

*A New Class Action System in Japan
(New Act Enacted and Promulgated in December 2013)*

I. Introduction

In recent years, the Japanese government has been developing a series of legislation with the aim of facilitating the protection of consumers. In 2001, the Consumer Contract Act (Act No. 61 of 2000) came into effect. This Act introduced substantive laws for consumer protection, such as the invalidation of provisions in a contract concluded between a consumer and a business operator (“**Consumer Contract**”) which are significantly detrimental to the consumer. In 2007, an amendment to the Consumer Contract Act came into effect introducing “Consumer Organization Proceedings”. These proceedings allowed “Qualified Consumer Organizations” (“**QCOs**”) to seek injunctions for the benefit of relevant consumers against business operators, so as to prevent business operators from performing certain unfair acts, such as soliciting the execution of a Consumer Contract which contains unfair provisions. However, under the Japanese laws currently in force, there is no special procedure under which a group of consumers can recover damages collectively. In other words, as a general principle, consumers who seek to recover damages caused by the actions of a business operator are required to file individual lawsuits on their own behalf.

As a further attempt to promote consumer protection, the Japanese government has been working on legislation to introduce a new Japanese Class Action System (“**New System**”). This New System proposes to enable consumers to recover damages collectively in a simple and prompt manner. On 4 December 2013, the bill for the New System was finally enacted (the Act on Special Provisions of Civil Court Procedures for Collective Recovery of Property Damage of Consumers (Act No. 96 of 2013) (“**New Act**”). The New Act was promulgated on 11 December 2013, and will take effect within three (3) years from the date of promulgation and on a date which will be separately designated by a cabinet order. It should be noted that the New System will not apply, in principle, to claims in connection with Consumer Contracts concluded before the New Act takes effect.

The New System is being developed solely for the purpose of protecting consumers in relation to Consumer Contracts. At the same time, to avoid putting an excessive burden on business operators, the New System limits the entities which may bring claims and the claims which may be brought, as well as kinds of damages that may be recovered through the New System. Due to these limitations, the New System is considerably different from the US class action system.

This legal update summarizes the New System based on the New Act.

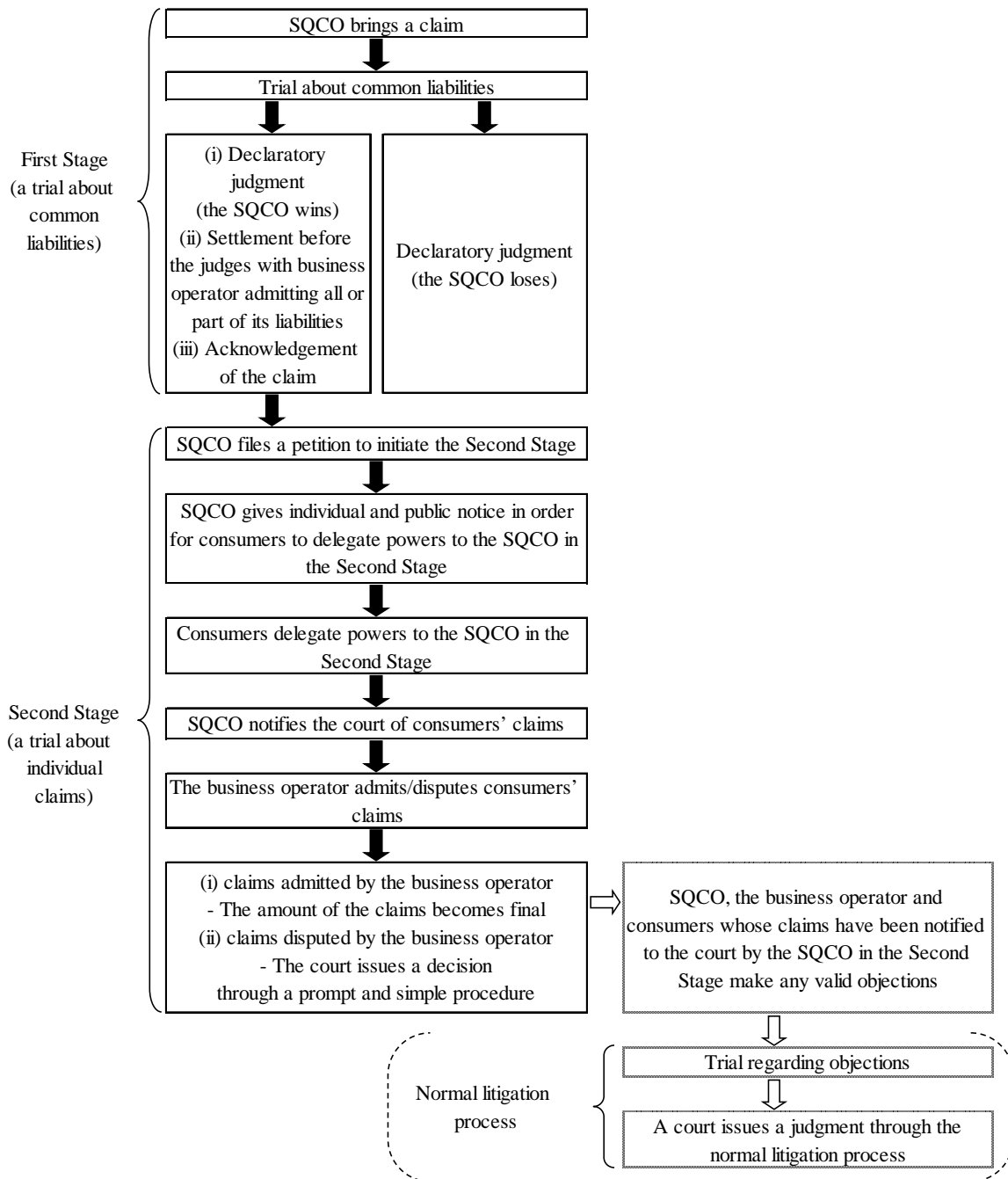
II. Outline of the New System

1. The overall structure of the New System

The New System consists of two stages. The first stage countenances a procedure which has as its end result the issuance of declarations on common liabilities, being the liabilities of a business operator to a considerable number of aggrieved consumers which arise from a common legal and factual cause (“**Common Liabilities**”) (“**First Stage**”). Common Liabilities include, for example, the obligation of a business operator to return monies which were paid by the consumers in relation to fraudulent Consumer Contracts. This First Stage procedure can only be filed by a “Specified Qualified Consumer Organization” (“**SQCO**”) and may only be filed against business operators as defendants.

If the SQCO, acting for the benefit of a considerable number of aggrieved consumers, succeeds at the First Stage, the amount to be paid to each aggrieved consumer will be determined at the second stage (“**Second Stage**”). If, on the other hand, the business operator succeeds at the First Stage, the Second Stage will not commence but the decision of the First Stage will not be binding on consumers. This allows consumers to bring individual claims against a business operator even where the relevant SQCO fails at the First Stage.

The Second Stage is initiated by a petition filed by the SQCO. Once the Second Stage has commenced, the SQCO will give individual and public notice to aggrieved consumers in order for them to delegate powers to the SQCO in the Second Stage. At the Second Stage, the amount that each aggrieved consumer is entitled to recover will be determined.



2. SQCOs

Under the New System, a claim can only be brought by an SQCO. As of January 1, 2014, there are eleven QCOs certified by the Prime Minister under the Consumer Contract Act. Among these eleven QCOs (and certain other designated entities which will shortly acquire QCO status), only those certified by the Prime Minister as fulfilling the requirements of the New System will become SQCOs. Under the New System, an SQCO will be entitled to receive certain compensation and expenses from consumers under certain conditions as required by law.

3. Claims which can be brought under the New System

Claims brought under the New System shall be claims which arise in conjunction with Consumer Contracts and must fall within the scope of one of the following:

- i. a claim for the performance of a Consumer Contract (e.g., a claim for payment of sales proceeds based on a sales agreement where the consumer is the seller and the business operator refuses the payment based on an unfair provision);
- ii. a claim for the return of unjust enrichment resulting from the cancellation, non-existence or invalidity of a Consumer Contract (e.g., a claim for the return of a payment made under a Consumer Contract which is related to a fraudulent business and is invalid due to a violation of the public policy of Japan);
- iii. a claim for compensation of damage based on the default of a Consumer Contract (e.g., a claim against a warehouseman where stored consumers' goods have been spoiled due to the warehouseman's breach of duty of due care of a prudent manager) ;
- iv. a claim for compensation based on liability for a product defect under a Consumer Contract (e.g., a claim against a seller for compensation of damage arising from defective products); or
- v. a claim for compensation of damage resulting from a tort committed in conjunction with the conclusion or performance of a Consumer Contract (e.g., a claim for compensation of damage incurred due to unlawful solicitation through the use of a uniform brochure).

In addition, the claims which can be brought under the New System are limited to monetary claims against a business operator. Furthermore, with respect to items (iii) through (v) above, damage relating to the subject matter of a Consumer Contract may be compensated, but not secondary loss, lost earnings, damages for personal injury/death or damages for pain and suffering.

The questions as to what specific claims can be brought under the New System have been clarified, to a certain extent, in the Answers to Public Comments issued by the Consumer Affairs Agency of Japan. Several of these answers are as listed below:

- Claims based on a leak of personal information will be excluded, at least so far as the consumers seek compensation for pain and suffering (i.e., no specific damage relating to property);
- In principle, claims based on false statements in an annual securities report cannot be brought under the New System because, in the context of continuous disclosure (as opposed to disclosure at the time of offering), there is generally no Consumer Contract between consumers and the filer of an annual securities report; and
- Claims arising from defective products will be subject to the New System. However, because the New System excludes compensation for secondary loss, lost earnings, damages for personal injury/death and damages for pain and suffering, compensation from business operators under the New System will generally be limited to the amount that was received for the defective products.

Please note that these Answers do not have any binding effect on the court, but can have influence on the SQCOs which have been certified by, and been under the supervision of, the Prime Minister.

4. The First Stage: A lawsuit for a declaration on Common Liabilities

To initiate the First Stage, the claim which is brought must be related to a Consumer Contract as described in II-3 above. Furthermore, the following requirements must be met:

- i. A considerable number of consumers affected by the conduct of the business operator must exist. According to the Consumer Affairs Agency, dozens of people would suffice to meet this “considerable number of consumers” requirement.
- ii. The liabilities of the business operators must arise from a common legal and factual cause.
- iii. In the event that a prompt and adequate decision at the Second Stage appears to be difficult, the court has the discretion to dismiss the case.

In the First Stage, the court will render a declaratory judgment on the Common Liabilities. If the court grants all or part of the claim, then the case will progress into the Second Stage. On the other hand, if the court dismisses the claim entirely, then the case will stop without going into the Second Stage.

The defendants under the New System are, in principle, limited to business operators who are alleged to have concluded the Consumer Contracts in question. As to tort claims (i.e., (v) in II-3 above), business operators other than those concluding the Consumer Contracts,

such as (1) those who perform such Consumer Contracts or (2) those who solicit or facilitate (either by themselves or through third parties) the conclusion of such Consumer Contracts may also become defendants.

It should be noted that the SQCOs are authorized to reach a settlement before the judges with the defendant business operators at the First Stage. In case a defendant business operator admits all or part of its liabilities in the settlement, the SQCOs can (and, in principle, must) proceed to the Second Stage.

5. The Second Stage: The procedure to determine the individual claims of each of the aggrieved consumers

At the Second Stage the court, through a prompt and simple procedure, issues a decision regarding the amount or existence of the relevant claim brought on behalf of a considerable number of consumers. The Second Stage commences upon the lodgment of the petition of the SQCO that was the victorious plaintiff in the First Stage. After the Second Stage is commenced, the relevant SQCO will give individual notices to aggrieved consumers, urging the consumers to delegate their powers to the SQCO in the Second Stage. The SQCO will also give public notice through various media such as the internet. The SQCO can also request that the business operator: (i) give a public notice (for example, via the website of the business operator); and (ii) provide the SQCO with documents that contain names and addresses or contact information of aggrieved consumers so that the SQCO may give individual notices to individual consumers. If the business operator does not meet request (ii) without any justifiable reason, the court can, upon a petition by the SQCO, order the business operator to do so. A breach of this court order without justifiable grounds is subject to a non-penal fine of not more than 300,000 yen.

Once consumers delegate powers to the SQCO in the Second Stage, the SQCO will notify the court of these consumers' claims. If the business operator admits those consumers' claims, the amount of the consumers' claim becomes final. If the business operator disputes the amount or existence of any or all of the consumers' claims as contained in the SQCO's notice, the court will issue a decision relating to the amount or existence of the various consumers' claims.

In respect of the court decision, the SQCO, the business operator and consumers who have delegated powers to the SQCO in the Second Stage can object. If there is no objection, the decision of the court becomes final. If any of the three parties files a valid objection, the amount or existence of the claim will then fall to be determined through the normal litigation process, which in all probability will take longer than the processes used in the Second Stage of the New System.

6. Advantages and disadvantages of the New System for relevant entities

Under the New System, each of the aggrieved consumers can decide whether to delegate powers to the SQCO in the Second Stage after the SQCO has triumphed at the First Stage (including cases where the settlement before the judges has been reached and where the defendant business operator has admitted the claim). Therefore, consumers can dispense with the cost required for the First Stage and expect low-risk and prompt recovery in the Second Stage. However, at the same time, the claims which can be brought under the New System are limited and therefore consumers may not be able to claim certain losses, such as losses arising from secondary loss, lost earnings, damages for personal injury/death or damages for pain and suffering (as noted in II-3 above).

As to business operators, the New System might be beneficial for the prompt resolution of disputes with multiple consumers on a collective basis. Although a decision which is adverse to an SQCO will not bar other claims from consumers, from a practical viewpoint, it may discourage consumers from bringing claims and also be influential when courts are required to decide other claims made by consumers. The disadvantage for business operators is that the New System, with its streamlined, convenient procedures, may increase the risk of claims from the SQCOs/consumers.

Under the New System, an SQCO will be entitled to receive certain compensation and expenses from consumers who delegate powers in the Second Stage under certain conditions as required by law. This may motivate SQCOs to bring lawsuits under the New System more readily. QCOs and other entities may also be incentivized by this to acquire SQCO status.

III. Expected impact on practice

Under the New Act, only SQCOs may bring claims based on the New System. Furthermore, the claims which can be brought under the New System are claims related to Consumer Contracts and are subject to other requirements. Considering this, from a practical viewpoint, the scope of the New System is much more limited than the class action system in the US.

Be that as it may, the New System will certainly increase the risk of litigation for business operators. Furthermore, after the New System takes effect, there is a possibility that a Japanese court or legislators may try to extend the scope of the New System if it proves to be effective for protecting consumers. For a business operator dealing with consumers, it would be advisable to thoroughly examine the risks that may arise from the New System.

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