Figure 1. Japan's current pork tariffs



Footnotes

1) When members were limited to only the original four countries, this partnership was called P4 instead of TPP.
2) In addition to the gate price system, Japan imposes additional border protection for pork in case of an upsurge in pork imports. This is called the safeguard system. Due to space constraints, this paper does not discuss this system.
3) The gate price system has been occasionally revised. Its brief history has been provided at Yoshihisa Godo, " The Gate Price System for Japan's Pork Imports", *FFTC Agricultural*

Policy Platform (Food & Fertilizer Technology Center for the Asian and Pacific Region) March 28, 2014 (downloadable at http://ap.fftc.agnet.org/ap_db.php?id=217).

4) 64.53 is obtained by subtracting 482 from 546.53.
5) Thus, the current gate price system can be considered a type of minimum import price system.
6) Among Japanese traders, pork is often marketed by carcass, rather than by primal cut meat. If pork is imported by carcass, the gate price and specific tariff are set as 393 yen/kg (instead of 524 yen/kg) and 361 yen/kg (instead of 482 yen/kg), respectively.
7) See Godo, "Gate Price."
8) This means that customs levy no tariff on pork whose c.i.f. price is higher than the gate price 10 years after the TPP agreement becomes effective. This situation can be considered a type of sliding tariff system.
9) Evaluation of the TPP agreement differs among Japanese mass media. Some people argue that the TPP agreement would provide significant damages on pork imports by a large-scale reduction in the specific tariff. For example, see "TPP and Okinawa (1): Pork," morning edition of *Okinawa Times*, October 9, 2015 (in Japanese). However, we consider that such arguments have stemmed from a misunderstanding of the gate price system.

Date submitted: Feb. 26, 2016
Reviewed, edited and uploaded: March 1, 2016