Contract Problems in U.S.-Japanese Joint Ventures

Dan Fenno Henderson
University of Washington School of Law

Follow this and additional works at: https://digitalcommons.law.uw.edu/wlr
Part of the Comparative and Foreign Law Commons

Recommended Citation
Available at: https://digitalcommons.law.uw.edu/wlr/vol39/iss3/6

This Article is brought to you for free and open access by the Law Reviews and Journals at UW Law Digital Commons. It has been accepted for inclusion in Washington Law Review by an authorized editor of UW Law Digital Commons. For more information, please contact cnyberg@uw.edu.
CONTRACT PROBLEMS IN U.S.-JAPANESE JOINT VENTURES

BY DAN FENNO HENDERSON*

U.S.-Japanese joint ventures are by far the most important form of direct foreign investment in Japan. For unlike most advanced governments elsewhere in the world, Japanese officialdom has, with precious few exceptions, denied validation under the Law Concerning Foreign Investment to all enterprises wholly-owned or even majority-owned by

* Professor of Law and Director, Asian Law Program, University of Washington.

The author wishes to acknowledge the assistance of Teisuke Akamatsu, Esquire, of the Tokyo Bar in the preparation of this article.

Although the term “U.S.-Japanese joint venture corporation” might be applied to corporate ventures in which all the shareholders are nationals of the place of incorporation but the activities are elsewhere (or where all or most of the activities of a Japanese corporation are in the United States, or vice versa), we use the term here, as it is used in Japanese parlance, to mean a Japanese corporation with operations in Japan and in which the major shareholders include both Japanese and U.S. firms. For further general discussions of definitions, see Comment, International Joint Venture Corporation: Drafting of Control Arrangements, 1963 DUKE L. J. 516; FRIEDMANN & KALMANOFF, JOINT INTERNATIONAL BUSINESS VENTURES (1961).


Note, however, that generally Japanese policy has discouraged all direct investment (whether joint venture or wholly owned) in favor of separating the induction of technology and capital, and excluding foreign management. Thus, Japanese policy has encouraged straight licensing to obtain foreign technology and loans or portfolio investment to obtain capital from abroad. See Introduction p. 405 supra.

See figures as of 1957 in FRIEDMANN & KALMANOFF, op. cit. supra note 1, at 18-19. About a fourth of the total investments in all areas involved less than 95 percent United States ownership; this figure may be taken as an indication of the extent of joint ventures in United States direct foreign investments. Most of this joint investment (20 percent, out of the total of 25 percent) was in the category of 50-95 percent United States ownership. Minority positions for the United States investors (in effect from 25 percent to 50 percent ownership) are represented only to a small extent. The category of “95 percent or more ownership,” which accounts for three-fourths of the total, may be taken to represent wholly United States-owned investments.

Note, however, the trends since 1957 would probably show a greater use by U.S. firms of joint ventures abroad.

* Out of a total of 183 international joint venture companies validated under the Law Concerning Foreign Investment (see note 5 infra) in Japan from 1950 to Oct. 1963, in only 25 did the foreign investor have a majority and most of these were prewar positions or, in any event, approved before the occupation ended, April 1952. There were also twenty-three fifty-fifty joint ventures. JUKAGAKU KOGYO TSUSHINSHA, GAIROGU GIYUTSU BONYU YORAN (Guide to induction of foreign technology) 49 (1964).

Gai-shi ni kansuru hōritsu (Law No. 163, 1950) [hereafter cited FIL], in 5 EHS No. 5410.

479
foreigners. Furthermore, it was basic Japanese policy not to validate even a minority equity in a Japanese enterprise unless the foreigner possessed essential technology which he would not make available to Japanese industry by straight patent or know-how licensing arrangements. Since before July 1963 validation only meant the right to repatriate capital and earnings in foreign currency, many foreign firms had chosen to forego validation and operate a wholly-owned or majority-owned Japanese corporation for yen only, but even this opportunity for an unapproved and underprivileged majority holding was foreclosed on July 1, 1963, when the Japanese Government declared that the so-called "yen operation" could no longer be established without official validation.

With only minority positions possible, it is not surprising that foreign investors have attempted to mitigate the weaknesses of their corporate position by special corporate control provisions inserted in preincorporation joint venture contracts with the Japanese partner. It is mainly this range of contract problems raised in the interstices of Japanese contract, corporate, and administrative law which will be explored below. The discussion will be limited to the problems as

6 All yen operations established before July 1, 1963, when further yen operations were forbidden, were ordered to report to the Minister of Finance by January 31, 1964, and as a result of these reports it was found that there were some 289 yen corporations and 273 foreign corporate branches in Japan, but only 120 of these yen corporations were manufacturing companies; another 109 were sales companies, mostly of minor scope. The total capital of all (289) was estimated at $140,000,000 book value. TRADE BULLETIN CORP. (TOKYO), THE APRIL 1964 SUPPLEMENT TO FOREIGN INVESTMENT, FOREIGN EXCHANGE CONTROL AND IMPORT CONTROL SYSTEM (BOOK II) 32-33 (Social and Economic Laws of Japan series, 1964).

7 The 1963 change took place as an amendment to the Cabinet Order Concerning Exceptions, etc., to Standards of Validation Based on the Law Concerning Foreign Investment (Gaishi ni kansuru kōitsu no kitei ni motozuku ninka no kijun no tokurei-tō ni kansuru seirei) (Cabinet Order No. 221, July 1, 1952) in 5 EHS No. 5470. The amending order was Cabinet Order No. 228, June 29, 1963, effective July 1, 1963.

8 But note that history was made on August 11, 1964, when the Japanese Government validated the first 100% (¥200,000,000) equity in a Japanese corporation since 1950. Asahi Shimbun (Asahi Newspaper), Aug. 12, 1964, p. 2.

The foreign investor was British United Shoe Machinery. But the import of its product was already freely allowed. So the validation is doubtless a special case.

9 Practically nothing has been written on U.S.-Japanese joint venture contracts either in Japanese or English. On the how-to-do-it level see GAIROKU KAWASE BÔEKI KENKYÛKAI, GAIROKUJIN NO NIHON NI Okeru gôbengaihô sesshûtsu keiyaku ni tsuite (Concerning contracts establishing foreigners' joint venture corporations in Japan) (1963). See also JÔKAGAKU KÔGÔ TÔSHINSHA, op. cit. supra note 4, at 367, for a complete list of foreign stock equities in joint venture corporations validated under the FIL.

10 For general aspects see Bradshaw, Joint Ventures in Japan, 38 Wash. L. Rev. 58 (1963); for general contract drafting problems see Comment, supra note 1; for the leading work on U.S. joint ventures generally in various countries see FRIEDMANN & KALMANOFF, JOINT INTERNATIONAL BUSINESS VENTURES (1961); also see BOULTON, BUSINESS CONSORTIA 52-62 (1961), for a detailed discussion on "documenting the
they appear to the drafting lawyer in the initial contracting phase, although, of course, in drafting the lawyers look prospectively to performance and enforceability for reference, meaning, deterrence, and, only in the most marginal situations, to litigation. Emphatically, the implication must be avoided that litigated results can be a major guide in this peculiarly complex and creative type of private law making. Rather, the legal doctrine and enforcement apparatus of the law function more as aids to understanding and clarity of communication, as voluntary guides to performance, or possibly as moral deterrents to breach. The efficacy of law in the international private contracting process is, of course, premised on good faith and mutual purpose—things which cannot be legally compelled. Thus, litigation means little more than salvage, not specific performance or even adequate compensation even though the Japanese legal system has tolerable doctrines in this area. U.S. domestic experience with its affirmative enforcement of partnership or close corporate relations generally bears this proposition out, but there are other factors peculiar to U.S.-Japanese transactions which amplify this basic premise. Foremost among these peculiarities is the Japanese businessman’s attitude toward contracts. In his domestic business affairs he uses detailed formal contracts relatively little and litigation even less, depending more on traditional organizational patterns, social hierarchy, and authority, which always have been the dominant features of perhaps the world’s most socially (not legally) organized society. The contracts employed in intercorporate business arrangements tend to be brief memorandums establishing flexible, adjustable relationships

---

13 The Japanese practice of using extralegal dispute settlement techniques is noted in Nippon Hodō Co. v. United States, 285 F.2d 766, 768 (Ct. Cl. 1961).  
14
which are governed by discussions and amicable compromises in case of disputes. More will be said on this flexible approach to contracting later.\textsuperscript{15}

A second point which de-emphasizes legalities of the U.S.-Japanese joint venture is the inefficacy of transnational litigation generally. This is not just the usual problem of judicial administration—expense, time, and inept procedures and remedies; transnational lawsuits generally reach an exquisite degree of disutility by the combination of ambiguous conflicts rules, unenforceable prorogation and choice-of-law clauses\textsuperscript{16} (meaning multiple law potentially applicable), translation and foreign law proof problems, and a paucity of legal experts.\textsuperscript{17} Saving for another time the difficulties of assuring that any single law will actually turn out to govern bilateral litigation, it will be assumed for the purpose of discussion that Japanese law governs because normally it is stipulated (and the parties think it governs, which for reasons mentioned above is important), because the operation is in Japan, and because usually neither the joint venture corporation nor the Japanese partner are suable elsewhere.\textsuperscript{18}

**THE SCHEME OF JAPANESE LAW APPLICABLE TO JOINT VENTURE CONTRACTS**

The first elemental question for the foreign lawyer is: where in the Japanese codes is the law of contracts\textsuperscript{19} relevant to joint ventures to be

\textsuperscript{15} See text, *Frustration and Modification*, at notes 125-36 infra.


\textsuperscript{18} But, of course, one or the other can always bring suit elsewhere and at least test the jurisdictional points, and therein lies the basic ambiguity. On matters of jurisdiction and "competence," see *Ehrenzweig, Ikehara & Jensen, American-Japanese Private International Law* 26 (1964).

\textsuperscript{19} Several secondary Japanese language works on contracts have appeared in recent years—texts, commentaries, collections of essays and forms. See e.g., 1 *Wagatsuma, Mimpō kōgi* (Lectures on the Civil Code) 196 (1963) on general provisions, including juristic acts, and volumes 4, 5 (1), (2), and (3) (1962) on obligations; *Keiyakukō taikei* (Compendium [essays] on Contract Law) (1963), a six-volume memorial collection of essays by many scholars on various contract law topics, dedicated to Professors Matsuura, Nishimura, Funabashi, Yagi, and Ishimoto; *Hironaka, Keiyakukō kenkyū* (Studies on contract law) (1958); *Wagatsuma & Ariizumi, 3 Kommentar, Sōkenhō* (Commentaries, obligation law) (1951), an article-by-article commentary on the code sections with case citations; 1 *Hanrei kommentar* (Case commentary) (Wagatsuma ed. 1963) is on the General Provisions (sōsōkū) of the Civil Code [the volumes on obligations are not out yet]; *Ono & Imanishi, Keiyaku zensho* (Complete collection on contracts) (1962), a collection of contract forms plus a commentary.
found? Because this law is interwoven into both the Civil Code and the Commercial Code along with several special laws, it is useful to approach the law in the German fashion as the Japanese lawyer would. He sees the codes as deductively systematic: the Civil Code is the source of general principle, perhaps analogous in this sense to the historical position of the common law in our system. On contracts, Civil Code Book I (articles 3-20, 90-137) covers Juristic Acts (hōritsu kōi) and Capacity (nōryoku) which, so far as it applies to contracts, corresponds roughly to our various problems of mutual assent, especially when considered with Book III (articles 399-696) on Obligations (saiken), particularly articles 399-548 on the formation and effect of contracts generally, and articles 549-696 covering thirteen specific types of contracts. Then a special and separate Commercial Code (Book III) elaborates the law governing any Commercial Transaction (shōkōi) including all transactions of Business Enterprises (kigyō) which are the main objects to which the Commercial Code is applicable. To determine the applicability of the Commercial Code, the first question is whether the joint venture contract is such a commercial transaction between such enterprises. It clearly is, because any Japanese corporation is a Trader (shōnin), and all transactions of a trader which are related to his business are commercial transactions under the Commercial Code, whether the other party is a trader or not.

The formation of a contract is generally determined by the Civil Code.

---

20 See generally, NISHIHARA, SHÔKÔIN (Law of commercial transactions) 1-2 (29 HÔRITSUGAKU ZENSHU ed. 1960) for the dominant theory that the objects of the Commercial Code are kigyō.

21 The definitions of various kinds of commercial transactions are found in Commercial Code arts. 501, 502, and 503. For the definition of a trader as mentioned in art. 503(1), see Commercial Code arts. 4, 52, and 523 and Limited Company Law (Yûgengaiisha) arts. 1 and 2 (Law No. 74, 1938).

22 As a consequence of several provisions (Commercial Code arts. 3, 4, 52, 501, 502, 503, 523 and Limited Company Law arts. 1 and 2), the Commercial Code applies to any business-related transaction of a company, whether stock-type or not, so long as it is incorporated in accordance with the provisions of the Commercial Code (Book II) or the Limited Company Law. The Commercial Code will always apply to any transactions effected in Japan by a foreign company with a Japanese company, whether it is recognized by Japanese law as a trader or not. This is because if the Japanese company is a trader and if the transaction is related to his business, as is generally the case (i.e., whenever it is in pursuit of benefit in the broadest sense), the Commercial Code always applies to the other party. Commercial Code arts. 3(1) and 503.
Code provisions\textsuperscript{23} and the basic requirement to form a contract is mutual assent (\textit{i.e.}, offer and acceptance). Such questions as capacity, fraud, mistake, duress, or illegality are considered to bear only upon the effect of the contract after mutual assent.\textsuperscript{24} There are no general requirements of consideration\textsuperscript{25} or writing.\textsuperscript{26} Since U.S.-Japanese joint venture contracts are always written embodiments of mutual bilateral promises duly signed, generally there would be no formation problems even under our law.\textsuperscript{27}

The general approach of the rest of the Civil Code (\textit{i.e.}, Book III) is to elaborate general rules for obligations and particularly rules for thirteen kinds of Typical Contracts (\textit{tenkei keiyaku}),\textsuperscript{28} none of which includes a joint venture contract as such, but the typical Partnership Contract (\textit{kumiai keiyaku}) would undoubtedly apply to these joint ventures before incorporation and also, when appropriate, after incorporation, as shall be seen later. Of course, the general provisions in Civil Code Book I and other general provisions, such as those on obligations and contracts, Book III articles 399-548, are applicable to all contracts\textsuperscript{29} including joint ventures. In a proper case some of the

\textsuperscript{23} \textit{Civil Code} arts. 521-528. Also, on offer and acceptance see \textit{Commercial Code} arts. 507, 508, and 509.

\textsuperscript{24} These questions are generally covered by Book I (General Provisions) of the \textit{Civil Code}. The relevant provisions are arts. 3-20 on Capacity and 90-137 on Juristic Act (\textit{hōritsu kō}). See \textit{Commercial Code} art. 504 on representation ("agency"). 5(1) \textit{Wagatsuma, Mīmō kōgi} (Lectures on the Civil Codes) 79 (1962); \textit{Suekawa, Keiyakubō} (Contract law) 20 (1958).

\textsuperscript{25} Of course, there is no direct Japanese case authority for the proposition that consideration is not required. But see \textit{Izawa, Beikoku shōgyō shōkenhō} (U.S. law on commercial papers) 244 (1955) and the discussion at note 41 infra.

\textsuperscript{26} There are exceptional contracts regulated by special statutes which specifically require that the contract be in writing. \textit{E.g.}, tenancy contracts, Farm Land Law (\textit{Nōchikō}) art. 25 (Law No. 229, 1952); contracts for construction work, Construction Industry Law (\textit{Kensetsugyōhō}) art. 19 (Law No. 100, 1949). Compare, share subscriptions (\textit{Commercial Code} art. 175); bond subscriptions (\textit{Commercial Code} art. 301(1)); and prorogation clauses in domestic suits (\textit{Code of Civil Procedure} art. 25), all of which require written documents related to contracts for regulatory law purposes, but in Japanese legal conception failure to comply with these requirements of writing only has regulatory significance and does not invalidate the respective oral contracts or defeat an action on them for damages.

\textsuperscript{27} Note that we have a rule derived from agency in some states, however, that mutual bilateral promises alone will not support an irrevocable proxy. \textit{E.g.}, \textit{Johnson v. Spartanburg County Fair Ass'n}, 210 S.C. 55, 41 S.E.2d 599 (1947). But see notes 96-98 infra.

\textsuperscript{28} The types are: gift (arts. 549-54); sale (arts. 555-85); exchange (art. 586); loan for consumption (arts. 587-92); loan for use (arts. 593-600); lease (arts. 601-22); employment (or service) (arts. 623-31); contract for work (arts. 632-42); mandate (arts. 643-56); bailment (arts. 657-60); partnership (arts. 667-88); life annuity (arts. 689-94); and compromise (arts. 695-96). Also see discussion at note 31 infra.

\textsuperscript{29} For the Japanese theory of Mixed Contracts (\textit{kongō keiyaku}) and Atypical Contracts (\textit{hetenkei keiyaku}), see 5(3) \textit{Wagatsuma, Mīmō kōgi} (Lectures on the Civil Code) 883 (1962); and for judicial handling of atypical contracts see \textit{Arimatsu v. Furukawa}, 22 Daishin-in minji hanketsuroku [hereafter cited Minroku] 1450 (Great
specific provisions on other typical contracts may be applied by Analogous Application (ruišū tekiyō) or Mutatis Mutandis (junyō), which are techniques found in Japanese theories of statutory construction.\(^{30}\) Also, there are a number of special laws, supplementary to the Codes, affecting certain contracts\(^{31}\) or certain aspects of contracts generally.

The exact legal equivalent of our joint venture concept does not seem to exist in Japanese contract law.\(^{32}\) But, much as in our system,\(^{33}\) the joint venture contract would be treated as a Japanese-type partnership subject to the rules of a typical partnership contract\(^{34}\) since it contemplates all the elements of a Japanese partnership: (1) an agreement; (2) Group Organization (dantai); and (3) joint assets.\(^{35}\) The important thing to be remembered, however, is that in Japanese legal concepts the “joint venturers” stand in several relationships to each other when moving from the simple contract to promotion of the new

---

30 Early Japanese courts confused the use of junyō and ruišū tekiyō. Morikawa v. Mori, 22 Minrou 1663 (Great Ct. of Cassation, Aug. 22, 1916), where mutatis mutandis (junyō) is used like the word analogous (ruisin tekiyō). However, recently scholars and courts have generally agreed that junyō is a statutory technique and must be provided in the law, whereas ruišū tekiyō is a method of legal reasoning employed in decisions by the courts on their own. Nagamoto and Takeshita v. Fukuhisa, 8 Saikō saibansho minji hanreishii [hereafter cited Minshi!] 1505 (Sup. Ct., Aug. 20, 1954).

31 Among the special statutes recognizing atypical contracts are Law Concerning Fidelity Guaranty (Mimoto hosho ni kansurut haritsu) (Law No. 42, 1933) in 2 EHS No. 2124; Land Lease Law (Shakuchihō) (Law No. 49, 1921) in 2 EHS No. 2130; House Lease Law (Shakuyahō) (Law No. 50, 1921) in 2 EHS No. 2131; and Labor Standards Law (Rōdō kijunho) arts. 13-28 (Law No. 49, 1947) in 8 EHS No. 8040 (as to labor contracts).

32 The Commercial Code also provides a number of types of contracts of a commercial nature such as contracts of account current (arts. 529-34), contracts of undisclosed association (arts. 535-42), etc. The Code applies to all contracts of a commercial nature, whether typical or atypical.

33 On this point in the United States, see HENN, CORPORATIONS 64 (1961):

"Generally, joint ventures are governed by some of the principles of partnership law, with some differences resulting from the more limited extent of the business undertaken by the joint venture. The authority of the adventurer to bind the others is more limited, and there is sometimes said to be no general agency."
corporation and finally to an operative corporation in which they are shareholders and officers. First, the U.S. and Japanese firms are legally Japanese partners by virtue of the joint venture contract. When they set about organizing the corporation, they must assemble seven promoters and Japanese jurisprudence subjects these promoters to the typical partnership contract rules with regard to their activities in establishing a new corporation. Thus, at this stage, if both joint venturers become promoters formally, they are legally members of two separate partnership arrangements, one under the joint venture contract and one as promoters, and in addition they can represent the Embryo Company (seiritsuuchū no kaisha) and can commit it to certain obligations so long as these commitments are limited to matters of incorporation, rather than commencement of business. Also, under the corporation law, all seven of the promoters will have fixed and distinct duties, powers, and liabilities to the corporation and third parties. After the new corporation is formed, the partnership relationship under the original joint venture contract may subsist, if such is intended, in parallel with the corporate relationships among the same joint venturers as shareholders. Joint venture or preincorporation agreements coexist in a similar way in close corporations in some U.S.

36 COMMERCIAL CODE art. 165: "Seven or more promoters are required for the incorporation of a kabushiki kaisha."

Seven promoters are required only during incorporation. One shareholder only is legal after registration; for example, where the other promoters transfer their shares to one person, the prohibition against one shareholder does not apply to a kabushiki kaisha. COMMERCIAL CODE arts. 404 and 94.

37 Nakajima v. Kondō, 24 Minroku 1480, 1483 (Great Ct. of Cassation, July 10, 1918); Hyaku-sanjūhachi Bank v. Toyo Seien Co., 16 Minroku 982 (Great Ct. of Cassation, Dec. 23, 1910); and cases cited in 13 (IV) HANREI TAIKEI (Compendium of decisions) 206-09. See Kitazawa, Setsuritsuuchū no kaisha (Company under establishment process), in 1 KABUSHIKI KAIHSHA KÔZA (Lectures on corporation law) 211, 218 (1958); and 1 ISHI, SHÔHÔ (Commercial law) 163 (rev. ed. 1959).

38 Specifically note that transactions by promoters before the corporation comes into existence which go beyond the scope of incorporation and have to do with the commencement of the future companies' business are not binding on the corporation when it comes into existence and the promoter may be held personally liable under CIVIL CODE art. 675. Shinsei Kōgyō K.K. v. Shimazaki, 7 Kakyū minshū 890 (Tokyo Dist. Ct., April 9, 1956) (new corporation not entitled to enforce a lease signed by person before he became one of plaintiff's promoters; moreover, here the lease was connected with future business, not incorporation). Tsuji v. Daiei Baseball K.K., 12 Minshū 3228 (Sup. Ct., Oct. 24, 1958) (promoter liable personally to baseball team because his arrangement for a game to celebrate the new company's inauguration was not within the scope of promoters' duties re incorporation).

39 COMMERCIAL CODE arts. 186, 192-95 for liability of promoters. Note that in Japanese law, unless he actually shows that he is signing for someone else, the person whose signature appears on the articles of incorporation is the promoter, regardless of how formalistic his participation may be intended to be by all concerned; Kakuda v. Matsuura Suian K.K., 22 Minroku 1862 (Great Ct. of Cassation, Oct. 7, 1916). For many other cases and a discussion of promoters' liability see Takeuchi, Hokkinin no sekinin (Liability of promoters), in 2 Sōgō HANREI KENKYÛ SÔSHO SHÔHÔ 147, 152 (1961).
However, the parallel spheres of contract and corporate law are much more distinct in Japanese law than in most American law as will be demonstrated. In summary then, the applicable law for the interrelations of joint venturers and promoters is the partnership contract law. The promoters, later the corporate shareholders, are, in addition and at the same time, subject to the corporate law in relation to the corporation and certain third parties.\textsuperscript{41}

**Problems of Form**

As mentioned, Japanese contracts, with few exceptions, need not be in writing; nor must there be consideration.\textsuperscript{42} Since in fact joint venture contracts are invariably in writing with mutual bilateral promises, these points would hardly be problems anyway.

Who is the proper officer to sign a contract for a Japanese corporation? While it is easy, given the time and requisite know-how, to determine from the public Corporate Registry (shōgyō tōkibo) who is the person registered as the Representative Director (daihyō torishīmariyaku) or manager of any Japanese corporation at a given office,\textsuperscript{43} still it frequently happens that hastily concluded contracts are signed by other officers or agents of a Japanese company. This does not necessarily mean that the corporation is not bound because others may have authority by power-of-attorney from the representative director


Another problem is presented as to whether a corporation can be a joint venturer in some U.S. jurisdictions where partnership law is largely applicable to joint ventures and corporations are not allowed to enter a partnership. Usually, however, even in such jurisdictions a corporation is permitted specifically to be a joint venturer. Weisman v. Awnair Corp. of America, *supra*; U.S. Fid. and Guar. Co. v. Dawson Produce Co., 200 Okla. 540, 197 P.2d 978 (1948); Nolan v. J. & M. Doyle Co., 338 Pa. 398, 13 A.2d 59 (1940); Excelsior Motor Mfg. & Supply Co. v. Sound Equipment, Inc., 73 F.2d 725 (7th Cir. 1934), cert. denied 294 U.S. 706 (1935). See ABA-ALI Model Bus. Corp. Act § 4(g) (1953).

\textsuperscript{41} See for details, Kitazawa, *supra* note 37, at 211, 218, 219.

\textsuperscript{42} Ogoshi v. Tokyo Tatemono, 22 Minshū 1845 (Great Ct. of Cassation, Oct. 4, 1916), where, of course, the court did not mention a lack of consideration, there being no such requirement in Japanese law, but the court did enforce a promise to pay more than the original contract called for without any further consideration from the other party. See for comparison, von Mehren, *Civil Law Analogues to Consideration: An Exercise in Comparative Analysis,* 72 Harv. L. Rev. 1009 (1959).

\textsuperscript{43} Commercial Code art. 188(2)viii requires that the name of the daihyō torishīmariyaku be registered at the appropriate public registry and art. 40 provides for registration of shihainin (managers).
or even by "Apparent Authority (hyōken daihyō)." To avoid difficulty, it is preferable to make sure that the representative director signs a document as important as a joint venture agreement. Also, in some cases, the usual license agreements, sales contracts, and other arrangements for the new corporation should be signed by the majority joint venturer as representative of the promoters in order to bind the new corporation and the majority joint venturer.

Most Japanese individuals have registered seals which they affix to documents instead of signing them by hand, although the custom of using the handwritten signature by Japanese is becoming common in international transactions. The very cautious person might find it advisable to check both the registry certificate of the corporation to ascertain the corporate existence and the registered representative's correct name, and the Seal Certificate (inkan shōmei) of the representative at the commercial registry if he uses his seal. Thus, the impression can then be compared with that used on the contract.

Another formal matter of importance should be mentioned—the normal practice of providing in the contract that conflicts in interpretation arising out of differences in the Japanese and English language versions will be resolved by reference to the English. One of the major language problems of these contracts relates to corporate control devices in the pro forma articles of incorporation which are annexed to the contract. These are required by law to be in Japanese. Quaere

44 Commercial Code arts. 42, 262; also see Civil Code arts. 109, 110, 112.
45 Law Concerning Matters To Be Signed Under the Commercial Code (Shōka-chū shōmei subeki baai ni kansuru horitsu) art. 1 (Law No. 17, 1900) provides for execution of commercial documents by seal.
46 Commercial Registration Law (Shōgyō tōkihō) art. 12 (Law No. 125, 1963); Commercial Registration Regulations (Shōgyō tōki kisoku) art. 16 (Ministry of Judicial Affairs Regulation No. 112, 1951). The Commercial Registration Law was enacted in 1963 and the provisions of the Law of Procedure in Non-Contentious Matters (Hishō jiken tetsuzukiho) arts. 142-205 (Law No. 14, 1898), in 2 EHS No. 2380, which previously regulated this subject, were deleted. The representative's seal is registered at the Commercial Registry, and this particular seal for corporate purposes is usually different from the seal which the same individual files with the municipal offices [in Tokyo the Ward Office (kuyakasho)] for his personal use.
47 E.g., see Commercial Registration Regulations (Shōgyō tōki kisoku) art. 38 (Ministry of Judicial Affairs Regulation No. 112, 1951), which presupposes the description to be in Japanese. According to the Notary Law, if the articles of incorporation are made as a Notarial Deed (kōsei shōsho) and the Notary (kōshōnin) can attest any private deed written in a foreign language except that the statement of attestation must be in Japanese. (Notary Law art. 27.) See Miyaji, Sasho ni kansuru tetsuzuki (Procedure for acknowledgments), 10 Jiyū to seigi (Freedom and justice) (No. 9) 30 (1959).

Of course, the language of the Japanese courts is Japanese. Court Organization Law (Saibansho) art. 74 (Law No. 59, 1947) in 2 EHS No. 2010. However, there is no such clear-cut provision for Non-Contentious Matters (hishō jiken) such as com-
whether in a dispute on the contract in such a situation the Japanese language would not in fact govern at least as to the rights of the joint venture corporation and third parties?

SHARE RESTRICTIONS AND CORPORATE CONTROL DEVICES

Introduction: The problem here involves the interplay between the corporation law and the preincorporation contract which the parties intend shall control their future action (as shareholders, directors, or officers) and through them, certain actions of the future joint corporation. Under the circumstances assumed, this immense field is essentially a Japanese corporation and contract law problem, but any lawyer with situational sense will be equally concerned with evidence, burdens of proof, procedural efficacy, and remedies. In this situation inquiry will be made as to whether in Japanese law pertinent kinds of preincorporation obligations can subsist and be enforced after incorporation and, if so, what the efficacy of enforcement actions might be. The latter inquiry extends to the effect on (1) the contracting joint venturers as shareholders, (2) the joint corporation, and (3) third parties where relevant. The availability of these remedies are particularly important in case of violations of the agreements in three critical areas: (a) restrictions on share transfers; (b) corporate control mechanisms, variant from the normal meeting and voting procedures of the corporation law; and (c) transactions contemplated in the contract to be accepted and carried out by the future joint corporation such as trademark, patent and know-how licenses, sales agencies, supply contracts, capital equipment imports, employment contracts for key engineers, and a host of other items which may be critical in the over-all bargain to one or the other of the parties.

It is a major problem of draftsmanship, after the creative planning, negotiating, and adjusting have produced a bargain, to sort out the parts of the over-all complex and to document them in optimum form—a master contract, pro forma articles of incorporation, and various side agreements or annexes. One problem is that official practice requires1 commercial registrations which are not within the jurisdiction of the court, but under the Ministry of Justice. The Law of Procedure in Non-Contentious Matters (Hishō jiken tetsuzukihō) art. 139 (Law No. 14, 1898) in 2 EHS No. 2380. Nevertheless, in Japanese practice the registry will not accept foreign language documents for commercial registration, such as articles of incorporation. So even though the articles had been attested by a notary as a private deed they would not be accepted in a foreign language by the registry office. Note that there is a similar rule against a trade name in English, which also states that an English trade name cannot be accepted for registration. 1 Suzuki, Kabushiki jitsumu (Practices relating to shares) 10 (1963).

48 Jūkagaku kōgyō tsūshinsha, op. cit. supra note 4, at 60.
that the joint venture contract must annex draft articles of incorporation, and legally the parties may find it advisable to include some of the above-mentioned policies in the articles. Others may simply subsist in the master contract or in side agreements depending on whether they need approval and how long they are intended to be effective. It shall be seen that it can make a difference under Japanese law, as it does in some American jurisdictions, whether the restrictions are in a side agreement or the articles. Japanese corporation practice does not have any exact counterpart to our by-laws, but something similar is often instituted by the directors or shareholders to govern details of directors’ meetings, share transfer procedure, and the like.\(^4\) As distinguished from American\(^5\) practice, however, such “by-laws” do not seem to have been used for the re-distribution of corporate control powers in close corporations.\(^6\) Obviously, the joint venture corporation under discussion resembles the close corporation,\(^7\) which in our domestic parlance has been largely an operational rather than technical term because they have traditionally received little special legislative support in the states until very recently. However, Japanese corporation law, since 1938, has provided for a juristic person called a Limited Company (yūgengaisha),\(^8\) which was legislatively intended as a vehicle for this kind of close-corporate enterprise. Like the English private company\(^9\) and the German Company with Limited Liability (Gesellschaft mit beschränkter Haftung),\(^10\) the yūgengaisha law limits the number of Members (shain) and permits informal meetings; restriction on membership transfers; and simpler incorporation procedures, corporate structures,

\(^{49}\) See 1 Tanaka, Saihin Kaisamō gairon (jō) (General theory of company law) 128-29 (1963), which notes that certain provisions of the Commercial Code seem to presuppose by-laws. E.g., see art. 282(2).

Any shareholder or creditor of the company may, at any time during business hours, demand inspection of the documents mentioned in the preceding paragraph and may demand delivery of a copy or an abstract copy of such documents, paying such fees as fixed by the company.

\(^{50}\) Even in some U.S. jurisdictions extraordinary controls over director or shareholder action can only be provided in the articles. Others allow restrictions in the by-laws. See 1 O'Neal, op. cit. supra note 10, at 200-02 (1957).

\(^{51}\) Quaere whether unregistered “by-laws” providing for abbreviated procedures, etc., would be valid under the corporation law?

\(^{52}\) Definitions of the close corporation vary, but generally the term means a corporation with only a few shareholders wherein ownership and management are coalesced and the shares are not traded on the securities markets. 1 O'Neal, op. cit. supra note 10, at 2-5 discusses various criteria suggested by the writers and courts.

\(^{53}\) Limited Company Law (Yūgengaishahō) (Law No. 74, 1938).


\(^{55}\) Schneider, The American Close Corporation and Its German Equivalent, 14 BUS. LAW. 228 (1958).
records and notices; but it still provides the desired juristic separateness and limited liability.\textsuperscript{66} Thousands of small, closely-held enterprises avail themselves of this juristic form in Japan, but the words \textit{yūgen-gaisha} must appear in the company’s name.\textsuperscript{67} Thus, unfortunately, in Japanese business and financial circles it has a diminutive connotation,\textsuperscript{68} and therefore U.S.-Japanese joint ventures have seldom, if ever, availed themselves of it. Instead the U.S.-Japanese joint venturers have generally chosen the Stock Corporation (\textit{kabushiki kaisha}), designed for wide public shareholding, and thus they have invited upon themselves many of the same problems of our clumsy, close corporation. Yet, the availability of the \textit{yūgen-gaisha} means that legal guidelines for close \textit{kabushiki kaisha} have been relatively unnecessary, and, therefore, undeveloped in Japan for fitting the requirements of a close corporation into the formalistic framework and procedure of the stock corporation. In contrast, our U.S. law (despite a multitude of close corporations) has never provided an adequate separate juristic entity designed for them.\textsuperscript{69} Only recently are these special problems beginning to get partial recognition in our statutes and judicial precedents, and even these changes are taking place largely within the ponderous corporation law framework designed for publicly held corporations.\textsuperscript{70} Ironically,

---

\textsuperscript{66} See generally, Tanaka, Yoshimaga & Yamamura, \textit{Zen'ei Kommentaru Kaisha} (Completely revised commentary on company law) 1405-1527 (1964); Ishii, \textit{op. cit. supra} note 37, at 556; Nomura, \textit{Yūgen-gaisha Setsuritsu Annaigai} (Guide to establishment of a limited company) (1964).

\textsuperscript{67} Limited Company Law (\textit{Yūgen-bushichô}) art. 3(1) (Law No. 74, 1938).

\textsuperscript{68} See Ōsumi, Nishihara & Ueda, \textit{Kabushiki kaisha no komponteki kaisei ni tsuite no kenkyû} (Study on basic revision of the stock corporation law), \textit{Shibyō Honmu Kenkyû} (No. 30) 1, 5 (1956). The Members (\textit{shain}) are limited to 50, but the size of capital and operations are, of course, not limited. They could conceivably attain great size, for example, like the Ford Motor Company in this country, before it went public.


b) Except in cases where the shares of the corporation are at the time or subsequently become generally traded in the markets maintained by securities dealers or brokers, no written agreement to which all of the shareholders have actually assented, whether embodied in the charter or bylaws or in any side agreement in writing and signed by all the parties thereto, and which relates to any phase of the affairs of the corporation, whether to the management of its business or division of its profits or otherwise, shall be invalid as between the parties thereto, on the ground that it is an attempt by the parties thereto to treat the corporation as if it were a partnership or to arrange their relationships in a manner that would be appropriate only between partners. . . . A transferee of shares covered by such agreement who acquires them with knowledge thereof is bound by its provisions.

---

\textsuperscript{66} See generally, Tanaka, Yoshimaga & Yamamura, \textit{Zen'ei Kommentaru Kaisha} (Completely revised commentary on company law) 1405-1527 (1964);

\textsuperscript{67} Limited Company Law (\textit{Yūgen-bushichô}) art. 3(1) (Law No. 74, 1938).

\textsuperscript{68} See Ōsumi, Nishihara & Ueda, \textit{Kabushiki kaisha no komponteki kaisei ni tsuite no kenkyû} (Study on basic revision of the stock corporation law), \textit{Shibyō Honmu Kenkyû} (No. 30) 1, 5 (1956). The Members (\textit{shain}) are limited to 50, but the size of capital and operations are, of course, not limited. They could conceivably attain great size, for example, like the Ford Motor Company in this country, before it went public.


b) Except in cases where the shares of the corporation are at the time or subsequently become generally traded in the markets maintained by securities dealers or brokers, no written agreement to which all of the shareholders have actually assented, whether embodied in the charter or bylaws or in any side agreement in writing and signed by all the parties thereto, and which relates to any phase of the affairs of the corporation, whether to the management of its business or division of its profits or otherwise, shall be invalid as between the parties thereto, on the ground that it is an attempt by the parties thereto to treat the corporation as if it were a partnership or to arrange their relationships in a manner that would be appropriate only between partners. . . . A transferee of shares covered by such agreement who acquires them with knowledge thereof is bound by its provisions.

c) An agreement between all or less than all of the shareholders, whether solely between themselves or between one or more of them and a party who is not a
then, our long and awkward experience with the close corporation has produced precedents, literature, and even a treatise\textsuperscript{61} useful as comparative guides for coping with partnership-type enterprises which choose to avoid, for reasons of prestige, the legally most appropriate vehicle in Japan, and instead set up a \textit{kabushiki kaisha}.

\textit{Restrictions on the Transfer of Shares:} Having usually invested considerable time and effort in carefully selecting each other for the enterprise at hand, U.S.-Japanese joint venturers understandably want to restrict the sale of shares to insure that the joint Japanese corporation will continue to be jointly owned by them alone. To this end, they usually agree on some restriction such as first-refusal rights for the other party in case one shareholder wants to sell. The first question raised by such a clause is the scope of the \textit{Commercial Code} provision\textsuperscript{62} which expressly forbids the prohibition or restriction of the transfer of shares of \textit{kabushiki kaisha}.

Contractual limitations, apparently violative of the \textit{Commercial Code} prohibitions against share transfer restrictions [article 204(1)], are considered valid and enforceable by most legal scholars in Japan. The key to understanding the limited legal effect given to article 204(1) by the Japanese scholars is in the systematic code structure of Japanese law, which separates contract and corporate law principles and gives them parallel validity in their own spheres. Thus, article 204(1) is thought to prevent only share transfer restrictions in the intra-corporate structure, articles of incorporation, rules (by-laws), and resolutions. So on this theoretical level restrictive contracts (1) between the shareholder, is not invalid, as between the parties thereto, on the ground that it so relates to the conduct of the affairs of the corporation as to interfere with the discretion of the board of directors, but the making of such an agreement shall impose upon the shareholders who are parties thereto the liability for managerial acts that is imposed by this chapter upon directors.

Also, the Florida Bar Association is drafting a new close corporation law.\textsuperscript{61} Both the cases and the periodical literature are exhaustively cited throughout both volumes of O'\textit{Neal}, \textit{Close Corporations} (1958) (Supp. 1963).\textsuperscript{62} \textit{Commercial Code} art. 204(1): “The transfer of a share shall not be prohibited or restricted even by the provisions of the articles of incorporation.” Article 204(1) was added by an occupation-sponsored amendment (Law No. 167, 1950), which also changed other features of Japanese corporation law relating to shares and shareholders. See Sono, \textit{Shōhō kaisei no rippōron-teki tenkai} (On the movement for revision of the Japanese Commercial Code), in \textit{Shōhō kaisei no dōkō to kihon mondai} (Trend for Commercial Code revision and its basic problems) 1, 18-20, 141 (1961). In English, see Salwin, \textit{The New Commercial Code of Japan: Symbol of Gradual Progress Toward Democratic Goals}, 50 \textit{Geo. L.J.} 478 (1962).

There are two other types of juristic entities (besides \textit{yūgenkaisha}, text accompanying note 53 supra), provided in the \textit{Commercial Code}, Book II. They are \textit{gōmei kaisha} (arts. 62-145) and \textit{gōshi kaisha} (arts. 146-64), both of which resemble in some respects our partnership. Being of unlimited liability, they are normally inappropriate for an international joint venture.
corporation and a shareholder or (2) between shareholders are legally outside the operative sphere of corporation law, and despite article 204(1) they will be enforced by the usual remedies for breach of contract. Only one relevant case since 1950 has been found, and the treatise authority is divided on the enforceability of the corporation-shareholder agreements. On upholding shareholder-shareholder contracts which restrict transfers, however, the authorities are almost unanimous. Judge Matsuda is a notable exception.

Thus, given the general validity of shareholder agreements restricting transfers, the remaining question is: How useful are the legal remedies of the non-transferring shareholder against the transferee, or the corporation? Can he get damages, injunctive relief, or recover from the transferee and correct the registration of the shares on the corporation shareholder list?

Consistent with the contract-corporate law dichotomy, most scholars seem to agree that, since the 1950 amendment, contractual restrictions on transfer of shares can only bind the parties and do not affect the right of the transferee, whether he takes with notice of the restrictions or not. The non-transferring shareholder has a damage
claim against the transferor, but the proof of damages for a violative transfer of shares without a ready market would be difficult, especially since most of the damage would result from the risk to the enterprise introduced by a strange new shareholder, a practically immeasurable factor. Thus, the most effective remedy would be an injunction to prevent any transfers in breach of the agreement, but, again the chances of getting enough information and court action on the threshold of an illegal transfer are highly unlikely. If the situation permits, however, the law is encouraging. The courts can grant an injunction and order that a notice thereof be inserted in the registry of the company or, alternatively, the court may order that the shares be delivered to the bailiff for safekeeping. Note, however, that injunctions are limited to the parties to the action or the persons named therein. A case regarding a disputed telephone right held that if a violative transfer occurs, the company, which was not mentioned in the injunction, must register the right at the request of the transferee (even after an injunction against the transfer and even though the transfer occurred with notice). Being non-negotiable, the telephone right is hardly comparable to a corporate share, which is necessarily negotiable, and

70 The writer witnessed a similar problem in one joint venture when the U.S. firm was bought by another U.S. firm with less interest and concern for foreign operations.

71 Unreported v. Unreported, 29 HANREI TAIKEI (Compendium of decisions) 704 (Osaka Dist. Ct., Sept. 6, 1939). The court dismissed an attack under CODE OF CIVIL PROCEDURE art. 759 against an injunction ordering the petitioner not to transfer shares.

72 See KANEKO, KYOSEI SHIKKOH (Execution law) 294 (1951); and KIRUKAWA, HANREI HOZEN SHOBUN (Provisional disposition decisions) 200 (1959).

73 Shimomura v. Japan, 18 Minshu 761 (Great Ct. of Cassation, July 19, 1939), supported by scholarly comments in KIRUKAWA, op. cit. supra note 72, at 197, 200, and in Case No. 53 (Kurusu’s comment), in HANREI MINJIHO, SHOWA JUYONENDO (Judicial review of civil cases, 1939).

This restrictive use of the so-called doctrine of relative effect of injunctions is very important on the practice level, and it also leads to the conclusion that injunctions must be specific as to the parties. E.g., where X obtains an injunction prohibiting Y company from registering a transfer of shares from A to B, X still cannot prevent A’s transferring those shares to C, and Y company cannot refuse C’s request to register. At the same time an attempt to obtain an injunction against all third parties in general would not be supported, since it would injure some interested third parties then unknown, and violate the doctrine of relative effect. See also, Nomura v. Fuji Seitetsu, 10 Koto salsbansho minji hanreiho [hereafter cited Kosoai minshstu] 181 (Tokyo High Ct., April 19, 1957; Kaneko, Kabushiki ni taisuru kyosei shikko (Execution on shares), in 2 KABUSHIKI KAISHAHO KOSA (Lectures on corporation law) 765, 774 (1956).
so a transferee of a corporate share in violation of an injunction would unquestionably obtain good title.\textsuperscript{74}

In summary then, despite the clear language of \textit{Commercial Code} article 204(1) against restrictions on transfer, the weight of authority limits the effect of article 204(1) to the intra-corporate law sphere. The authorities, therefore, support the parallel validity and enforceability of contractual restrictions both for damages or a preventative injunction in the case of a shareholder-shareholder contract, howsoever impractical the latter might be in the usual case. Some authority, notably Ishii, would support reasonable, corporation-shareholder contracts as well. No remedy either against the corporation to cancel the registry or against the transferee to regain title is generally supported by the authorities except in the case where the transfer proceeded in violation of an active injunction. Matsuda\textsuperscript{75} would strike down such restrictive contractual clauses under article 204(1) and deny them enforcement of any sort, but no decision has been found following his interpretation.

It should be noted again, however, that despite the validity of and legalistic remedies for breach of share transfer restrictions, the fact is that usually a timely injunction to prevent a sale is impossible and if a violative sale occurs, the amount or even the fact of actual damages is often prohibitively difficult to prove. The parties are, therefore, well advised to include a reasonable liquidated damage clause in the joint venture agreement providing that if a wrongful sale is made, the seller will pay the other party a sum fixed in advance. The Japanese \textit{Civil Code} provides for such clauses and forbids the courts to vary the amount.\textsuperscript{76} This provision thus seems to prevent a court from refusing to enforce a liquidated damage clause because it is too high or a "penalty,"\textsuperscript{77} in our terms. Extreme amounts have been struck down, however, as violating public policy,\textsuperscript{78} but generally Japanese law has no

\begin{itemize}
\item \textsuperscript{74} Cf. \textit{Kikukawa}, \textit{op. cit. supra} note 72, at 200.
\item \textsuperscript{75} \textit{Matsuda, op. cit. supra} note 65, at 154-55.
\item \textsuperscript{76} \textit{Civil Code} art. 420:
  \begin{enumerate}
  \item The parties may determine in advance the amount of compensation for damages payable in the event of the non-performance of an obligation; in such case the Court cannot increase or reduce the amount.
  \item The determination in advance of the amount of compensation for damages shall not prejudice the obligee's right to demand performance or rescission.
  \item A penalty is presumed to be a determination in advance of the amount of compensation for damages.
  \end{enumerate}
\item \textsuperscript{77} \textit{Utano v. Gyokuzōbō}, 1 \textit{Minshū} 431 (Great Ct. of Cassation, July 26, 1922) (liquidated damages granted despite lessee-defendant's claim that the land had been leased again after the breach without any actual loss); \textit{Mitate v. Takabashi}, 13 \textit{Minroku} 36 (Great Ct. of Cassation, Feb. 2, 1907) (proof of actual loss not required).
\item \textsuperscript{78} \textit{Yamamura v. Kanzaki}, 23 \textit{Minshū} 147 (Great Ct. of Cassation, Nov. 14, 1944)
\end{itemize}
overriding concept of penalty. Rather, such clauses are upheld without superimposing the court's judgment as to the adequacy of the amount or even the existence of any damages, unless they are contra bonos mores. Since both parties may be equally interested in such a provision at the time of contracting, it may be feasible, in spite of the disenchantment usually occasioned by introducing such ideas into the final stages of negotiations.

Corporate Control Devices for Protection of Minority Interests: In the U.S. a variety of devices including preincorporation agreements between prospective shareholders are used to effect custom-made controls over close corporations—voting trusts, pooling agreements, irrevocable proxies, specific employment and management contracts, as well as diverse charter and by-law arrangements to insure veto power for the minority by requiring extraordinary quorums and votes of both the shareholders and the board or by shifting decision-making power between them to achieve a veto effect over specific critical corporate actions. The utility of one or combinations of these measures in the U.S. depends on the promoters' bargain, the nature of the business, the statutes of the state chosen for incorporation, and other factors.

In U.S.-Japanese joint ventures, the shareholders similarly desire to act as partners among themselves but as shareholders with limited liability toward the outside world. They want to be able to act informally by agreement, and in order to insure a position for itself in corporate policymaking the minority, in particular, must rely on such agreements to avoid coercive majority votes. It has been demonstrated that, as their corporate vehicle, they ordinarily choose the kabushiki kaisha, which is as ponderously over-equipped for close corporation purposes as our general corporation. Specific attention, therefore, must

(denied, as against CIVIL CODE art. 90, liquidated damages for delay of payment on a note, where the amount was excessive, even though the usury law might not apply to a commercial matter).

79 E.g., N.Y. Bus. Corp. Law § 715 (effective 1963) provides that shareholders may be allowed to elect officers. The new New York and the new North Carolina statutes are most responsive to close corporation needs; and the Florida Bar Association has a close corporation statute in draft.

be given to control problems in each venture, and each problem requires its own specific solution. The purpose here is only to indicate from the richer U.S. experiences which devices may be most useful in drafting joint venture contracts for Japan operations.

**Corporate Controls; Effect of FIL Approvals on the Contract:** It should again be noted that in Japan the character of this kind of corporate control problem is significantly conditioned by the shape of the venture imposed by the postwar Japanese governmental policy of excluding foreign majority equities in Japanese enterprises. Ordinarily, the parties also stipulate that FIL approval is a condition precedent to the effectiveness of the master joint venture contract. One of the strong, though seldom articulated reasons for the Japanese policy against foreign majorities, is doubtless to prevent foreign management control. So whatever the motivation or wisdom of the policy, it means that the American investors' problems are limited to protecting minority interests by veto provisions and the like. It also means that adroitly patterned, multi-class, share structures, which must appear in the documents to be submitted for approval and which aim at giving the foreign minority a control over major policies, would ordinarily not be any more acceptable to the Japanese foreign investment authorities than more forthright requests for approval of majority ownership. Since the official validation is apparently now a condition precedent to a foreigner's right to acquire shares in a Japanese corporation, however much this may conflict with the spirit of the U.S.-Japanese Friendship, Commerce, and Navigation Treaty (1953), it becomes important to decide just what parts of the total bargain need FIL approval. This can influence the choice between the two general methods of formalizing veto devices agreed between the joint venturers: (1) shareholder agreements; and (2) provision in pro forma articles of incorporation. Also, for the parties' ease of future reference certain kinds of obligations fit best in separate contracts; that is, those agreements which are intended to have subsisting effect between the parties even after incorporation.

There are three parts to this drafting and distribution question: first, what parts of the total arrangements does the FIL say must be submitted and approved, and second, in doubtful instances involving risks, what are the administrative law consequences of mistake and violation? The third and related question inquires into the contract law effects of a shareholder's agreement which should have been, but has not been

---

81 FIL (Gaishi ni kansuru hōritsu) arts. 10 and 11 (Law No. 163, 1950, as amended by Law No. 33, March 31, 1964, effective April 1, 1964).
validated. The answer to these first two questions would depend on specifics, but in general the FIL requires in these situations validation of share acquisitions (thus requiring submission of the proposed articles of incorporation) and inductions of technology only, leaving open the possibility that other side arrangements between the joint venturers as prospective shareholders need not be submitted, or might be submitted later. The law does not specifically forbid foreign control, and there may be some side agreements giving a veto with legal efficacy only as a contract between the parties which, depending upon the situation, would not need validation. If it is deemed necessary to make the veto binding in the corporate law, then it must be put into the articles and receive FIL approval. If approval is required and not obtained, penalties, including even imprisonment, may be incurred.

When approval is required by the administrative law, the third question relating to the effect between the parties of an unapproved contract has been of interest to foreigners throughout the period of tight Japanese foreign exchange controls, but it was only recently litigated. The cases examined have all held that such unapproved contracts are valid, but what sort of enforcement they might be entitled to in court is not as clear. The result on the point of validity is

---

82 Ibid.
83 See JUKAGAKU KÔGYÔ TSUGIHINSHA, GAIKOKU GIJUTSU DÔNYÔ YÔRAI (Guide to induction of foreign technology) 54-62 (1964) for details of application for approval under the FIL. FIL arts. 26 and 29 provide criminal penalties of up to three years' imprisonment and/or ¥300,000 fine for violation of the law. Note, however, that FIL approval is still not a prerequisite for the registration of a Japanese corporation by foreign promoters even after the FIL amendment (Law No. 33, March 31, 1964) requiring validation of all direct investments.
84 Lewin v. Greenberg, 11 Kakuryû minshû 2034 (Tokyo Dist. Ct., Sept. 30, 1960). Both parties in this suit for $10,000 were Americans. Defendant was a resident, and plaintiff was a non-resident. Thus, the transaction required a license under the Foreign Exchange and Foreign Trade Control Law (Gaikoku kawase oyobi gaikokoku bôeki kaoru) art. 27 (Law No. 228, 1949) [hereafter cited FECL]. Defendant asserted both (1) a lack of foreign exchange license and (2) duress as defenses. Judgment was for defendant, based on duress. But, in so deciding, the court also found that the lack of an FECL license did not invalidate the plaintiff's claim, reasoning that the FECL could not deprive the court of competence to handle suits between residents and non-residents. The holding has been properly criticized for reaching the right decision for wrong reasons. It would seem that the case has nothing to do with the court's competence; rather, the issue was whether the FECL restrictions invalidated an unapproved contract, and consistent with Japanese legal concept, the answer is that it would not, because the FECL is a regulatory law with its own purposes (and enforcement measures) going only to means of payment quite separate from the contract law, which creates private rights. For a critical comment on this case by Nishi, see Juristó (No. 241) 127 (1962). See also Nameoto, Gaikoku kawase oyobi gaikokoku bôeki kauri hoki to sono shôgai shi kôryoku ni tsuite (Concerning the laws and regulations for control of foreign exchange and foreign trade and their external effect), 54 KOKUSAISHÔ GAIKÔ ZASSHI ("The Journal of International Law and Diplomacy") (No. 4) 47, 79 (1955). Greenhill Trading Co. v. Shiro Trading Corp., 13 Kôsai minshû 696 (Tokyo High Ct., Oct. 29, 1960), recognizing an unapproved claim, conditioned on obtaining foreign exchange approval. The court's decision has
consistent with earlier scholarly theory and precedents of Japanese law which also compartmentalize the operative spheres of administrative (public) and contract (private) law, much as they do contract and corporate law as noted in the transfer restriction discussion above. The new FIL requirement, enacted in April, 1964, to the effect that certain contractual obligations themselves (not just payments) between Japanese and foreign investors must be approved could be enough more basic and restrictive in policy to justify finding the unapproved contract itself void, or at least unenforceable, to this writer's way of thinking. But it is doubtful whether the Japanese courts would find such a nexus between private and public law enforcement. Only future decisions will reveal the practical answer.

Corporate Controls; Shareholder Control Agreements: In this connection, there is another interstitial problem of Japanese contracts and corporation law similar to the one noted in the discussion of share transfer restrictions. In Japan, as elsewhere, the enforceability of shareholder agreements effecting corporate structure, procedures, and control are greatly affected by the basic theory underlying corporations in the legal system. For example, in English law the limited liability corporation evolved from partnership in turn based on contract and this approach still influences English statutes and decisions to allow the


1 WAGATSUMA, MINKU ZOGI (Lectures on the Civil Code) 225 (1963).

86 Tamaki v. Nakagawa, 25 Minshū 1715 (Great Ct. of Cassation, Sept. 25, 1919) (unlicensed plaintiff, who maintained a Rendezvous (machiai) for customers, was not precluded from collecting his fees).

87 Note that for public policy reasons in Iizuka v. Haritani, 26 Minroku 774 (Great Ct. of Cassation, May 28, 1920), the court denied promised support to a woman plaintiff from a man married to another woman as contra bonas mare, Civil Code art. 90, because plaintiff knew of defendant's married status. For treatise discussion of public policy considerations as stated in a statute which might invalidate violative contracts, see 1 WAGATSUMA, op. cit. supra note 85, at 223-26.

Quaere what kind of regulatory statutes, if any, in Japan would be deemed to establish a policy strong enough to void a conflicting contract? It seems that the Japanese concept of separate operative spheres for administrative and private contract law is basically different from the early position of our common law that contracts opposed to acts of Parliament were void. Of course with increased regulation of all activity, our law has long since receded from such an inflexible position and now often contracts are enforced though they may violate a pertinent regulatory statute, except where the statute expressly prohibits such a contract. E.g., Kaiser-Frazer Corp. v. Otis & Co., 195 F.2d 838 (2d Cir. 1952). See RESTATEMENT, CONTRACTS § 580 (1932); 6A CORBIN, CONTRACTS § 1374 (1962), and cases there cited. See Chapman v. Zakazaska, 273 Wis. 64, 76 N.W.2d 537 (1956), where the court reasoned, like the Japanese courts, that the regulation had its remedies and that accomplishing its purpose did not require voiding a contrary contract.

88 See text accompanying notes 62-65 supra.
incorporators to fix the corporate procedures and control features (i.e., voting and quorums) freely by contract. The English corporate law rules in this area are thus largely optional and for convenience if the parties do not wish to supersede them by special arrangement.  

On the other hand, in both Japan and the United States, the concept of corporation law is different in that the rules are to a degree at least mandatory and not subject to overriding contractual arrangements of the incorporators. In the United States, this theory stems from the early practice of granting corporate charters by special acts of the legislature giving rise to the so-called concession theory of incorporation. In the later general incorporation laws, it came to mean that the "corporate norms" embodied in the law were conceived as mandatory and designed mostly for publicly held corporations and to protect the public and shareholders. Japan, without such a history of special charter grants, nevertheless treats the corporate rules as mandatory unless the law otherwise provides. In addition, however, the systematic character of the code tends to support the theory that the corporate law requirements are only mandatory in the intra-corporate structure and as to corporate action as such.  

In consequence then, though the U.S. and Japanese law both tend to treat the corporate law control requirements as more generally imperative than the English contract theory, the Japanese law has little difficulty at the same time in holding that contrary contracts in their separate spheres are both valid and enforceable between the parties for damages at least.  

The U.S. cases show their usual variety of holdings, exacerbated especially in this instance by early failures to recognize in the legislation the obviously different needs of close and publicly held corporations. Some U.S. cases hold that the shareholders cannot vary the control mechanisms fixed by the corporate law, and if they try to do so, the by-law or contract will not be enforced. Others will enforce

---

89 See Gower, Some Contrasts Between British and American Corporation Law, 69 Harv. L. Rev. 1369, 1375-76 (1956).
90 17 (II) HANREI TAIKEI (Compendium of decisions) 190, where a provision in the articles to the effect that directors would be liable for the company's obligation was held by a Tokyo Appellate Chamber decision (Mar. 14, 1932) not to make directors liable directly to a corporate creditor.
91 Benintendi v. Kenton Hotel, Inc., 294 N.Y. 112, 60 N.E.2d 829 (1945); Sensabaugh v. Polson Plywood Co., 135 Mont. 562, 342 P.2d 1064 (1959). In these cases the courts declined to enforce admittedly invalid by-laws as contracts between the parties.
92 Compare, e.g., Jackson v. Hooper, 76 N.J. Eq. 592, 75 Atl. 568 (Ct. of Err. App. 1910), and Loverdos v. Vomvouras, 200 N.Y.S.2d 921, 923 (1960) (holding against survival of preincorporation joint venture agreements because they are inconsistent
shareholder contracts as such even though they may be invalid as by-laws.\textsuperscript{93} Overall, however, the needs of the close corporation in the United States seem to be leading to more enforcement of contracts which are contrary to the corporate law provisions. Similar separate and distinct treatment of corporate and contract law has been forthrightly recognized in Japanese law from the beginning, thus contrary contractual provisions are normally valid. Again, the only question is whether there are any useful remedies given the fact that the corporate law is adverse and no action is possible against the corporation in case of breach.\textsuperscript{94}

\textit{Corporate Controls; Provisions in the Articles:} Because of the inherent inadequacy of affirmative injunctions to enforce contracts entirely dependent upon cooperation in a close corporation, the desired veto devices for a foreign minority in Japan are probably best achieved in the articles of incorporation by adjusting quorum and voting ratios required for decision within the scope allowed by the code, coupled with cumulative voting in electing directors. At the outset, however, it should be noted that this technique will not insure a veto for a minority of one third or less because a two-thirds’ vote will amend the articles and this vote is not legally subject to variations in the articles.\textsuperscript{95} Also, it is necessary to provide for preemptive rights to new shares in the articles in order to enable the minority to maintain its shareholding ratio. Otherwise, the code authorizes the Board to decide upon a share issue, although if preemptive rights are allocated to outsiders, a two-
thirds' vote under *Commercial Code* article 343 is required [article 280-2(2)]. If preemptive rights are provided and the minority can block an amendment, then the articles can insure a veto power by extraordinary vote on most matters.

The reason for this approach, where the minority has more than one third, is that the irrevocable proxy, the voting trust, and share classes are ordinarily not practicable in Japan. The scholars are unanimous in the view that voting trusts and irrevocable proxies are not legal in Japanese corporate law. This conclusion flows from the requirement that shareholder proxies be limited in effect to a single meeting which rules out irrevocable proxies and has been interpreted to bar voting trusts also. Presumably they are, however, effective as contracts, subject to the weaknesses of affirmative remedies discussed above.

On the other hand, different classes of shares are possible in Japanese corporation law, including preferred shares (up to 25% of the total shares), which may be nonvoting so long as preferred dividends are not suspended. In practice, however, preferred shares in general are exceedingly rare in Japan (or any type of share except par value, non-bearer common), and preferred shares seem to carry implications of fiscal weakness. Besides, they are cumbersome for attaining no more

---

96 Note that the provision against irrevocable proxies [*Commercial Code* art. 239(4)] is not held to prevent appointment of a Permanent Representative (jonin dairin) in Japan to act for foreign shareholders. Both the corporate practice and the recent scholarly comment support the proposition that a foreign shareholders' Japan representative, duly appointed, can vote for the shareholder without special proxies at each meeting and can also appoint a sub-proxy. See 3 SUZUKI, *KABUSHIKI JITSUMU* (Practice relating to shares) 76-78 (1963).

97 As to the various aspects of the voting trust problem, see Ueda, *Giketsukken to sono dairi-kōshi* (Voting right and its proxy), in *ZOKU JITSUMU KABUSHIKI KAISHAHO ROKKŌ* (Six more essays on practical stock corporation law) 155, 164 (SHŌJI HÔMU KENKYUKAI ed. 1960); Kawamoto, *Kimeki kabuken to furikae kessai seido* (Non-bearer shares and the exchange system by way of pooling shares with a trustee), 13 *KÔBE HÔGAKU ZASSHI* ("Kobe Law Journal") 18, 72, 74 (1963); Sono, *supra* note 62, at 118.

98 *Commercial Code* art. 239(3) and (4):

3. A shareholder may exercise his vote by proxy. Such a proxy, however, shall file with the company a document establishing his power of representation.

4. The confinement of the power of representation mentioned in the preceding paragraph shall be made for each general meeting.


100 *Commercial Code* art. 242(1) and (2):

1. In cases where a company issues two or more classes of shares, it may be provided for by the articles of incorporation that with respect to shares of preferred class regarding the distribution of profits, a shareholder shall not be entitled to vote; however, such shareholder shall be entitled to vote from the time when the resolution to the effect that he shall not receive the preferred distribution provided for by the articles of incorporation has been adopted to the time when the resolution to the effect that he shall receive such distribution has been adopted.

2. The total number of the shares mentioned in the preceding paragraph shall not exceed one-fourth of the total number of the issued shares.
than veto power in an otherwise simple close corporate arrangement, and if they do more, they could complicate the official validation process.

In placing minority veto power in the articles of incorporation, draftsmen must pay careful attention to the code provisions. They specify certain items which must be in the articles (seitaiteki kisai jikō); others are made optional in various provisions of the code, but they must be placed in the articles if they are to be effective (sōtaiteki kisai jikō); and still other provisions may be freely inserted (ninentei kisai jikō) even though they are not treated in the codes so long as they do not violate the law or contradict the basic corporate concepts or public policy. 101

The details of corporation law and incorporation procedure are a separate subject, so only the code provisions defining the boundaries for draftsmanship will be indicated. The most basic provision is, of course, the amending power in Commercial Code article 343 requiring a two-thirds' vote, and as mentioned, this vote is not subject to modification in the articles. It is clear enough that minorities with less than a third cannot be given a veto power in the articles which is secure against amendments. Given the requisite one third of the voting shares, the code provisions relevant to a veto power over corporate policy are those which specify quorums, votes required for resolutions of the board or shareholders; those regarding election of directors and representative directors; those specifying the powers of the board or shareholder meetings; and those specifying the points which may be freely decided in the articles. Articles 239 and 260-2 require a simple majority of a quorum of half of the issued shareholdings for shareholders' and directors' resolutions respectively, but significantly, both articles authorize provisions for larger majorities and quorums in the articles of incorporation. Article 230-2 then allows the articles of incorporation to fix matters to be decided by the shareholders in addition to those specified in the code. There are doubtless some policy limits to these options, though it is difficult to define the degree of flexibility permitted. For example, some scholars say that shareholders may not be authorized to elect the representative director (ordinarily elected by the board), 102 and one decision has held that the articles may not give the president the power to determine the Retirement

101 SUZUKI, op. cit. supra note 96, at 4-8; and TANAKA, KAISHARÔ (Company law) 100 (1959).

102 TANAKA, YOSHINAGA & YAMAMURA, op. cit. supra note 56, at 573-74.
Allowance (taishokukin) of directors because this is a power reserved to the shareholders by Commercial Code article 269, unless retirement matters are fixed in the articles. Thus, delegation to the president in the articles was deemed inappropriate.  

Election of directors is by the shareholders and cumulative voting may be provided or prohibited (article 256-4) in the articles of incorporation, but even if it is prohibited in the articles, 25 percent or more of the shareholders may require it by simply filing a request therefor prior to any given meeting. If cumulative voting is not prohibited in the articles, any shareholder may demand it before an election (article 256-3). Of course, in U.S.-Japanese joint ventures, both preemptive rights to new shares and cumulative voting should be provided in the articles, though as a matter of practice this is seldom done by purely Japanese corporations. Arithmetic will show what number of directors must be correlated with the ratio of shareholdings to get the most out of a minority by cumulative voting.  

Agreements Between the Joint Venturers Committing the Joint Corporation to Future Specific Policies and Transactions: Most U.S.-Japanese joint venture contracts envisage future transactions between the new joint company and one or both of its parents. These transactions may be critical to the over-all bargain, as for example, transfers of property such as capital equipment, plant sites, patent licensing, supplies, agreements, or other arrangements such as sales agencies, employment of specific personnel, and the like. Drafting responsibility requires a lawyer to first decide whether such arrangements can, and if so should, be made binding on the embryo joint corporation or its promoters, or whether they should be provided only in an initial side agreement unvalidated by the FIL authorities and binding only between the joint venturers as future shareholders. To anticipate, ordinarily it seems that the shareholders' agreement is preferable, although legally
the new corporation and promoters can be bound by following prescribed procedures at the proper stage. The most important exception to such a formula is where the FIL requires approval. For example, all licensing agreements must be approved and in past practice a share acquisition would not gain validation without a licensing agreement inducting technology otherwise unavailable to Japan. So the licensing transaction would have to accompany the application for validation of the share acquisition, leaving only the question of whether the licenses (or transfers) of technology may be treated for FIL purposes as separate transfers to be entered into by the new corporation after validation and after corporate establishment by the Commercial Code article 246 adoption (see below). Or, must the licensing be treated as a concurrent transaction such as a Contribution-in-Kind (gembutsu shusski) under article 168(1)v or property to be taken over later under article 168(1)vi, both to be entered in the articles. Note that timing is also critical in these problems: (1) first, a joint venture contract (perhaps with several side agreements, separate, annexed, or incorporated by reference) is signed; (2) then seven persons (probably including one or both joint venturers) become promoters by signing the articles; (3) the constituent shareholders’ and directors’ meetings are held at which elections occur and evaluations of contributions are reviewed; (4) after that, registration is effected, at which time the new corporation comes into existence and can act on its own.

Generally, there are two ways to proceed in order to transfer the contemplated obligations arising from these transactions from mere plans of the joint venturers to commitments of the new corporation. The commitment to transfer property can either (1) be made by entering (a) the name of the transferor (subscriber, promoter, or third

---

106 Commercial Code art. 168(1)v and vi:

v. The full names of the persons whose contributions are in the form of property other than money, the property forming the subject-matter of such contributions, the value of such property, and a statement as to whether shares to be given therefor are those having par value or those without par value, together with their classes and their number;

vi. Property which has been stipulated to be taken over after the coming into existence of the company, its value and the full name of the transferor.

Note these items, amongst others, are known technically as Items of Abnormal Incorporation (hentai setsuritsu jikō). See generally Imai, Hentai setsuritsu jikō (Items of abnormal incorporation), in 2 Sōsō Hanrei Kenkyū Sōsho Seihō 94 (1961). Note that the requirement to list these in the articles brings with it the duty of passing a court inspection of the transaction before registration of the articles can be accomplished. Commercial Code art. 173(2) in case of Promoter Incorporation (hokki setsuritsu); arts. 181, 185(1) in case of Public Offering Incorporation (bosshū setsuritsu).
persons), (b) the property (anything which can be entered on the balance sheet), and (c) its value in the articles,\textsuperscript{107} before the constituent meeting,\textsuperscript{108} or (2) the transaction can be adopted by the new corporation after it is registered. However, if this latter course is followed, the contract must be recognized as a new one between the new corporation and the parent involved, meaning either can actually refuse to enter into the arrangement. In addition the new corporation can only enter into such a transaction\textsuperscript{109} by a two-thirds’ vote of the shareholders,\textsuperscript{110} and an attempt to adopt the old obligation, without contracting anew, will fail because the old contract is void for lack of entry in the articles.\textsuperscript{111} It is also useful to remember at this point that promoters are not competent to act for or to bind the embryo corporation in any matters looking to the Commencement of Business (kaigyo jumbi koi), as opposed to acts necessary to incorporation.\textsuperscript{112}

Of course, the thrust of these rules is to prevent evasion of the requirement of similar entries in the articles when a contribution of property (instead of cash) is to be made for the initial shares of the corporation,\textsuperscript{113} which contribution-in-kind must be delivered before

\textsuperscript{107} COMMERCIAL CODE art. 168(1) v and vi.
\textsuperscript{108} Unreported v. Unreported, 17 (II) HANREI TAIKEI (Compendium of decisions) (Great Ct. of Cassation, Dec. 24, 1932) (constituent meeting not empowered to accept a setoff of property of a subscriber in lieu of his obligation to pay cash for shares).  See ISHII, SHOHO (Commercial law) 188 (rev. ed. 1959).
\textsuperscript{109} COMMERCIAL CODE art. 246:
The provisions of Article 245 paragraph 1 shall apply mutatis mutandis in cases where, within two years after its coming into existence, a company makes an agreement to acquire, for value equivalent to not less than one-twentieth of the capital, property existing prior to its incorporation and intended to be continuously used for purposes of the business.
\textsuperscript{110} COMMERCIAL CODE art. 245(1):
A resolution as provided for in Article 343 is required for a company to effect the following acts:
(1) The transfer of the whole or of an important part of the business of the company;
(2) The making, alteration or rescission of a contract for leasing the whole of the business, for giving a mandate to manage such business, or for sharing with another person the entire profits and losses in relation to the business or of a similar contract;
(3) The taking over of the whole of the business of any other company.
\textsuperscript{111} WakO Seizo Kogyo K.K. v. Maruyama, 7 Minshii 1299 (Sup. Ct., Dec. 13, 1953), holding against new corporation attempting to defend (against seller’s claim of rescission) old promoter’s contract to buy land because corporation adopted the sale contract by two-thirds’ vote provided in COMMERCIAL CODE art. 246. The court held that a new sales contract could have been so adopted, but not the old one, which was void for failure to list it in the articles. TANAKA, YOSHINAGA & YAMAMURA, ZENTEI KOMMENTARU KAISHAHO (Completely revised commentary on company law) 332 (1964).
\textsuperscript{112} ISHII, op. cit. supra note 108, at 165; Fuji Kousoku Insatsu K.K. v. Tomita, 7 Kakyii minshii 125 (Tokyo Dist. Ct., Jan. 30, 1956); also, Unreported v. Unreported, 17 (II) HANREI TAIKEI 94 (Great Ct. of Cassation, Nov. 24, 1924).
\textsuperscript{113} COMMERCIAL CODE art. 168(1)v. Note that only promoters may contribute
the corporation can be registered and comes into legal existence. When either of these types of transfers is planned, the Commercial Code requires that they be listed in the articles and that a court appoint an inspector to investigate and report on the propriety of the evaluation and other aspects of the transaction. If improprieties are found, changes may be ordered by the constituent meeting or the court, depending on which of the two available incorporation procedures is being followed. All of these are, of course, to protect the subscribers and the public from depletion of assets by inside deals. The provision allowing post-incorporation transfers, so long as they were listed in the articles and inspected by the court, was enacted as late as 1938 after a decision that unlisted transfers were void.

A review of these rules is especially pertinent to a joint venture because the parties often want to transfer intangible industrial property or capital equipment to the new corporation and difficulties, real or imagined, of proving its value and delivery have motivated the parties to avoid the court inspections during incorporation where legally possible, even though they submit technology transfers for FIL approval. So, for corporate law purposes, instead of a direct single transaction whereby a contribution-in-kind of patents, know-how, etc., is transferred for shares, they arrange to pay cash for the shares (without mention of the property transfer contemplated later), and after incorporation the shareholder receives his money back in exchange for his patents, etc. This kind of prearrangement is entirely void against the joint corporation. Also, whether the technology is to be a contribution-in-kind or transferred after incorporation, it requires FIL approval, and can involve some of the most difficult tax problems as well.

Leaving these latter problems aside, such a result may not be so disadvantageous to suggest listing the transaction in the articles, because if the joint venturers are bound contractually to cause the new company to act in accordance with the plan, there should be little

---

property for shares, but this is a restriction on initial share issues at the time of establishment. Property instead of cash may be exchanged for shares in subsequent issues after incorporation by any one where agreeable to the directors, and no court inspection is required. Commercial Code art. 280-2(1). So the technique of a later share issue, if agreed in a side agreement, would avoid the court inspection procedures but not the FIL scrutiny, of course.

114 Commercial Code art. 185(1).
115 Commercial Code art. 173(2).
116 See note 106 supra.
117 Shirai v. K.K. Daiei Marugumi, 12 Minshū 2861, 2866 (Great Ct. of Cassation, Dec. 18, 1933).
difficulty in obtaining the new corporation's acceptance of a new contract to transfer the property by the two-thirds' vote required. Should the majority shareholder fail to carry through, surely the venture will fail anyway, and for salvage operations a claim against the other joint venturer for damages, especially if liquidated damages are specified, is as good as any remedy against the ineffectual new corporation. However, for maximum security the other party must be made to specifically undertake to cause the new corporation to do as stipulated or compensate the other party for the loss. In summary then, it seems that because of the formalisms of the kabushiki kaisha law, it is preferable in most of these matters (except licenses of technology which need FIL approval) to rely on side agreements between prospective shareholders for legal commitments of a specific nature such as transfers of property to the new corporation. Of course, for guarantees of corporate positions or employment contracts and the like, there is no alternative because they cannot be put into the articles legally.

Joint Venture Corporation's Third Party Beneficiary Rights: From the joint company's point of view, it could be important to know what right the new corporation has in Japanese law to accept and enforce the benefits conferred upon it by the side contract of the parents. Again, consistent with general Japanese theory, one might suppose that the contract should be enforceable despite the corporate law stricture since the Civil Code recognizes the right of a third party beneficiary, even though the third party may be a corporation not yet in existence at the time of contracting. But the right is only perfected when the beneficiary notifies the obligor of his acceptance of the benefit and obligation.

It has been demonstrated, however, that in one case the court

---

118 Civil Code art. 537:
1. Where a party to a contract has agreed therein to effect an act or performance in favor of a third person, such third person is entitled to demand such act of performance directly to the obligor.
2. In the case mentioned in the preceding paragraph, the right of the third person shall come into existence as from the time when he declares to the obligor his intention to accept the benefit of the contract.


120 See Nagase v. Matsuda, 20 Minroku 313 (Great Ct. of Cassation, April 22, 1914), holding that the contract is binding between the original parties, whether or not the third-party beneficiaries elect to accept the contract.

held that the contract for transfer of land, concluded between a promoter and the seller for benefit of an embryo corporation but not listed in the articles, was void and the third party new corporation could not, after incorporation, accept the benefits and enforce the contract against the seller even by compliance with Commercial Code article 246 (two-thirds' vote). Doubtless, the holding in this case is understandable as an example where, as in U.S. law, a contract is not enforceable when the state specifically forbids that the corporation be bound as a party by such contract itself without conforming to the prescribed procedures, which is apparently the effect of article 168(1)vi.123

There are, however, other types of obligations such as employment and advisory services which the joint venturers undertake for the new corporation as third-party beneficiary which cannot and need not be entered into the articles because they involve no property transfer. With respect to these arrangements, the joint corporation as a third-party beneficiary would have a right to accept the benefit, and duty if any, and could enforce the contract directly against the obligor parent.

**Frustration and Modification**

We have emphasized throughout that, whatever the legalities of the situation may be, a court cannot in fact affirmatively enforce the continued confidence and cooperation required for the success of a close corporate operation any more than it could in a marriage. These relationships depend for continuance of effective operations almost entirely on confidence born of mutual interest and understanding. In what then is essentially private law-enforcing as well as private law-making, legal obligations, if clearly understood by the parties to be such, may have functional preventive and deterrent value; or in case of failure of the enterprise, they may be legally useful in the litigious sense in salvaging some pieces. But, the law will rarely put together what the parties have put asunder, and the wise lawyer, like the wise bamboo, will bend with the wind and use his skills to induce initial mutuality and clarity of legal commitment—only theoretically enforce-

123 If on the facts it is to the advantage of the new corporation to accept the benefit of the contract, as was the situation in the Wako case (apparently the value of the land had gone up from 1944 to 1953 far beyond the contract price), then it seems the court should give effect to the overriding policy of upholding the bargain of the parties. In the Wako case there were, however, added considerations, e.g., the new corporation did not pay the price in time and seller had opted to rescind.
able—for whatever value of the sort mentioned above it may turn out to have.

But even though the original bargain seems clear enough, both between the parties and in law, there is the additional problem, particularly relevant to a minority position, of subsequent coerced modifications—a danger which a majority may be peculiarly able to exploit in a joint venture where the bullied minority knows full well that success is dependent on continued cooperation and that legal remedies to that end are ineffectual. An analogous situation in our law is the position of a contractor, in the middle, confronted with demands for a higher price by a subcontractor.

There are three Japanese factors—one, a matter of Japanese business practice, the other two, legal points which bear on the potential problem of coerced modification of U.S.-Japanese joint venture agreements and which a draftsman needs to bear in mind. First, we have noted that Japanese businessmen, unlike Americans, do not habitually use formal detailed contracts drafted with a view to enforcement by litigation in their domestic business relations; they traditionally have preferred flexibility in their hierarchical relationships to meet problems as they unfold and preferred social power and conciliation to resolve disputes. In their domestic society, uniquely organized both in degree and kind, that approach seems to work well enough. But an awkward foreigner can hardly "while in Japan do as the Japanese ethnocentrically and particularistically do," and a foreign minority position is thus untenable, unless the basic bargain is faithfully observed in accordance with the universalistic codes and unless the terms of the bargain are observed without unwarranted requests for changes or subsequent renegotiation.


125 See note 11 supra. Note that Europeans also are said to use formal contracts much less than Americans. Van Hecke, A Civilian Looks at the Common-Law Lawyer, in PARKER SCHOOL, INTERNATIONAL CONTRACTS 5 (Reese ed. 1962).

126 There are no careful behavioral studies, but there are occasional journalistic comments critical of Japanese attitudes toward contracts with foreigners. E.g., U.S. News and World Report, May 18, 1964, p. 104; Themes and Variations, Wall Street Journal, Feb. 3, 1964; and De Mente, JAPANESE MANNERS AND ETHICS IN BUSINESS (1960); and De Mente, How Business Is Done in Japan (1963). Comments in these latter books are sometimes extreme, but doubtless express the feeling and misunderstanding of some foreigners dealing with Japan, and they are cited here for evidence of those attitudes of foreigners.
Novation (kökai) is, of course, provided for in the Japanese Civil Code, and it presents no special legal problems here, requiring as it does the agreement of both parties. It is significant in this discussion of security for contractual commitments to a minority interest to note, however, that in Japanese law a later promise by one party to do more than the signed contract calls for, based for example on threats of nonperformance by the other and without any change in the other’s obligations, is binding even though the subsequent promise is oral and, in our usual conception, without consideration.

In avoiding erosion of the initial bargain, it is, therefore, important to know when a request for modification has some legal support; for example, what sort of changed circumstances will excuse nonperformance. Impossibility is, of course, recognized as an excuse for nonperformance, and, as a general rule, the risk of loss is on the obligor.

---

127 Civil Code arts. 513-18. Article 513 reads:

1. If the parties have entered into a contract in which the essential elements of the obligation are modified, such obligation shall be extinguished by novation.

2. The removal, addition, or alteration of conditions shall be deemed to be a modification of the essential elements of the obligation. The same shall apply where a bill of exchange is issued in lieu of the performance.

128 Ogoshi v. Tokyo Tatemono, 22 Minroku 1845 (Great Ct. of Cassation, Oct. 4, 1916) (no “consideration” but change in rent upheld); Unreported v. Unreported, Hōritsu shimbun (No. 2055) 17 (Tokyo Appellate Chamber, July 21, 1922); Unreported v. Unreported, 11 (II) HANREI TAIKEI (Compendium of decisions) 1137, HANPE TIMES (No. 30) 34 (1953) (Sup. Ct., March 20, 1953) (no “consideration” but change of price for immovables upheld); see cases cited in 13 (III) HANREI TAIKEI 312. Note the interesting emphasis of the foregoing cases on novation. The discussion centers around the problem of whether a subsequent promise to pay more without any change in the other’s performance was a change in the “essential elements” of the obligation in each case which would extinguish the prior contract by novation (per art. 513; see note 127 supra). At common law such a subsequent “novation” would doubtless fail for lack of consideration, leaving the original contract the same. See Ames, Two Theories of Consideration, 12 HARV. L. REV. 515, 521 (1899). But in the Ogoshi case, supra, where a surety was defending by arguing that a novation took place without his consent, thus superseding all the old contracts, the court held that the price change was not a change of an “essential element” required for novation which would extinguish the prior contract; so the court held the surety liable on the subsisting old contract.

For the German and French approach see, von Mehren, Civil Law Analogies to Consideration: An Exercise in Comparative Analysis, 72 HARV. L. REV. 1009 (1959); Keyes, Cause and Consideration in California—A Reappraisal, 47 CALIF. L. REV. 74 (1959); and Smith, A Refresher Course in Cause, 12 LA. L. REV. 2 (1951).

129 For discussion of various aspects of the problem, see Corbin, supra note 123, and Note, supra note 124; cf. Note, 2 HOUSTON L. REV. 132 (1964).

130 Civil Code art. 536:

1. Except in the cases mentioned in the preceding two Articles, if the performance of an obligation becomes impossible by any cause for which neither of the parties is responsible, the obligor is not entitled to counter-performance.

2. If performance becomes impossible by any cause for which the obligee is responsible, the obligor shall not lose his right to demand counter-performance; however, if he has received any benefit through being relieved of his own obligation, he shall return such benefit to the obligee.

The text alone is confusing on the point because it only provides that the obligor is not entitled to counter-performance without saying he is excused from performance
with the exception of sales of identified specific goods where the risk is shifted to the purchaser even before payment and delivery.131

The Doctrine on Change of Circumstance (jijō henkō no gensoku) is more closely related to our inquiry here.132 As exemplified in the Japanese precedents, it is a far different thing from a flexible contract to allow adjustments for inconvenient contingencies. In a leading case, Iguchi v. Ikegami, the Supreme Court while refusing to recognize a defense of changed circumstances laid down four criteria which seem to be generally accepted law:133

1. Substantial change of circumstances must have occurred since the contract was formed.
2. The changes must have been unforeseeable.
3. The change must have been caused by forces for which neither party was responsible.
4. And, thus, to enforce the contract would violate the Principle of Faith and Trust (shingi seijitsu no gensoku).

The code basis for this doctrine is Civil Code article 1(2)134 requiring that rights be exercised faithfully and in accordance with the principles of trust. The weight of scholarly opinion says that an objective, unforeseeable change for which the parties were not responsible must be found first; then the situation is examined to see whether the parties' own positions and actions warrant excuse of performance under article

131 Civil Code arts. 534-36. See criticism of article 534 in 5(1) Wagatsuma, op. cit. supra note 130, at 85, 102 (1962); for a practical discussion of this problem, see Bōeki to hōritsu (Trade and law) 352-79 (8 Bōeki jitsumu kōza (Lectures on trade practice) ed. (1962).


134 Civil Code art. 1(2): "The exercise of rights and performance of duties shall be done in faith and in accordance with the principles of trust."
The cases have been very strict in the postwar period, and it is safe to assume that argument for a change in contractual terms on this basis will have to be supported by real hardship without fault and caused by extreme and unforeseeable changes of circumstance after the contract was made.

In summary, Japanese substantive law as administered by the courts furnishes ample security against claims for modifications merely convenient for one side. Also, for a Japanese operation, the draftsman does not need an elaborately tailored force majeure clause, at least from the minority point of view. Nonetheless, Japanese parties occasionally wish to insert a clause to the effect that in case of changed conditions or disagreement, the parties will discuss the matter and reach an amicable agreement. In this innocuous sounding suggestion is often planted the seeds of traditional flexibility which may come to be understood as a right to change. In the interest of security of the commitments, it is advisable to discuss these matters thoroughly and to leave such clauses out, especially since legally the parties can always agree to a partially or wholly new arrangement.

CONCLUSION

Experienced international practitioners will know that the role of law and the efficacy of courts vary from place to place, and that, consequently perhaps, businessmen choose to give formal contracts a role which varies with the country. Compared to us, Japanese rely little on formal contracts domestically, and they rely even less on litigation. This point of behavior regarding the uses of contract law and the role of law generally needs to be understood, even though increased international business contacts are focussing more attention on their positive law.

Additionally, it is common sense that the legal meaning of a U.S.-Japanese contract in the Holmesian sense (the law is what the court says it is) cannot be understood prospectively unless we know from which law it derives its meaning. And we cannot, in fact, determine which law would govern in litigation for sure, until we know where a suit will be brought, which in turn is indeterminable so long as the
parties can sue in more than one country—and they can—considering both of them separately as potential plaintiffs. When our federalistic complex is introduced into any bilateral problem with some states showing little or no respect for foreign judgments, prorogation, and choice-of-law clauses, the single law standard for understanding the legal meaning of a contract as an enforceable instrument, prospectively, is largely illusory at the only point where the law can add anything more to the security of the transaction than the parties’ good faith—namely in a lawsuit.

In U.S.-Japanese joint ventures nearly all American firms have a minority position because of Japanese official policy against foreign majority equities in Japanese enterprises. This fact molds the constitutive contracts in a fairly fixed pattern, and by all odds the most important problem is to protect the minority interest within the limits possible under the Japanese contract, administrative, and corporation laws. We find that it is possible to restrict the transfer of shares by contract valid between the parties, but that no enforcement is possible against the corporation or third parties and although specific performance is available in the law, it is in fact unlikely to be useful against the other party. Damage claims are similarly ineffectual unless liquidated damages are included in the contract; if they are, they will be upheld unless they are so excessive as to be contra bonos mores, which is a standard apparently much more permissive than our penalty.

A minority veto power over certain critical transactions is given in the Commercial Code itself to the shareholder with more than one third of the votes, and the veto can be extended legally in the articles to other transactions. Higher votes can be provided in the articles, but ultimately small minorities cannot be so protected because the articles can be amended by a two-thirds’ vote and this required vote cannot be made larger by the parties in the articles. To protect a veto power, it is necessary to provide for preemptive rights for the existent shareholder in the articles. The veto power can be extended to the board by properly calculating the number of directors and providing for cumulative voting in the articles plus adequate extraordinary board votes in the articles; even more than two-thirds could apparently be required.

Prospective commitments for later property transfers between the parents and the joint corporation can be made effective against the new corporation only by including them in the articles and by getting a
court inspector's approval at the time of incorporation. Often it would be reasonably safe and much simpler to bind the other joint venturer, on the risk of otherwise paying liquidated damages, to cause the new corporation to enter a new contract and to approve the transfer by a two-thirds' shareholder vote required for certain transfers within two years after incorporation. Where transactions other than property transfers are contemplated for the future company, they can only be fixed as legal obligation between the joint venturers, but the Japanese law provides benefits for the third party new corporation.

The conclusion which comes through more clearly is that without good faith cooperation, no affirmative legal remedy is adequate to make a joint venture work. Nevertheless, a well-planned legal structure set up and operating will make the bargain understandable, operable, and then, given the modicum of initial good faith, sustainable. Careful legal planning will also help salvage something from a stalemate. Liquidated damage clauses are as useful in a breakdown as they are difficult to negotiate.